

LEVINE, BLASZAK, BLOCK & BOOTHBY, LLP

2001 L STREET, NW
SUITE 900
WASHINGTON, D.C. 20036
(202) 857-2550
FAX (202) 223-0833

October 29, 1999

VIA ELECTRONIC COMMENT FILING SYSTEM

Ms. Magalie Roman Salas
Office of the Secretary
Federal Communications Commission
Room TW-A324
445 Twelfth Street, SW
Washington, D.C. 20554

Re: Access Charge Reform, CC Docket 96-262; Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1; Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers, CCB/CPD File No. 98-63; Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA, CC Docket No. 98-157

Dear Ms. Salas:

Pursuant to the Fifth Report and Order and Further Notice of Proposed Rulemaking in the above-captioned matter, enclosed please find an electronic original of the Comments of the Ad Hoc Telecommunications Users Committee. These Comments are being filed via the Federal Communications Commission's Electronic Comment Filing System ("ECFS").

If you have any questions regarding this filing, please do not hesitate to call me at (202) 857-2560.

Sincerely



Betsy Eisen

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)	
)	
Access Charge Reform)	CC Docket No. 96-262
)	
Price Cap Performance Review for Local Exchange Carriers)	CC Docket No. 94-1
)	
Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers)	CCB/CPD File No. 98-63
)	
Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA)	CC Docket No. 98-157
)	

COMMENTS OF THE
AD HOC TELECOMMUNICATIONS USERS COMMITTEE

Patricia D. Kravtin
Scott C. Lundquist
Economics and Technology, Inc.
One Washington Mall
Boston, MA 02108-2617
617-227-0900

Colleen Boothby
Levine, Blaszak, Block & Boothby, LLP
2001 L Street, NW
Suite 900
Washington, DC 20036
(202) 857-2550

Economic Consultants

Counsel for
Ad Hoc Telecommunications
Users Committee

October 29, 1999

SUMMARY

The *NPRM* proposes a number of revisions to the price cap indices (PCIs) for the common line, traffic-sensitive, and trunking baskets, and to the rate structure for local switching and tandem-switched transport elements. These revisions seek to correct economic inefficiencies and fundamental imbalances inherent in the Commission's price cap regulation of the LECs, due primarily to the fact that the LECs' costs are non-traffic sensitive, whereas the rates the LECs charge customers are largely usage-based and applied in an environment of high usage growth.

Ad Hoc has consistently supported principles of cost causation and the resulting economic efficiency gains that result from adherence to those principles. Accordingly, and for the reasons elaborated in these Comments, Ad Hoc strongly supports the proposed revisions as long overdue in the context of insuring effective ongoing regulation of price cap LECs.

The specific revisions to the price cap indices proposed by the Commission involve a move from "half g" to "full g" in the common line basket PCI formula, and the introduction of an analogous "q" factor to the PCIs applicable to the traffic-sensitive and trunking baskets. The use of a full "g" bestows the benefits of usage growth entirely to the IXCs and their end user customers. It is widely acknowledged – indeed, the Commission itself made this finding almost five years ago – that the IXCs, along with general trends outside the control of price cap LECs, have been responsible for the growth in interstate usage demand. Accordingly, the move to a full "g" is long overdue, as is the implementation of similar growth-related factors to the PCI formulation applied to switching and

trunking baskets. Adoption of these changes, along with one-time adjustments reflecting a restatement of the PCIs down to the levels that would have resulted had the Commission incorporated the proposed “g” or “q” factors at the inception of price caps regulation in 1991, is necessary to produce efficient going-forward price cap regulation.

The Commission’s proposal to devise capacity-based charges for local switching creates a better match between the underlying cost characteristics of the network plant involved and the switched access rate structure. Given the basic uniformity of local switching facilities across all ILECs, the Commission should take the lead in prescribing an optimum local switching rate structure. For similar reasons, the Commission should also pursue the development of capacity-based charges for tandem switching. However, the application of full “g” and “q” factors as recommended in these Comments will reduce the ILECs’ incentives to shift revenue recovery from their flat-rate to their per-minute charges, so that revisions to the basket structure may not be necessary to deter such shifts. Finally, concerns regarding the impact of cost-causative, capacity-based charges on smaller IXCs appear unwarranted in light of industry data which indicates that smaller IXCs are thriving in the wake of similar access rate structure modifications adopted previously.

Table of Contents

	<u>Page</u>
SUMMARY	i
INTRODUCTION.....	1
DICUSSION	3
I. THE “G” FACTOR IN THE COMMON LINE PCI FORMULA SHOULD BE INCREASED TO A FULL “G” SINCE THE IXCS, AND TRANDS OUTSIDE THE LECS CONTROL, ARE RESPONSIBLE FOR GROWTH IN USAGE.....	3
II. THE COMMISSION CORRECTLY RECOGNIZES THE NEED TO IMPLEMENT A “Q” FACTOR IN THE PCI FOR THE TRAFFIC SENSITIVE AND TRUNKING BASKETS.....	6
III. THE COMMISSION SHOULD REQUIRE ONE-TIME PCI ADJUSTMENTS TO REFLECT, ON A GOING-FORWARD BASIS, CHANGES TO THE “G” FACTOR AND INTRODUCTION OF A “Q” FACTOR.....	8
IV. A CAPACITY-BASED CHARGE FOR LOCAL SWITCHING WOULD INCREASE THE ECONOMIC EFFICIENCYOF THE SWITCHED ACCESS RATE STRUCTURE.....	9
V. THE COMMISSION SHOULD FURTHER EXPLORE THE POTENTIAL FOR CAPACITY-BASED CHARGES FOR TANDEM SWITCHING	14
CONCLUSION.....	15

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of)	
)	
Access Charge Reform)	CC Docket No. 96-262
)	
Price Cap Performance Review for Local Exchange Carriers)	CC Docket No. 94-1
)	
Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers)	CCB/CPD File No. 98-63
)	
Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA)	CC Docket No. 98-157
)	

COMMENTS OF THE
AD HOC TELECOMMUNICATIONS USERS COMMITTEE

The Ad Hoc Telecommunications Users Committee ("Ad Hoc" or the "Ad Hoc Committee") submits these Comments on the Commission's Fifth Report and Order and Further Notice of Proposed Rulemaking in the above-captioned proceeding, FCC 99-206 (released August 27, 1999) ("*NPRM*")¹.

INTRODUCTION

The members of the Ad Hoc Committee are some of the nation's largest corporate users of telecommunications services, collectively spending hundreds of millions of dollars annually on telecommunications services. The Ad Hoc Committee's members collectively

¹ *Access Charge Reform* (CC Docket No. 96-262), *Price Cap Performance Review for Local Exchange Carriers* (CC Docket No. 94-1), *Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers* (CCB/CPD File No. 98-63), *Petition of US Wets Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA* (CC Docket No. 98-157), Fifth Report and Order and Further Notice of Proposed Rulemaking, FCC 96-206, rel. Aug. 27, 1999 ("*NPRM*").

employ over a million workers. As large, institutional users of telecommunications services, the members of Ad Hoc share compelling interests in the outcome of this proceeding. In particular, the Commission has proposed a number of possible revisions to the price cap formula which, if adopted, could significantly lower the indices for price cap baskets. These revisions seek to correct, on a going-forward basis, for the imbalance between ILECs and customers of the ILECs' access services that has existed for years as a consequence of the formula's failure to properly reflect two fundamental attributes of these services, and the interrelation between the two. These attributes are: (1) the substantial growth rate in interstate minutes of use since the inception of price caps regulation, and (2) the increasingly non-traffic sensitive nature of the ILECs' access costs. For the reasons detailed below, Ad Hoc strongly supports the proposed revisions to ensure effective, ongoing regulation of the price cap LECs.

In addition, the Commission proposes a number of rate structure changes to reflect the non-traffic sensitive nature of access costs, specifically for the local switching and tandem-switched transport rate elements. Ad Hoc supports the Commission's proposals in this area as important steps towards achieving increased economic efficiency in access markets.

The Commission's proposals in the NPRM would affect many of the rate structures and regulations that are also addressed by the Coalition for Affordable Local and Long Distance Services ("CALLS") in a proposal which was submitted to the Commission on July 29, 1999, and is the subject of a Notice of Proposed Rulemaking in both CC Docket Nos. 96-262 and 94-1.² Because the CALLS proposal would be an alternative to the

² *Access Charge Reform* (CC Docket No. 96-262), *Price Cap Performance Review for Local Exchange Carriers* (CC Docket No. 94-1), *Low-Volume Long Distance Users* (CC Docket No. 99-49),

current price caps and access rules, Ad Hoc anticipates that it will support aspects of the CALLS proposal which may be inconsistent with the rule changes proposed by the Commission in this phase of those rulemakings and supported by Ad Hoc in the comments which follow.

DISCUSSION

I. THE “G” FACTOR IN THE COMMON LINE PCI FORMULA SHOULD BE INCREASED TO A FULL “G” SINCE THE IXCS, AND TRENDS OUTSIDE THE LECS’ CONTROL, ARE RESPONSIBLE FOR GROWTH IN USAGE.

The FCC has invited comment on “whether the g factor in the common line PCI formula should be increased, and if so, whether it should be increased to a full ‘g.’”³ The use of a full “g” is consistent with a policy that bestows on the IXCs the benefits of demand growth attributable entirely to the IXCs. As discussed below, the IXCs – and not the price cap LECs – have been responsible for the growth in interstate usage demand.

A policy that bestows the benefits of demand growth entirely to the IXCs is indeed the correct one, from both an economic efficiency standpoint and a fairness perspective. In terms of economic efficiency, the incentive structure should unambiguously reward the IXCs for their efforts to stimulate demand for interstate minutes, not the price cap LECs for their continuing market power in the access market. From a fairness perspective, the IXCs and their end user customers, rather than LEC shareholders, should benefit monetarily from the IXCs’ efforts, and other factors outside the LECs’ control, that have served to increase end user demand.

Federal-State Joint Board on Universal Service (CC Docket No. 96-45), Notice of Proposed Rulemaking, FCC No. 99-235, rel. Sept. 15, 1999.

³ *NPRM* at ¶ 227.

The g/2 factor was originally adopted by the Commission in its 1990 LEC Price Cap Order (Docket 87-313) based on a finding that LECs exert some influence over common line usage growth and therefore that it was reasonable to share the benefit of that growth equally among the LECs and the IXCs.⁴ That finding was tenuous at best, and was made in the absence of any specific empirical support as the Commission itself would acknowledge some five years later in the *First Report and Order* in Docket 94-1.⁵ In that 1995 decision, the Commission finally and properly concluded that there was no hard evidence to find that the ILECs were responsible for stimulating demand growth in this market. In the Commission's own words:

Although the LECs assert that their marketing efforts and high service quality contribute importantly to the growth in common line traffic, they provide little concrete evidence that these efforts in fact have a significant effect on the volumes of interstate calling per line. As the other commenters point out, this usage appears to be almost totally a function of the price, quality, and marketing of IXC service as well as general economic trends.⁶

Because the IXCs, along with trends outside the LECs' control, have been responsible for growth in common line usage, the Commission properly concluded that the price caps rules should create incentives for the IXCs to further stimulate demand. The proper structure for such an incentive is the effective flow-through of all growth-related revenue gains resulting from the recovery of non-traffic sensitive LEC costs from an ever-growing level of usage demand. Conversely, given the Commission's

⁴ *Policy and Rules Concerning Rates for Dominant Carriers*, CC Docket No. 87-313, Second Report and Order, 5 FCC Rcd 6786 (1990) at ¶¶ 60 and 65.

⁵ *Price Cap Performance Review for Local Exchange Carriers*, CC Docket No. 94-1, First Report and Order, 10 FCC Rcd 8961, 9078 (1995) ("*LEC Price Cap Performance Review First Report and Order*").

⁶ *Id.* at 9078.

determination that the LECs did not influence common line usage demand, the Commission rightly found no reason to provide price cap incentives for them to do so.⁷

The Commission did not implement a “full g” back in 1995 (after concluding that the IXCs and trends outside the LECs’ control were responsible for demand growth) because of uncertainty regarding the adoption of a Total Factor Productivity (“TFP”)-based productivity offset.⁸ As the Commission acknowledges in the *NPRM*, this concern was unfounded since the Commission did not adopt a moving average TFP.⁹

The Commission nonetheless chose not to revise the common line formula to include a full “g” on the grounds that per-minute CCL rates would soon be phased out.¹⁰ The Commission has also acknowledged that this expected development did not occur as quickly as anticipated.¹¹ In Ad Hoc’s view, there are no more excuses for delaying implementation of a full “g.”

Increasing the “g” factor from “g/2” to a full “g” is the most efficient means to flow through the benefits of growth in common line usage to the IXCs and their end user customers, and it should be implemented immediately. Ad Hoc acknowledges that implementation of the full “g” for the common line basket will be short-lived at this point, since the “g” factor would be eliminated when the CCL is eliminated as part of access

⁷ *Id.* at 9078-79.

⁸ *Id.* at 9079-80.

⁹ *NPRM* at ¶ 227

¹⁰ *NPRM* at ¶ 227, citing *Price Cap Performance Review for Local Exchange Carriers* (CC Docket No. 94-1), *Access Charge Reform* (CC Docket No. 96-262), 12 FCC Rcd 16642, 16709-10 (1997) and *Access Charge Reform* (CC Docket No. 96-262), *Price Cap Performance Review for Local Exchange Carriers* (CC Docket No. 94-1), *Transport Rate Structure and Pricing* (CC Docket No. 91-213), *End User Common Line Charges* (95-72), 12 FCC Rcd 15982, 16027-28 (1997).

¹¹ *NPRM* at ¶ 227.

charge reform.¹² Nevertheless, the policy of moving to a full “g” is the correct one and, as discussed below, the Commission’s implementation of the full “g” for the common line basket has important implications for the adoption of similar adjustments to the price cap formula applicable to the traffic-sensitive and trunking baskets.

Conditions extant in the long distance marketplace today only further corroborate the conclusion correctly reached by the Commission almost five years ago that IXCs, and not the ILECs, are responsible for the steady growth in demand for interstate usage. The long distance market has become highly competitive over the past ten years since adoption of price caps regulation, with competition among IXCs producing aggressive marketing and pricing practices that provide an important stimulus to growth in interstate minutes of use.

II. THE COMMISSION CORRECTLY RECOGNIZES THE NEED TO IMPLEMENT A “Q” FACTOR IN THE PCI FOR THE TRAFFIC SENSITIVE AND TRUNKING BASKETS.

The FCC has invited comment on whether to include a “q” factor, similar to the “g” factor used in the common line PCI, in the PCI for both the traffic-sensitive and trunking baskets to account for trunk growth.¹³ Because of the same economic trends and factors described above in the context of the “g” factor, the Commission should apply a “full q” factor to all elements in both the local switching and trunking baskets that involve per-minute charges to recover capacity-based costs. Application of a “q” factor is also appropriate where capacity-based rates are in place if those rates do not reasonably track the causation of costs for the LECs. As the Commission observes, in

¹² See *NPRM* at ¶ 227.

¹³ *Id.* at ¶¶ 218, 225.

the case of local switching, costs are incurred only when an actual expansion of switch capacity is required which will not always coincide with trunk demand growth.¹⁴

The Commission's price cap policy must be applied consistently and must also be consistent with the economic principles underlying incentive regulation. As described in the preceding section, the fact that IXCs (in conjunction with general economic trends) are responsible for growth in access demand, rather than the LECs, was correctly determined by the Commission almost five years ago. The implementation of "q" factors for the local switching and trunking baskets, as proposed in the *NRPM*, is a necessary application of this finding. Indeed, the application of a "g" factor in the context of the common line formula, but not in analogous situations involving the local switching and trunking baskets, could not be justified on economic or public policy grounds.

Ad Hoc recognizes there are some differences between application of the "g" factor in the case of the common line basket and the proposed application of the "q" factor. For example, local switching is not the only element in the traffic-sensitive basket. However, a full "q" adjustment based upon the growth in trunks, and implemented in a manner analogous to the full "g" recommended above for the common line basket, best reflects the economic principles underlying incentive regulation. The full "q" need only be applied selectively to those elements (or to a predetermined portion of the total basket) where, because of growth, there is a mismatch between the manner in which rates are charged and the manner in which costs are incurred by the LECs.

¹⁴ *Id.* at ¶ 218.

A capacity-based rate structure will eliminate some of this mismatch between rate structure and cost causation. But, as the Commission indicates, local switching costs will not tend to vary directly with the associated per-trunk demand.¹⁵ And if the rate structure for local switching is not changed to include capacity-based rates, then the implementation of a “q” factor is even more essential to ensuring that LECs will not be overcompensated, as they have been in the past, for the effects of demand growth over which they have no control.

III. THE COMMISSION SHOULD REQUIRE ONE-TIME PCI ADJUSTMENTS TO REFLECT, ON A GOING-FORWARD BASIS, CHANGES TO THE “G” FACTOR AND THE INTRODUCTION OF A “Q” FACTOR

In conjunction with the Commission’s proposals to implement a full “g” in the PCI formula for the common line basket and to introduce an analogous “q” factor in the PCI formula for the local switching and trunking baskets, the Commission seeks comment on whether a one-time adjustment to the respective PCI formulae should be made to reflect these changes.¹⁶ These one-time adjustments would involve a restatement of the PCIs down to the levels that would have resulted had the Commission incorporated the proposed “g” or “q” factors either at the inception of price caps regulation in 1991, or as of some more recent year. Ad Hoc strongly supports the application of a one-time adjustment to the PCI formulae that took effect in 1991, for several reasons.

First, without a one-time adjustment based on a restatement of the PCIs from 1991 onward, the Commission cannot fully correct on a going-forward basis for the observed imbalances resulting from the recovery of essentially flat costs through traffic-sensitive rates since LEC price cap regulation took effect in 1991. Merely applying the

¹⁵ *Id.*

new PCI formulation to the current level of the PCI will not suffice, as the current level of the PCI reflects almost ten years of overstated price changes. That the LECs have benefited from an overly generous price cap formulation is corroborated by the high level of earnings they have enjoyed under price cap regulation. As the Commission itself acknowledges, the prior failure on the part of the Commission to include appropriate growth factors in the PCI formulas historically is likely a major contributing factor to the unexpectedly high level of LEC earnings under price cap regulation.¹⁷

Second, as mentioned previously, an adjustment of this type is consistent with the prior PCI adjustment required by the Commission's *Price Cap Performance Review Order* in connection with the Commission's subsequent exclusion of the 1984 data point in its original X factor studies.¹⁸ The reasoning underlying the Commission's prior adjustment (pertaining to the 1984 data point) applies with equal force to the current situation. One-time adjustments to the relevant PCIs to reflect the implementation of the "q" factor and the move from half "g" to full "g" would achieve the material correcting impacts needed to produce accurate going-forward PCIs for these baskets. Ad Hoc's preliminary estimates suggest these one-time adjustments could be quite substantial, i.e., in the range of one to two billion dollars.

IV. A CAPACITY-BASED CHARGE FOR LOCAL SWITCHING WOULD INCREASE THE ECONOMIC EFFICIENCY OF THE SWITCHED ACCESS RATE STRUCTURE.

The *NPRM* revisits the issue of the degree to which ILEC's local switching functions are non-traffic-sensitive ("NTS") and requests comment on the feasibility of

¹⁶ See *NPRM* at ¶¶ 222, 225, and 233.

¹⁷ *Id.*

¹⁸ *LEC Price Cap Performance Review First Report and Order*, 10 FCC Rcd at 9069-73.

changing the existing per-minute rate structure for local switching to capacity-based local switching charges.¹⁹ The Commission previously addressed this issue in the Access Charge Reform proceedings' *First Report and Order*, at which time it directed the ILECs to establish flat-rate charges for line-side ports and dedicated trunk ports.²⁰ With the cost recovery for those switching components removed from the per-minute local switching rate, that rate generally recovers now the costs of the switch central processor, the switching matrix and shared trunk ports.²¹

The ILECs' per-minute local switching rates may also recover certain other shared costs incurred during the provision of local switching that are not explicitly recovered elsewhere, such as costs for associated land, buildings, and power. Yet some of these costs are likely to be non-traffic-sensitive within a fairly wide range of demand levels.

Compared to the facilities that are dedicated to particular users, such as dedicated trunk ports, it may prove to be quite difficult to quantify the cost-capacity relationship for the shared facilities encompassed by the per-minute local switching charge. The underlying economic characteristics of end office switch components are likely to vary somewhat by item and among vendors' differing technological solutions. Moreover, those characteristics may be obscured by vendors' pricing practices, such as

¹⁹ *NPRM* at ¶¶ 211-216.

²⁰ *Access Charge Reform* (CC Docket No. 96-262), *Price Cap Performance Review for Local Exchange Carriers* (CC Docket No. 91-1), *Transport Rate Structure and Pricing* (CC Docket No. 91-213), *End User Common Line Charges* (CC Docket No. 95-72), *First Report and Order*, 12 FCC Rcd 15982, 16035-40 (1997) ("*Access Charge Reform First Report and Order*").

²¹ *Id.* at 16040. As discussed below, some ILECs have used their pricing flexibility under the price cap regime to essentially circumvent the Commission's determination to adopt the flat-rated structure for recovery of port and trunk costs.

the application of sometimes substantial discounts based upon the total volume of equipment ordered.

Nevertheless, Ad Hoc supports the principle of recovering the majority of local switching costs through capacity-based charges, because doing so will track the manner in which those costs are incurred more closely than per-minute charges. Whether or not the timing and incremental cost of capacity additions can be modeled precisely, it is well established that the non-dedicated portions of local switching facilities are sized to accommodate maximum (*i.e.*, peak busy-hour) demand and, are expanded on a time frame of months to years.²² By contrast, a per-minute rate structure implicitly assumes that local switching facilities are instantaneously scaled to match increases in traffic. This is unrealistic.

By creating a better match between underlying cost characteristics and the switched access rate structure, the Commission would increase the economic efficiency of switched access rates, which benefits the ILECs, their carrier customers, and end users. To the extent that the Commission chooses to implement capacity-based local switching charges, Ad Hoc urges the Commission to give particular scrutiny to the trunk demand forecasts that ILECs will presumably use to develop their proposed rate levels for the new charges. Given the magnitude of the access revenues at stake, the ILECs will undoubtedly face the same economic incentives that caused several ILECs to systematically under-estimate usage in the traffic demand forecasts for their 1997 access tariff restructure filings.²³

²² See, *e.g.*, Bell Communications Research, TR-TSY-000517, Issue 3, *LATA Switching Systems Generic Requirements, Section 17*, March 1989.

²³ *1997 Annual Access Tariff Filings*, 13 FCC Rcd 3815, 3825-26 (1997).

As discussed in the previous section, Ad Hoc also supports the use of formulae incorporating full “g” and “q” factors to establish charges assessed on a per-minute and per-trunk basis, respectively, consistent with the same goal of promoting economic efficiency. The current mismatch between the rate structures used by the ILECs and the aggregate costs they recover is likely to be greater in the case of per-minute charges than per-trunk, flat-rated charges. Nevertheless, capacity-based, per-trunk charges can be more closely aligned with carriers’ costs by applying a full “q” factor to each such charge that is ultimately included in ILECs’ switched access tariffs.

Ad Hoc agrees with the Commission’s tentative conclusion that the adoption of capacity-based local switching charges would not place smaller IXCs at an artificial disadvantage.²⁴ Historically, precisely the reverse has held true. Since the Commission’s 1993 modification of its switched transport rate structure to eliminate the artificial and inefficient “equal charge rule”²⁵ – and to better reflect real cost differences between low- and high-volume users of switched access services – smaller IXCs, as a group, appear to be thriving. For example, the Industry Analysis Division’s report on toll markets for the fourth quarter of 1998 indicates that smaller IXCs increased their market shares by seven-fold during the interval 1984-1997, from less than three percent in 1984 to twenty percent in 1997.²⁶ Accordingly, the continued viability of smaller IXCs

²⁴ NPRM at ¶ 215.

²⁵ *Transport Rate Structure and Pricing*, CC Docket No. 91-213, Report and Order and Further Notice of Proposed Rulemaking, 7 FCC Rcd 7006, 7007-8 (1992). The “equal charge rule” was originally adopted as a requirement in the Modification of Final Judgment (“MFJ”). *Id.* at 7008. See also *Access Charge Reform First Report and Order*, 12 FCC Rcd at 16059-60.

²⁶ Industry Analysis Division, Common Carrier Bureau, *Long Distance Market Shares: Fourth Quarter 1998*, March 1999, at 11.

would not appear to be compromised by moving the switched access rate structure another step closer to cost-causative characteristics.

The Commission should take the lead, however, in prescribing an optimum local switching rate structure, rather than allow the ILECs to devise their own capacity-based rates for local switching.²⁷ The Commission should take into account any credible empirical data the ILECs supply concerning the manner in which local switching costs are incurred. But, given that the underlying local switching functionalities and facilities are essentially the same for all ILECs, the carriers' rate structures should reflect that uniformity.

The Commission observes in the *NPRM* that certain ILECs (notably, GTE and Sprint) used their pricing flexibility under the price caps system to eliminate the flat-rated trunk port charges established in the *Access Reform First Report and Order*.²⁸ The *NPRM* seeks comment on whether the Commission should revise the price cap baskets to deter such manipulation.²⁹ Ad Hoc shares the Commission's concern that ILECs should be discouraged from manipulating their access charges to maximize revenues at the expense of economically efficient rate structures. However, if the Commission applies full "g" and "q" factors as discussed in the sections above, the manner in which demand growth is taken into account in the determination of access rate levels will be greatly improved, and the ILECs' incentive to shift revenue recovery from their flat-rate to their per-minute charges will be greatly reduced. Replacing the per-minute rate

²⁷ *NPRM* at ¶ 214.

²⁸ *Id.* at ¶ 234.

²⁹ *Id.*

structure for local switching with a capacity-based charge would, of course, further reduce such opportunities.

V. THE COMMISSION SHOULD FURTHER EXPLORE THE POTENTIAL FOR CAPACITY-BASED CHARGES FOR TANDEM SWITCHING.

The Commission seeks comment on two issues relating to the possible introduction of capacity-based charges for tandem switching, namely: (1) whether capacity-based charges are appropriate for tandem switching, given its differences from local switching; and (2) whether the Commission should add a “q” factor to the trunking basket PCI, and how such a “q” factor should be defined.³⁰ As indicated in Section II, above, Ad Hoc supports the principle of applying a “q” factor to the trunking basket PCI in order to properly take into account growth in the number of trunks in use. Ad Hoc also believes that the concept of capacity-based charges for tandem switching has merit and should be pursued by the Commission.

Over two years ago, the Commission deferred the development of capacity-based charges for tandem switching until a later time so that it could benefit from the experience of unbundled network element (“UNE”) rate structures that disaggregated traffic sensitive and non-traffic-sensitive switching costs.³¹ In most cases, the details of the ILEC cost studies for unbundled tandem switching and other UNEs were filed with state public utility commissions (“PUCs”) on a confidential basis and are thus unavailable to third parties. Publicly-available information suggests that ILECs typically developed unbundled tandem switching costs based on traditional proprietary costing models such as the BellCore Switching Cost Information System (“SCIS”) model, which

³⁰ *Id.* at ¶¶ 223-225.

³¹ *Access Charge Reform First Report and Order*, 12 FCC Rcd at 16064-65.

express their cost results in a traffic-sensitive manner (*i.e.*, SCIS outputs are expressed in terms of costs per call-setup and per minute of usage),³² without necessarily re-examining whether that assumption best reflects how costs are incurred. However, other state PUCs, as well as the ILECs themselves, may have more up-to-date data that would illuminate this issue.

CONCLUSION

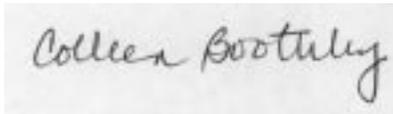
For the foregoing reasons, the Commission should adopt the proposed changes to the PCI formulae for the common line, local switching, and trunking baskets. Specifically, the Commission should move from half “g” to full “g” in the PCI formula for the common line basket and implement an analogous “q” factor in the PCIs for the local switching and trunking baskets. These changes are long overdue. In order to meaningfully correct on a going-forward basis for the imbalances that are inherent in the PCI formulae, which have favored the LECs since the outset of price cap regulation, the Commission should require one-time adjustments to the PCIs for each of these respective baskets. In addition, the Commission should also adopt, as proposed herein, rate structure changes for local

³² See, *e.g.*, California PUC, Docket R.93-04-003/I.93-04-002, D.98-02-106 (February 19, 1998), at 42-44 and attached Compliance Reference Document (redacted) at 1; Sprint/Central Telephone Company-Nevada, Costing Methodology and Studies for Unbundled Elements and Avoided Costs (redacted version), May 9, 1997, Tabs “Tandem Switching” and “Local Switching” (filed in Nevada PSC Docket No. 96-9035); and PUC of Ohio, Case No. 96-922-TP-UNC et al, Decision (June 19, 1997), at 171 (1997 Ohio PUC LEXIS 440).

switching and tandem switching that better align those rate structures with the manner in which costs are incurred and, in so doing, enhance economic efficiency in the ILECs' markets.

Respectfully submitted,

AD HOC TELECOMMUNICATIONS USERS
COMMITTEE



By: _____

Economic Consultants:
Patricia D. Kravtin
Scott C. Lundquist
Economics and Technology, Inc
One Washington Mall
Boston, Massachusetts 02108
(617) 227-0900
October 29, 1999

Colleen Boothby
Levine, Blaszak, Block & Boothby, LLP
2001 L Street, NW, Suite 900
Washington, D.C. 20036
(202) 857-2550

Their Attorneys

Certificate of Service

I, Betsy Eisen, hereby certify that a true and correct copy of the preceding Comments of the Ad Hoc Telecommunication Users Committee was served this October 29, 1999 via hand delivery upon the following party:

International Transcription Services, Inc.
1231 20th Street, NW
Washington, DC 20037



Betsy Eisen
Legal Assistant

October 29, 1999