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Before the
FEDERAL COMMUNICATIONS COMMISSION
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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

AT&T COMMENTS ON LEC PRICING FLEXIBILITY FNPRM

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TABLE OF CONTENTS

SUMMARY i

I. GEOGRAPHIC RATE DEAVERAGING FOR SWITCHED ACCESS SERVICES SHOULD NOT BE PERMITTED WITHOUT CERTAIN COMPETITIVE PREREQUISITES HAVING BEEN MET 3

II. A LEC MUST BE REQUIRED TO SATISFY A MEANINGFUL COMPETITIVE TEST BEFORE IT IS ALLOWED PHASE II PRICING FLEXIBILITY FOR SWITCHED SERVICES 8

III. CAPACITY-BASED LOCAL SWITCHING CHARGES SHOULD NOT BE ADOPTED BUT THE PRICE CAP MECHANISM SHOULD ACCOUNT FOR GROWTH IN THE TRAFFIC-SENSITIVE BASKET 12

A. The Local Switching Rate Structure Should Remain Per-Minute-Based 12

B. A Q Factor Should Be Added To The Traffic-Sensitive PCI Formula 17

C. A One-Time Adjustment Should Be Made To The Traffic-Sensitive Basket PCI 19

IV. OTHER LIMITED MODIFICATIONS TO THE PRICE CAP MECHANISM, INCLUDING A FULL G FACTOR OR REVENUE PER LINE CAP FOR THE COMMON LINE BASKET, SHOULD BE ADOPTED 20

A. The Common Line Price Cap Formula Should Be Modified So That The Common Line Revenue Requirement Is Permitted To Increase With The Average Growth Rate Of Total Lines 20

B. A One-Time Adjustment Should Be Made To The Common Line Basket PCI 26

V. PERMISSIVE DETARIFFING OF CLEC ACCESS CHARGES IN EXCESS OF ILEC RATE LEVELS WILL BEST SERVE THE COMMISSION'S GOALOF FOSTERING MARKET-BASED CONSTRAINTS ON RATES 27

CONCLUSION 33

SUMMARY

In these comments, AT&T responds to the Commission's FNPRM on issues related to price cap LECs' common line and traffic-sensitive services: geographic rate deaveraging, Phase II pricing flexibility, and modifications to the price cap formulas for the baskets containing those services. AT&T also responds to the FNPRM's proposals on constraining CLEC access charges.

In Section I, AT&T opposes affording LECs the ability to geographically deaverage their common line rates in a study area prior to competitive prerequisites having been met, and opposes deaveraging of traffic-sensitive rates even after such conditions have been met. Absent specific conditions as outlined herein, such deaveraging would allow the LECs to employ anticompetitive tactics such as cross-subsidization in markets where there is not sufficient competition to discipline exchange access pricing. In addition to 254(g) forbearance, the CCLC, PICCs and ILEC Flowback must be eliminated and all remaining carrier access charges must be set at forward-looking economic cost in the study area. Deaveraged UNE loops must also be available in the study area where deaveraging relief is requested. Once these preconditions are met, the FCC should permit common line deaveraging using the a straightforward adaptation of the FCC's universal service cost proxy model to develop the costs for each UNE zone. Also, an interstate access-related USF should be established to ensure that universal service is preserved in areas with high loop costs. The Commission should not permit deaveraging of traffic-sensitive elements (local switching and tandem switching), because there is no clear evidence to suggest that the costs of these elements vary geographically within a study area.

As demonstrated in Section II, in addition to the preconditions for common line deaveraging having been met, Phase II relief should not be granted for common line and

traffic-sensitive services until facilities-based competition exists for each component of access for which relief is sought throughout a given MSA. The relevant precedent for determining the existence of competition to guide the Commission's review for Phase II relief is the AT&T nondominance proceeding. Before Phase II relief may be granted in an MSA, facilities-based competitor(s) must offer the services for which the LEC seeks regulatory relief at a price and quality comparable to that of the LEC; competitors' services must be available to 75% of subscriber locations and 50% of subscriber locations must actually be served by such alternate facilities-based providers in the MSA. Facilities-based competitors must have sufficient capacity to absorb substantial amounts of LEC traffic in the event of a significant non-transitory price increase. Even at Phase II, some level of averaging should be required for common line rates to match UNE zones (with a maximum of four zones).

AT&T shows, in Section III.A, that a capacity-based rate structure for local switching should not be adopted because there is no evidence that more switching costs should be recovered on a per-trunk basis than reflected in the LECs' January 1, 1998 tariffs. Moreover, even though the Commission gave them the option of a capacity-based charge for UNE switching, nearly all state commissions have implemented UNE rate structures that consist of line port, trunk port and minutes-of-use rates – essentially the same as the FCC's structure for interstate access. Further, because IXCs order trunks based on their own peak period traffic, which comprises only a small portion of overall LEC traffic and whose peak may differ from that of the LEC's traffic, a capacity-based charge would not capture peak demand any better than a per-minute charge.

As discussed in Section III.B, the Commission's proposal to adjust the traffic-sensitive basket PCI for growth in traffic volumes represents a constructive approach to bringing local switching rates closer to their underlying costs and should be adopted, regardless of whether

the local switching rate structure remains usage-based or is changed to a capacity-based structure. A "q" factor will properly adjust the LECs' traffic-sensitive PCIs as a result of IXC-initiated growth in local switching minutes and/or trunks, while the LECs will continue to earn a reasonable profit given that unit costs decline with growth in traffic volumes. Such an adjustment is needed because despite a 66% growth in switching minutes from 1991 to 1998, the RBOCs' expenses and investment have declined substantially, resulting in a 52.5% rate-of-return for local switching in 1998. LECs should also be required to reduce their PCIs to the levels that would have resulted had the FCC incorporated a q factor in the traffic-sensitive PCI in 1991.

As shown in Section IV.A, the FCC's concerns about whether the g factor, as well as the multiline business PICC, generate the appropriate amount of revenue can be addressed by capping common line rates on a revenue per line basis, thereby permitting "common line revenue to increase with the average growth rate of all common lines." FNPRM, ¶ 233. The current g/2 formula confers an unwarranted windfall on those LECs that still charge the CCLC, which generally tend to be the LECs with the highest interstate access rates. Because multiline business lines are growing faster than the primary residential and single-line business lines that receive a subsidy via the multiline business PICC, LECs have reaped a substantial windfall since January 1, 1998. With a revenue per line cap, the amount of revenue obtained from subsidy elements – i.e., the multiline business PICC and CCLC – is equal to the shortfall in revenue per line collected from the lines receiving the subsidy. As an alternative to capping total common line revenue on a per line basis, the Commission can achieve similar results by using a full "g" in the common line PCI formula and adding the requirement that total revenue from SLCs and PICCs be capped on a per line basis. As shown in Section IV.B, the LECs should also be required to reduce their PCIs to the levels that

would have resulted had the FCC incorporated a full g factor in the common line PCI formula at the inception of price caps.

As discussed in Section V, CLECs whose switched access charges do not exceed the ILEC level should be permitted to continue filing tariffs under current streamlined review standards, or to proceed at their option through contractual arrangements with IXCs. However, the Commission should require CLECs that elect to file tariffed switched access rates that exceed the ILEC level in the same service area to justify those charges in traditional, non-streamlined review proceedings, with full cost support. Alternatively, CLECs that wish to charge a higher originating and/or terminating switched access rate than the corresponding ILEC and do not wish to use the tariff process, may proceed on a detariffed (i.e., contractual) basis with IXCs that desire to do business with them. This paradigm allows competitively priced CLECs to retain the administrative convenience of the tariff mechanism for charges that are somewhat constrained by regulation of the incumbent. Moreover, it does not preclude any IXC from negotiating with the CLEC for a satisfactory access rate. This approach promotes effective and economical operation of the competitive marketplace, to the benefit of all consumers, preserves the Commission's longstanding policy of relying on market forces, and avoids the complexities of the geographic rate deaveraging and calling/called-party-pays regimes, on which the Commission seeks comment in the FNPRM.

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AT&T COMMENTS ON LEC PRICING FLEXIBILITY FNPRM

Pursuant to the Commission's Fifth Report and Order and Further Notice of Proposed Rulemaking, FCC 99-206, released August 27, 1999 in the above proceedings ("Fifth Report" and "FNPRM," respectively), and Section 1.415 of its rules, AT&T Corp. ("AT&T") submits these comments on the Commission's proposals to: (1) allow geographic deaveraging of common line and traffic-sensitive access charges by incumbent price cap local exchange carriers ("LECs" or "ILECs"); (2) define the triggers and relief for Phase II pricing flexibility for switched services; (3) modify the rate structure for local switching and the price cap formula for the traffic-sensitive basket; (4) revise the price cap mechanism for the common line basket and make other modifications to price caps; and (5) adopt rules to address the failure of market forces to constrain competitive local exchange carrier ("CLEC") access charges.

Several of the Commission's proposals, including the "q" factor for the traffic-sensitive basket, the full "g" factor for the common line basket, and one-time adjustments to the price cap indices ("PCIs") for each of those baskets, would impact future access rates. AT&T and Bell Atlantic, BellSouth, GTE, SBC and Sprint are part of the Coalition for Affordable Local and Long Distance Services ("CALLS") and have recently made a proposal to the Commission which, if accepted, would obviate the need for such prospective rate adjustments for LECs who are CALLS members.[1] In addition, the CALLS proposal allows for geographic deaveraging of common line rates subject to certain prerequisites and constraints. AT&T's position on geographic rate deaveraging and other issues is different herein than in CALLS, which is, of course, a compromise plan.

Given its numerous public interest benefits, AT&T strongly supports the CALLS proposal and urges the Commission to adopt it for *all* price cap LECs. If the Commission does so, the CALLS proposal would resolve, in an equitable and sustainable manner, virtually all of the issues addressed in Sections I, III, and IV of these comments. If the Commission adopts the CALLS proposal only for LECs that have voluntarily agreed to the CALLS proposal, the positions that AT&T advocates herein would be largely applicable to those price cap LECs, including but not limited to Ameritech and U S WEST, who are not members of CALLS. Although the CALLS plan should be adopted to rationalize the access and universal service regimes, if for any reason it is not adopted by the Commission, AT&T's positions, as stated herein, would apply to all price cap LECs.

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1 Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Low-Volume Long Distance Users, and Federal-State Joint Board on Universal Service, CC Docket Nos. 96-262, 94-1, 99-249 and 96-45, Notice of Proposed Rulemaking, FCC 99-235, released September 15, 1999 (requesting comments on the CALLS proposal).

I. GEOGRAPHIC RATE DEAVERAGING FOR SWITCHED ACCESS SERVICES SHOULD NOT BE PERMITTED WITHOUT CERTAIN COMPETITIVE PREREQUISITES HAVING BEEN MET.

The FNPRM (¶¶ 190-199) requests comment on whether the Part 69 access charge rules should be amended to permit price cap LECs to deaverage interstate common line and traffic-sensitive access charges within their study areas and, if so, what, if any, preconditions should exist before such deaveraging is permitted, and how it should be accomplished. In general, AT&T opposes affording LECs the ability to geographically deaverage their common line rates prior to certain prerequisites having being met in a given study area and opposes deaveraging of traffic-sensitive rates even after such conditions have been met. Absent the conditions outlined below, deaveraging would allow the LECs to employ anticompetitive tactics – specifically, cross-subsidization – in markets where sufficient competition to provide exchange access discipline has not yet developed. *(See Section II for the Phase II triggers).*

Because competition will emerge initially in high density zones, without limitations on geographic deaveraging, LECs could cross-subsidize the charges in those zones by increasing (or refusing to make appropriate reductions to) rates in low-density zones. Geographic averaging reduces the likelihood of such behavior and it also allows customers in lower density zones to enjoy the price reductions engendered by new entrants in other market segments. Moreover, as the Commission acknowledges, if it permits "LECs to deaverage common line and/or traffic sensitive access charges, this may increase pressure on IXCs to deaverage interstate interexchange service rates in a manner that conflicts with section 254(g) of the Act." FNPRM, ¶ 191. Thus, any geographic deaveraging that is permitted must be accompanied by FCC action forbearing from Section 254(g)'s requirements.

In addition to 254(g) forbearance, the following conditions must prevail before common line rates may be deaveraged in a LEC study area. The carrier common line charge ("CCLC"), presubscribed interexchange carrier charges ("PICCs"), and ILEC Flowback must

be eliminated from carrier access charges; and remaining carrier access charges must be set at forward-looking economic cost. And, unbundled network element ("UNE") loops must be available on a deaveraged basis throughout the study area where deaveraging relief is requested by the LEC.[2]

The CCLC, PICCs and ILEC Flowback are all implicit subsidies paid by interexchange carriers ("IXCs") to the LECs. The Commission recognized in the Access Charge Order that recovering nontraffic-sensitive ("NTS") costs through flat monthly charges imposed on *end users* would promote optimal utilization of telecommunications facilities,[3] and that "it is important to move towards collecting these costs from customers rather than carriers on a flat rather than usage sensitive basis."[4] Nonetheless, 15 years later loop costs are still recovered only in part from flat charges on end users via SLCs, and IXCs must subsidize these loop costs through the CCLC and PICCs.[5] Charging IXCs for recovery of loop costs

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2 The availability of deaveraged UNEs is mandated by the Commission's local competition rules, irrespective of any pricing flexibility granted to the LEC. 47 C.F.R. 507(f). The Commission has indicated that it will lift the stay of its deaveraged UNE rule six months after the release of its (recently-announced) orders in CC Docket No. 96-45 (*Universal Service)* implementing high-cost universal service support for non-rural LECs under Section 254 of the Telecommunications Act. Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Deaveraged Rate Zones for Unbundled Network Elements, CC Docket No. 96-98, Stay Order, FCC 99-86, released May 7, 1999, ¶ 3; see also FCC News, Common Carrier Action, FCC Reforms High-Cost Support to Ensure the Preservation and Advancement of Universal Service, Summary of High-Cost Universal Service Orders, released October 21, 1999 (announcing adoption of Input Values for the Forward-Looking Cost Model (CC Docket Nos. 96-45, 97-160, FCC 99-304, and New Mechanism for Federal Universal Service High-Cost Support Provided to Non-Rural Carriers (CC Docket No. 96-45, FCC 99-305), p. 3.

3 See, e.g., MTS and WATS Market Structure, 93 FCC 2d 241, 242, 279 (1983) (Access Charge Order).

4 Access Charge Order, 97 FCC 2d at 265.

5 Access Charge Reform, First Report and Order, 12 FCC Rcd. 15982, ¶¶ 53-60 (1997) (Access Reform Order); id., Order on Reconsideration, FCC 97-247, ¶ 15, released July 10, 1997 (Reconsideration Order).

violates economic cost-causation principles because the loop cost is not an incremental cost of providing access to carriers.[6] Similar to the ILEC Flowback, which the Fifth Circuit recently found to be an impermissible implicit subsidy, any continued assessment of the CCLC and PICCs on IXCs violates "the mandate in Section 254(e) of the 1996 Act that all support be explicit."[7] Indeed, the fact that the CCLC and PICCs are assessed only on IXCs is flatly inconsistent with Section 254(d), which requires every carrier that provides interstate telecommunications services to contribute on an "equitable and nondiscriminatory basis" to universal service. Accordingly, all of these elements must be recovered by a LEC exclusively from its end user customers before any common line deaveraging is permitted.

Further, the remaining carrier-paid access rate elements must be set at forward-looking economic cost to avoid the cost/price squeeze created by excessive LEC access rates. Most directly, excess access rates confer a tremendous strategic advantage, particularly as the LECs contemplate in-region entry into long distance services. Given that the LECs are both competitors and suppliers of IXCs in certain markets (and of competitive access providers ("CAPs") in many more markets), LECs have the opportunity to 'price squeeze' their competitors by raising prices of bottleneck services and lowering price in competitive

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6 As the Commission has expressly found:

> "A subscriber who does not use the subscriber line to place or receive calls imposes the same NTS costs as a subscriber who does use the line. A subscriber who does not make local calls would normally pay a flat fee for the exchange portion of such costs. Imposing a flat charge for the interstate portion of those costs is equally reasonable. Any other procedure violates the general principle that costs should be recovered from the cost-causative ratepayer whenever it is possible to do so." Access Charge Order, 97 FCC 2d at 278, ¶ 121.

7 Texas Office of Public Utility Counsel v. FCC, 183 F.3d 393 (5th Cir.1999), *petitions for rehearing and rehearing en banc denied* (Sept. 28, 1999).

downstream markets.[8] To the extent that access charges exceed economic costs, a LEC faces a lower cost of providing long distance services than competitors who must pay excessive exchange access charges. For that reason, a LEC "ha[s] an incentive to discriminate in providing exchange access services and facilities that its affiliate's rivals need to compete in the interLATA telecommunications services . . . market."[9] The harm to competition is not limited to interexchange markets. As customers increasingly demand "one-stop shopping" for bundles of local exchange, exchange access, and toll services, LECs can use their cost advantage to protect local markets as well. "This artificial advantage may allow the BOC affiliate to win customers even though a competing carrier may be a more efficient provider in serving the customer."[10] Thus, prior to deaveraging of common line rates, it is critical that all carrier-paid access charges in the study area be set at efficient, forward-looking economic cost.

Once all of these conditions are met, and the LEC has made available deaveraged UNEs in the study area where deaveraging relief is sought, the Commission should permit, but not require, a LEC to deaverage its common line rates in the following manner. First, the Commission's forward-looking cost proxy model that is being developed in the Universal Service proceedings, CC Dockets 96-45 and 97-160, should be modified as appropriate and used to develop common line costs for the UNE zones in a study area.

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8 Policy and Rules Concerning Rates for Dominant Carriers, 5 FCC Rcd 6786, ¶ 19 (1990) (LEC Price Cap Order).

9 Implementation of the Non-Accounting Safeguards of Section 271 and 272 of the Communications Act of 1934, CC Docket No. 96-149, First Report and Order and Further Notice of Proposed Rulemaking, ¶ 7, released December 24, 1996 (Non-Accounting Safeguards Order).

10 Non-Accounting Safeguards Order, ¶ 12.

The Commission should not require identical zones for all access elements, because the market for different elements will vary and some elements may not have any geographically distinct cost characteristics. FNPRM, ¶ 195. LECs should not be permitted to define their own common line zones, and, in no event, should common line zones be based on trunking zones, which, under the Fifth Report, need not be cost-based.

Deaveraging of common line rates should not be predicated on *current* SLC caps (FNPRM, ¶ 194). Rather, SLC rates should be permitted to increase to the extent necessary for the SLC in any given zone to recover fully the interstate-assigned portion of the loop, line ports and retail marketing expense. To the extent that subsidies are needed to defray the SLC to ensure universal service in high-cost zones, the Commission should provide the necessary support through an interstate access-related universal service fund ("USF"). If recovery of common line revenues in excess of what the LEC is able to recover in a high-cost zone from end users via SLCs and USF support is permitted, these costs should be allocated to recovery via SLCs in the lowest cost zones so that these amounts can be competed away quickly. FNPRM, ¶ 194.

The Commission should not permit deaveraging of the traffic-sensitive access elements, namely, local switching and tandem switching. There is no evidence to suggest that the costs of these elements vary geographically within a study area. State commissions generally have not found a basis for deaveraging unbundled switching elements. The per-minute local switching and tandem switching UNE rates have been deaveraged by only a handful of states. Most states have provided switching UNE rates that are averaged across the study area.[11] Thus, unless the states find some cost-based justification for geographic

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[11] Petition of AT&T Communications of New York, Inc., for Arbitration of an Interconnection Agreement with New York Telephone Company, "Order Approving

(footnote continued on following page)

deaveraging of these elements, there would be no predicate for, and the FCC should not permit, any deaveraging of equivalent exchange access elements because it would create undesirable arbitrage opportunities that would distort customer usage and investment decisions.

II. A LEC MUST BE REQUIRED TO SATISFY A MEANINGFUL COMPETITIVE TEST BEFORE IT IS ALLOWED PHASE II PRICING FLEXIBILITY FOR SWITCHED SERVICES.

With respect to Phase II pricing flexibility for common line and traffic-sensitive services, and the traffic-sensitive components of tandem-switched transport services offered by price cap LECs, the Commission requests comment on: (i) the appropriate triggers for such relief, and (ii) how Phase II relief for common line and traffic-sensitive services might differ from the Phase II relief for dedicated transport and special access services established in the Fifth Report. FNPRM, ¶ 200. The Commission also seeks comment on whether it should impose certain safeguards with respect to Phase II relief for common line and traffic-sensitive services that it did not impose with respect to dedicated transport and special access services. FNPRM, ¶ 205.

Phase II relief should not be granted for common line and traffic-sensitive services until facilities-based competition exists for each component of access for which relief is sought throughout a metropolitan serving area ("MSA"). In addition, all of the preconditions cited above for common line deaveraging in a study area (namely, 254(g) forbearance; elimination of CCLC, PICCs, ILEC Flowback; all remaining carrier-paid access rate elements

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(footnote continued from previous page)
Interconnection Agreement," Case No. 96-C-0723, New York Public Service Commission (June 13, 1997); Petition of AT&T Communications of the Southwest, Inc. for Compulsory Arbitration to Establish an Interconnection Agreement between AT&T and Southwestern Bell Telephone Company, "Arbitration Award," Docket No. 16226, Public Utility Commission of Texas (Dec. 19, 1997).

priced at forward-looking economic cost; and deaveraged UNE loops available) must exist before Phase II relief is granted for an MSA within that study area. Thus, in addition to the presence of facilities-based competition discussed below, there should be no Phase II relief for an MSA unless it is located in a study area where deaveraged UNE loops are available and these other preconditions have been met.

The relevant precedent to guide the Commission's review as to the existence of facilities-based competition is the AT&T nondominance proceeding. The ultimate decision to grant AT&T greater flexibility and release it from various regulatory constraints came only after substantial time and consideration of many factors including market share, demand responsiveness, supply responsiveness, and AT&T's pricing behavior. In support of its decision to release AT&T from the price cap system, the Commission cited numerous factors indicating the presence of at least two national facilities-based competitors plus hundreds of other carriers that employ facilities or resale or both to provide service to customers, and AT&T's lack of control over "bottleneck facilities for over ten years."[12] The Commission must conduct an equally rigorous inquiry for LEC Phase II relief. AT&T believes that UNE loops, for which a new entrant is entirely dependent on the LEC, should <u>not</u> be considered a competitor's own facilities for purposes of the competition test. Nonetheless, because the Commission has held that it would treat UNE loops as a competitor's facilities in the Fifth Report (¶ 113), AT&T has incorporated information concerning such loops in its test.

AT&T suggests that the following criteria to determine the existence of facilities-based competition should be met before Phase II relief is granted for common line and traffic-sensitive services in an MSA. Facilities-based competitor(s) must offer those services at a

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[12] <u>Motion of AT&T Corp. To Be Reclassified As A Non-Dominant Carrier</u>, 11 FCC Rcd 3271, ¶ 41 (1995).

price comparable to the LEC's price cap rate and at a level of quality comparable to that of the LEC. Such competitive services must be available to 75% of subscriber locations in the MSA, and 50% of subscriber locations in the MSA must actually be served by such alternate facilities-based providers rather than the LEC. Facilities-based competitors must have sufficient capacity to absorb substantial amounts of the LEC's business in the event of a small but significant non-transitory price increase. Data used to measure competition should be drawn from sources that are reliable and verifiable by an independent third party.

For Phase II relief, a price cap ILEC should be required to demonstrate that competitors provide common line and traffic-sensitive services to 50% of ILEC subscriber locations on their own facilities in the MSA. These data can be determined in the following manner. The LEC should provide the data relating to the number of subscribers it serves using its own common line and switching facilities as well as the number of UNE loops that it has provided to other carriers that do not use LEC switching facilities. AT&T commits that it will provide, on a confidential treatment basis, the data regarding the number of customer locations it serves via cable facilities, and it believes that other major carriers would be willing to provide comparable data concerning the number of subscriber locations they serve over their own local distribution (non-UNE-loop) plant. The Commission should also require any incumbent LEC that is providing local service outside of its own franchise area to provide these data. Although this "data gathering net" will not provide data on every new entrant, it will certainly cover the vast majority of customer locations in a given MSA. In no event, should the Commission allow the 50% market penetration test to be demonstrated solely by a showing that new entrants "offer" (rather than actually "provide") service to 50% of subscriber locations, as the Commission appears to have done in allowing using of advertising to meet the Phase I trigger. Fifth Report, ¶¶ 120-121. At this time, the Commission should exclude mobile wireless service from the Phase II trigger because it has yet to be

demonstrated that wireless service is a substitute for local landline telephony. Inclusion of wireless loops may be appropriate once wireless carriers are classified as LECs within a study area. FNPRM, ¶ 202.

The Commission also asks whether, once the Phase II triggers have been met, a LEC should be permitted to offer its common line and traffic-sensitive services outside of the Part 69 rate structure and Part 61 price cap rules, and file tariffs on one day notice, which is the Phase II relief that the Fifth Report granted for special access and dedicated transport services. Certain constraints are required for common line and traffic-sensitive services, even after the Phase II triggers have been met. For the reasons stated in Section I, there should be no deaveraging of traffic-sensitive rates, and some level of averaging should be required for common line rates to match UNE zones. There is simply no reason to allow LECs to granularize their common line rates below the UNE zone level, particularly when competitors are dependent on UNE loops to serve their end user customers and the subscribers served via such loops are counted toward the 50% market penetration test. AT&T also believes that it would be reasonable to limit common line deaveraging to no more than four zones in a study area in order to protect LEC subscribers who may not have the ability to choose to subscribe to service from a CLEC under the competitive triggers suggested herein.

Moreover, so long as carriers continue to receive USF high-cost interstate access-related support (USF III) based on presumed high-cost rate caps, LECs that receive such USF support must adhere to the high-cost rate cap. Otherwise there would no constraint to ensure that a LEC was not recovering from its end user customers an amount above the high-cost rate cap on which the forward-looking USF support was based, while drawing the full support amount from the USF. Although the LEC should be permitted to charge a rate to the end user that is above the high-cost rate cap used for determining USF support, if it does so, it should be required to forego such support or, at a minimum, offset dollar-for-dollar such

increased revenue against USF support to avoid double recovery. Further, for the reasons indicated in Section I, the LEC must continue to charge all common line costs and its USF contribution expense to the end user even after Phase II relief. In other words, a LEC should not be able to undo the predicate for Phase II relief, once such relief is granted. FNPRM, ¶¶ 204-206.

III. CAPACITY-BASED LOCAL SWITCHING CHARGES SHOULD NOT BE ADOPTED BUT THE PRICE CAP MECHANISM SHOULD ACCOUNT FOR GROWTH IN THE TRAFFIC-SENSITIVE BASKET.

A. The Local Switching Rate Structure Should Remain Per-Minute-Based.

The Commission seeks comment on whether LECs should be required to develop capacity-based local switching charges (by considering the aggregate number of trunks switched by the LEC) rather than per-minute-based charges. FNPRM, ¶ 207. AT&T believes that the current rate structure for local switching is reasonably cost-based and no changes to the Part 69 access charges rules are needed.[13] Thus, a capacity-based rate structure for local switching based on the number of trunks connected to end office switches should not be adopted.

Trunk-based charges have already been established as part of the Access Reform Order (¶¶ 125-29) with trunk port charges initially accounting for about 7%-8% of local switching revenue. No evidence has been presented thus far to suggest that the current

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[13] As discussed in the Section III.B, *infra,* certain Part 61 price cap changes are required. First, the Commission's proposed "q" factor is needed in order for local switching rates to properly reflect the decline in unit costs resulting from growth in traffic volumes. Second, additional constraints are needed to prevent LECs from undermining the current structure by shifting revenues from their trunk port charge to the per-minute charge. This can be accomplished by establishing a zero upward pricing band limit on the per-minute local switching rate (as was done with the TIC in the local transport restructure).

structure fails to reflect cost causation. Specifically, no one has provided any evidence that more costs should be recovered on a per-trunk basis in addition to the trunk port costs identified by the LECs in connection with their January 1, 1998 tariffs.[14] Because the current rate structure has been in effect only since January 1998, it would be premature to abandon it without solid evidence that a new structure could be implemented that would be more efficient.

The Commission permitted state public utility commissions to adopt either traffic-sensitive or capacity-based rate structures for local switching UNEs.[15] FNPRM, ¶ 210. Local switching costs have been (thoroughly and extensively) reviewed by state regulators who, in nearly all instances, have implemented UNE rate structures that consist of line port, trunk port, and minutes-of-use rates – essentially the same as the FCC 's structure for interstate access.[16]

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14 Access Reform Order, ¶ 134.

15 FNPRM, ¶ 210, citing Local Competition Order, 11 FCC Rcd at 15878-79, 15905.

16 Alabama, Docket 26029, Consideration of TELRIC Studies, August 25, 1998, p. 42; Arkansas, Docket 96-395-U, Order No. 16, July 8, 1998; Arizona, Docket U-3021-96-448, Commission Order Rates/Terms, January 30, 1998, p. 7; California, Application 96-08-040, In the Matter of the Petition of AT&T Communications, Inc. for Arbitration Pursuant to Section 252(b) of the Telecommunications Act of 1996 to Establish an Interconnection Agreement with Pacific Bell, Decision 96-12-034, December 9, 1996, Attachment 8, Appendix A, pp. 1-2; Colorado, Docket 96S-331T, Commission Order adopted, July 16, 1997, p. 62; Iowa, Final Decision and Order, April 23, 1998, p. 1; Florida, Docket No. 960833-TP, Petition by Metropolitan Fiber Systems of Florida, Inc. for Arbitration with BellSouth Telecommunications Inc., Concerning Interconnection Rates, Terms, And Conditions Pursuant To The Federal Telecommunications Act of 1996, April 06, 1998; Georgia, Docket No. 7061U, Review of Cost Studies, Methodologies & Cost-Based Rates for Interconnection and Unbundling of BellSouth Telecommunications Services, December 16, 1997, p. 37; Idaho, Case No. USW-T-96-15 ATT-T-96-2, Arbitration Order 27236, February 1, 1997, p. 13; Kansas, 97-AT&T-290-ARB, May 18, 1998; Kentucky, Docket No. 96-482, ICA negotiations between AT&T Communications of the South Central States, Inc. and BellSouth Telecommunications Inc., July 14, 1997; Louisiana, Docket No. U-22022, Review and Consideration of BellSouth Telecommunications, Inc.'s TSLRIC and LRIC Cost Studies Submitted Pursuant To Sections 901(C) and 100(E) of the Regulations for Competition

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The Commission suggests that by reflecting peak demand, a capacity-based rate structure may better reflect the manner in which LECs incur local switching costs, because IXCs presumably order capacity based on their peak period traffic. FNPRM, para 211. The

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in the Local Telecommunications Market as adopted by General Order dated March 15, 1999 in Order To Determine The Cost Of Interconnection Services And Unbundled Network Components To Establish Reasonable, Non-Discriminatory, Cost Based Tariff Rates; see also U-22093, Review and Consideration of BellSouth Telecommunications Inc.'s tariff filing of April 1, 1996, filed pursuant to Sections 901 & 100 of the Regulation for Competition in the Local Telecommunications Markets, which tariff introduces interconnection and unbundled services and establishes the rates, terms, and conditions for such service offerings, October 17, 1997; Maine, Interconnection Agreement, April 7, 1999. Massachusetts, Proposed UNE Tariff, DPU No. 17; Minnesota, Docket Numbers p-442, 421/M-96-855, p-5321, 421/M-96-909, p-3167, 421/M-96-729, Order Resolving Arbitration Issues, December 2, 1996, p. 60; see also Arbitrator's Report, November 5, 1996; Mississippi, Docket No. 97-AD-544, To Establish "Permanent" Prices for BellSouth Interconnection and Unbundled Network Elements, August 25, 1998; Missouri, Case No. TO-98-115, March 30, 1998; see also Case No. TO-97-40; Montana, Docket D96.11.200, Response Petition for Reconsideration, May 12, 1997, p. 29; North Dakota, PU-453-96-497, Order Approving Arbitrated Agreement, June 23, 1997, p. 5; Nebraska, APP No. C-1385, Approved ICA, July 1, 1997, p. 3; New Hampshire, Interconnection Agreement, April, 27, 1999; Investigation Regarding Local Exchange Competition for Telecommunications Services, Docket No. TX95120631, Telecommunications Decision and Order, p. 62 (N.J. Bd. of Pub. Utils. 1997); Application of Bell Atlantic-Delaware, Inc. for Approval of its Statement of Terms and Conditions under Section 252(f) of the Telecommunications Act of 1996, PSC Docket No. 96-324, Findings Opinion & Order No. 4542, Exhibit E (Del. PSC 1997); New Mexico, Docket 96-307-TC, Conclusions, p.7; see also New Mexico, Docket 96-411-TC, p. 7. New York, Case No. 95-C-0657, PSC Opinion No. 97-2, April 1, 1997; North Carolina, Docket No. P-100, Sub 133d, To Determine Permanent Pricing for Unbundled Network Elements, December 10, 1998, p. 7; Oklahoma, Cause No. PUD 990000225, Order No. 434291, August 9, 1999; Oregon, Order 96-188, Appendix C, p. 1; Rhode Island, Interconnection Agreement, June 7, 1999; South Carolina, Case No. 97-374-C, To Review BellSouth Cost Studies for UNE, September 18, 1998, Order No. 98-723; South Dakota, Docket TC-96-184, Order on Reconsideration, July 15, 1997, p. 2; Texas, Docket 16226, AT&T/SWBT Interconnection Commitment Appendix Pricing UNE Schedule of Pricing, April 1, 1998, p. 3; Tennessee, Docket No. 97-01262, To Convene A Contested Case Proceeding To Establish Permanent Prices For Interconnection and UNEs, January 25, 1999; Utah, Order 94-999-01, June 2, 1999, p. 11; Vermont, Interconnection Agreement, June 10, 1998; Washington, Docket UT 960309 Arbitrator Report and Decision, November 27, 1996, p. 39; Wyoming, Docket No. 5 72000-TF-96-95, ¶ 74; see also Docket No. 70000-TF-96-319, Order On Rehearing March 22, 1999, ¶ 157.

number of trunks purchased by an IXC, however, is not necessarily a good proxy for the amount of switching capacity required during peak periods.[17] IXCs order trunks based on their own peak period traffic, while the amount of switching capacity required depends on overall traffic during the LEC's peak period, of which IXC access traffic is only a small portion.[18] Further, as CLECs expand, IXCs will need to order additional trunks to interconnect with CLECs, causing trunking requirements to increase relative to the amount of local switching usage.[19]

Despite the added complexities associated with trunk-based charges as identified in the FNPRM (¶¶ 213-214), it is not clear that payments associated with trunk-based charges would differ much from those based on existing per-minute charges. According to evidence obtained from the price cap LEC tariff review plans and AT&T's internal records, growth in trunk ports tends to coincide closely with the growth in local switching minutes. *See Infra at Section III.B in q factor discussion.* Because trunking requirements depend on traffic volumes, trunk ports can be expected to grow at rates that are similar to the growth in minutes-of-use (except as noted above).

If the FCC nevertheless decides to adopt a capacity-based rate structure for local switching (which it should not), the rate relationship between DS-1 and DS-3 trunks should be similar to the relationships established for transport facilities. Because DS-3 trunks generally carry less than 28 times the traffic volume of DS-1 trunks, the DS-3 charge should be less

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17 Access Reform Order, Appendix B, ¶ 47.

18 Less than 15% of LEC traffic is interstate access. See Industry Analysis Division, Common Carrier Bureau, FCC, Trends in Telephone Service, September 1999, Table 12-1. Interstate toll traffic is only 525 billion minutes out of the total volume of 3,612 billion minutes, i.e., 14.5%.

19 As IXCs need to interconnect with more CLECs, the efficiency of existing trunking arrangements would be expected to decline. Thus, capacity-based charges for LEC

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than 28 times the DS-1 charge, as is generally the case with rates for both entrance facilities and interoffice facilities. FNPRM, ¶ 213. The Commission should not impose any requirement that incumbent LECs charge for local switching based on the DS-1 equivalent capacity of an access customer's trunks, in which case the DS-3 charge would be 28 times the DS-1 charge. FNPRM, ¶ 214. Naturally, all trunks, including local trunks, would have to be used to determine a capacity-based local switching rate. FNPRM, ¶ 213.

For the same reasons as discussed above with respect to local switching, the Commission should not modify the rate structure for tandem switching. FNPRM, ¶ 223. If the tandem switching rate remains usage-sensitive (as it should) and even if local switching rates were capacity-based, there would still be no need for the Commission to take actions to prevent larger IXCs from maintaining an inadequate number of trunks to the LEC switch and using tandem switching as an "inexpensive" alternative. FNPRM, ¶ 224. If the tandem rate is compensatory, as it should be since the local transport restructure, IXCs will not have artificial economic incentives to shift traffic to tandem switching.

Even if capacity-based switching charges were appropriate (and they are not), LECs should not be permitted to develop their own capacity-based rate structures to be reviewed during the tariff review process. The Commission must ensure that a consistent, nondiscriminatory rate structure is applied by all LECs. Moreover, any rate structure change would need to be thoroughly reviewed; the current rules for streamlined tariffs do not afford sufficient time to review and evaluate capacity-based switching rate proposals.

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switching would recover a greater share of switching costs from users that require a decreasing share of the LEC's switching capacity.

B. A Q Factor Should Be Added To The Traffic-Sensitive PCI Formula.

In the FNPRM (¶ 218) the Commission tentatively concludes that it would not be reasonable to permit incumbent LECs to retain all the benefits of growth in the traffic-sensitive basket if they are not exclusively responsible for encouraging that growth. The Commission thus invites comment on whether the traffic-sensitive PCI formula should include a "q" factor, similar to the "g" factor in the common line formula, to incorporate growth into the traffic-sensitive basket PCI.

The FCC's proposal to adjust the PCI for growth in traffic volumes represents a constructive approach to bringing local switching rates closer to their underlying costs and should be adopted, regardless of whether the local switching rate structure remains usage-based or is changed to a capacity-based structure. A "q" factor will properly adjust the LEC's traffic-sensitive PCI as a result of IXC-initiated growth in local switching minutes and/or trunks, while the LECs will continue to earn a reasonable profit given that unit costs decline with growth in traffic volumes.

The same reasons for including the g factor in the common line formula also support the adoption of a q factor for the traffic-sensitive basket. Recognizing that "[t]he unique characteristic of common line is that costs do not vary at all with changes in demand"[20] and "a LEC's marginal cost of providing an additional minute of service over common line facilities approaches zero,"[21] the FCC concluded (when it initiated price cap regulation) that it needed to adopt a formula for the common line basket PCI to reflect that common line rates

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20 Policy and Rules Concerning Rates for Dominant Carriers, Report and Order and Second FNPRM, 4 FCC Rcd 2873, ¶ 723 (1989) (LEC Price Cap SFNPRM).

21 LEC Price Cap SNPRM, ¶ 717.

are traffic-sensitive even though common line costs are nontraffic-sensitive.[22] A growth (g) factor was included in the common line PCI to address "the problems of setting a price cap for the carrier common line rate" that "stem from attempting to use a per minute charge to recover a fixed cost."[23]

The facts are similar in the traffic-sensitive basket. Demand growth results mainly from the efforts of IXCs rather than those of the LECs. Moreover, most of the revenue in the traffic-sensitive basket comes from local switching, the costs of which tend not to increase with growth in traffic. Despite substantial growth in local switching minutes over time – 66% growth from 1991 to 1998 for the RBOCs – expenses and investments associated with local switching in ARMIS have declined substantially over time.[24] As a result, the RBOCs' rate-of-return for local switching has been rising steadily, increasing from 13% in 1990 to 52.5% in 1998.[25]

Regardless of whether the local switching rate structure remains the same or is changed to a capacity-based structure, the FCC's proposed q factor should be included in the traffic-sensitive PCI formula. Available evidence demonstrates that growth in minutes is generally accompanied by growth in trunk capacity.[26] For example, total RBOC trunk ports increased by 5.6% from 1996 to 1997 and then by 5.8% from 1997 to 1998 – nearly as much as the growth in total RBOC interstate access minutes, which increased by 6.6% and 5.8%,

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22 LEC Price Cap Order, 5 FCC Rcd at 6793.

23 Policy and Rules Concerning Rates for Dominant Carriers, Supplemental NPRM, 5 FCC Rcd 2176, ¶ 25 (1990) (LEC Price Cap Supplemental NPRM).

24 See Attachment A (p. 1), which shows that minutes grew from 246.7 billion in 1991 to 409.0 billion in 1998, a 66% increase, and Attachment B.

25 See Attachment C.

26 See Attachment D.

respectively.[27] These general results are confirmed by AT&T's own experience that growth in trunks tends to mimic the growth in traffic volumes. A q factor is thus needed to adjust for growth in billed units under *either* a minutes-based or trunk-based rate structure. Moreover, inclusion of a q factor in the traffic-sensitive PCI formula would accommodate differences among LECs, with those LECs that experience the most growth in usage being required to offer additional price reductions.

C. A One-Time Adjustment Should Be Made To The Traffic-Sensitive Basket PCI.

The Commission acknowledges that the existing per-minute rate structure for local switching provides an incumbent LEC with more revenue whenever per-minute demand increases, regardless of whether the LEC's costs have increased. This revenue increase results in higher earnings for the LEC, regardless of whether it has become more productive in its provision of local switching. Accordingly, the FNPRM (¶ 222) asks whether the Commission should require a one-time downward adjustment of the LECs' traffic-sensitive PCIs to correct for any imbalance on a going-forward basis, similar to the X-Factor adjustments required in the Price Cap Performance Review Orders.[28]

LECs should be required to reduce their PCIs to the levels that would have resulted had the FCC incorporated a q factor in the traffic-sensitive PCI at the inception of price caps in 1991.[29] As noted in the FNPRM (¶ 222), "using per-minute charges without

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27 Data on trunk ports were obtained from Tariff Review Plan ("TRP") Rate Element Detail files associated with the January 1, 1998, January 1, 1999 and July 1, 1999 access filings. Interstate access minutes from FCC Statistics of Communications Common Carriers, Table 2.20.

28 See, e.g., Price Cap Performance Review Order For Local Exchange Carriers, CC Docket No. 94-1, 12 FCC Rcd 16642, ¶ 179 (1997) (1997 Price Cap Performance Review Order).

29 A similar term could also be added to price cap formula for the trunking basket, based on growth in tandem switching minutes.

simultaneously using a q factor may have exacerbated [the] imbalance" (between the interests of IXC customers and LEC stockholders), and such an imbalance remains "embedded in the incumbent LECs' traffic-sensitive PCIs." Price cap indices should thus be adjusted, or "reinitialized," as if the new growth adjustments had been in effect since 1991. Attachment A (p. 2) shows the impacts on RBOC local switching revenue and the local switching earnings ratio that would have resulted from adjusting 1998 rate levels for the growth that has occurred since 1990, based on the growth in minutes per switch.[30] This adjustment would have resulted in an average earnings ratio of about 14% for local switching in 1998 – substantially less than the 52.5% realized by the RBOCs, but still quite profitable.

IV. OTHER LIMITED MODIFICATIONS TO THE PRICE CAP MECHANISM, INCLUDING A FULL G FACTOR OR REVENUE PER LINE CAP FOR THE COMMON LINE BASKET, SHOULD BE ADOPTED.

As proposed in the FNPRM, the Commission should adopt a full g factor or revenue per line cap for the common line basket and make a one-time adjustment to the common line basket PCI.

A. The Common Line Price Cap Formula Should Be Modified So That The Common Line Revenue Requirement Is Permitted To Increase With The Average Growth Rate Of Total Lines.

The Commission correctly acknowledges that the access reform rules have not eliminated per-minute CCL charges for some companies as quickly as anticipated and requests comment on whether the "g" factor in the common line PCI formula should be

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30 The general approach for adjusting the traffic-sensitive PCI for growth can be characterized by the following formula for updating the PCI:

$$PCI(t) = PCI(t-1)[1 + GDPPI - X - q],$$

where q is the growth in local switching volume.

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increased from "g/2" to a full "g." FNPRM, ¶ 227. The FCC's concerns about whether the g factor, as well as the multiline business ("MLB") PICC, generate the appropriate amount of revenue can be addressed by capping common line rates on a revenue per line basis, thereby permitting "common line revenue to increase with the average growth rate of all common lines." FNPRM, ¶ 233.

A mechanism for capping common line rates on a revenue per line basis should be adopted. For one, a revenue per line cap would be consistent with the FCC's long range objective of recovering common line costs on a flat-rated rather than usage-sensitive basis.[31] Moreover, such a cap would eliminate the need for a "g factor" in the common line formula. Capping revenue on a per line basis is equivalent to increasing the g factor to a full g. With revenues capped on a per line basis, any increase in CCL minutes per line would have to be offset by reducing the CCL rate in order to prevent CCL revenue per line from increasing.

It is beyond dispute that common line costs vary mainly with the number of subscriber lines rather than with usage on those lines. Indeed, the Commission has repeatedly acknowledged that "[t]he unique characteristic of common line is that costs do not vary at all with changes in demand,"[32] and "a LEC's marginal cost of providing an additional minute of service over common line facilities approaches zero."[33] The Commission thus recognizes "the problems of setting a price cap for the carrier common line rate" that "stem from attempting to use a per minute charge to recover a fixed cost."[34]

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For example, if billed volume (e.g., minutes) grows by 8% annually, q is 8%, and the effect of the growth adjustment is to reduce the PCI by an extra 8%. (Further details regarding the implementation of such a mechanism are explained in Attachment E).

31 See, e.g., Access Charge Order, 93 F.C.C.2d at 268-269.

32 LEC Price Cap SFNPRM, ¶ 723.

33 LEC Price Cap SFNPRM, ¶ 717.

34 LEC Price Cap Supplemental NPRM, ¶ 25.

The Commission also concluded in its price cap review proceedings that LECs have little influence on the growth of common line usage, stating that ". . . this [common line] usage appears to be almost totally a function of the price, quality, and marketing of IXC services as well as general economic trends."[35] The Commission went on to say "[t]he foregoing conclusions suggest that it is not necessary to create price cap incentives for LECs to increase growth in common line usage, because they have little influence over such growth. Instead, our analysis indicates that price cap CCL rates should be adjusted to reflect trends in common line usage in order to give IXCs an incentive to increase that usage."[36]

Despite its conclusions that common line costs do not vary with usage and that growth in usage is influenced almost totally by IXCs, in light of its pending rulemaking regarding the adoption of a productivity factor based on total factor productivity ("TFP"), the Commission "tentatively" decided to continue with the g/2 formula, where LECs and IXCs each receive 50% of the benefit of growth in common line usage as opposed to IXCs receiving the full benefit of this growth.[37] The Commission has not affirmatively upheld its 50-50 common line formula in any of its recent price cap orders.[38] Indeed, as a result of 1995 and 1997 price cap

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35 Price Cap Performance Review Order For Local Exchange Carriers, CC Docket No. 94-1, 10 FCC Rcd 8691, ¶ 267 (1995). (1995 Price Cap Performance Review Order).

36 Id., ¶ 269.

37 Id., ¶ 271.

38 In its 1995 Price Cap Performance Review Order, the Commission concluded "that the per-line formula properly recognizes that loop costs are not traffic-sensitive" (¶ 270) and reached the tentative conclusion "that the per-line formula is superior to the per-minute and 50-50 formulas for the long term" (¶ 271). Because the Commission adopted only an interim plan in its 1995 order, it declined to change the 50-50 formula, however, deferring the issue until it decided on a long term plan. In its 1997 order in Docket 94-1, the Commission once again declined to revise the 50-50 formula, on the grounds that the formula would no longer be used once the CCLC was phased out as a result of the access reform order and a desire not "to create any unnecessary rate churn" in the interim. 1997 Price Cap Performance Review Order, ¶ 109. However, as the Commission notes in the FNPRM (¶ 226), "[t]he transition away from per-minute CCL charges...is progressing

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performance review orders, the 50-50 formula has been retained largely as a matter of default. The time has come to finally dispose of this issue and give IXCs the benefit of per minute growth.

In addition to its other infirmities, the 50-50 formula creates inequities between those LECs that impose a relatively high CCL charge versus those LECs with a low or no CCL charge. Under the current common line price cap formula, growth in SLC and PICC revenue is a function of the growth in subscriber lines, while growth in CCLC revenue is equally a function of growth in both lines and minutes. Because minutes have been increasing by more than lines, those LECs with the highest CCL rates tend to realize more growth in revenue over time than LECs with low or no CCL rates. The current formula thus confers an unwarranted windfall on those LECs that still charge the CCLC, which generally tend to be the LECs with the highest interstate access rates. It is therefore not surprising that LECs with high CCL rates tend to have higher earnings.[39]

A revenue per line cap would also ensure that MLB PICCs recover the appropriate amount of revenue. The FNPRM (¶ 230) notes that primary residential and single-line business lines currently receive a subsidy from multiline business lines via the PICC, and correctly observes that "this subsidy increases disproportionately if multiline business lines grow more quickly than single-line business and primary residential lines." The FNPRM

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slowly for certain incumbent LECs" and its "access reform rules have not eliminated per-minute CCL charges for some companies as quickly as....anticipated." Id., ¶ 227.

39 For example, GTE and GSTC (Contel) had rates-of-return on interstate access (without USF flowback) of 17.7% and 23.4%, respectively, in 1998. Their rates-of-return for the common line category (with flowback revenue removed) were among the highest for price cap LECs.

(¶ 232) presents an example that shows how the high growth in multiline business lines results in increasing permitted revenue per line, thereby conferring a windfall upon the LEC.[40]

The growth rate of the amount received through the MLB PICC subsidy ideally should be equivalent to the growth rate of primary residential and single-line business lines. The PICC subsidy, however, will grow too quickly or too slowly whenever the lines giving a subsidy, multiline business lines, grow at a different rate than the lines receiving the subsidy, single-line business and primary residential lines. This subsidy increases disproportionately if multiline business lines grow more quickly than single-line business and primary residential lines. This subsidy fails to keep up with line growth if multiline business lines grow less quickly than single-line business and primary residential lines.

In recent years, multiline business lines have grown far more quickly than single-line business and primary residential lines. The Commission suggests that revising the common line formula in Section 61.46(d)(1), so that permitted common line revenues increase with the average growth rate of all common lines, would eliminate the windfall or shortfall that now occurs whenever multiline business lines grow faster or slower than primary residential and single-line business lines. AT&T agrees.

AT&T supports the Commission's proposal to change the common line formula and eliminate this windfall or shortfall. The Commission's objective as stated in the Access Reform Order is that all classes of lines should recover the average common line revenue per

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40 PICCs on single-line business and primary residential lines were set initially so that the sum of the PICC and SLC applicable to each of these lines was less than the average revenue per line permitted under the price cap rules. Those PICCs will increase until the sum of the applicable PICC and SLC is equal to the maximum permitted revenue per line. During the interim, price cap LECs are allowed to recover this shortfall through PICCs on multiline business lines. As a result, single-line business and primary residential lines receive a subsidy from multiline business lines during this interim period. Access Reform Order, ¶¶ 99-102; Reconsideration Order, ¶ 15.

line.[41] However, contrary to this objective, most LECs are charging a higher price than the average revenue per line for multiline business and non-primary lines and a lower price than the average revenue per line for primary residential and single-line business lines. The higher priced multiline business and non-primary lines are growing at a faster rate than the lower priced primary residential and single-line business lines. This has resulted in the LECs' maximum permitted common line revenues growing at a faster rate than if all classes of lines were priced at the average revenue per line as the Commission intended.[42] With a revenue per line cap, the amount of revenue obtained from subsidy elements – i.e., the MLB PICC and CCLC – is equal to the shortfall in revenue per line collected from single-line business and primary residential lines.[43] The Commission should adopt the revenue per line cap for the common line basket and eliminate the existing windfall.

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41 Access Reform Order, ¶¶ 94, 102.

42 This windfall/shortfall situation can also be corrected by eliminating or minimizing the subsidy that primary residential and single-line business lines receive from multiline business and non-primary lines. For example, the CALLS proposal (section 2.1.2.2.1) increases the maximum monthly charge for each primary residential and single-line business line to $5.50 beginning on January 1, 2000 with additional increases up until July 1, 2003 at which time the maximum monthly charge for these lines will be $7.00. These increases will allow these lines to recover the average revenue per line for the majority of LECs, so that primary residential and single-line business lines will no longer need to receive a subsidy from multiline business and non-primary lines, thereby eliminating any concern of windfalls or shortfalls resulting from this subsidy.

43 A revenue per line price cap mechanism can be implemented as follows:

1. Calculate existing common line revenue per line using current (June 30) rates and prior base year demand quantities. (In the CALLS proposal, marketing and residual TIC revenue, both of which are recovered from common line rate elements, are also included in the capped revenue per line amount.)
2. Revenue per line is adjusted by the change in PCI (calculated without the g factor, which would no longer be needed) at each annual filing. In this manner, revenue per line is adjusted to reflect inflation (GDP-PI), the X-Factor, and exogenous costs, but is not affected by changes in the relative numbers of MLB vs. SLB/PRL lines.
3. The adjusted revenue per line is multiplied by the current base year number of lines to obtain the new permitted price cap revenue.
4. Permitted revenue is then recovered from SLC, PICC, and CCL rates as calculated in the CAP-1 form of the TRP.

As an alternative to capping total common line revenue on a per line basis, the Commission can achieve similar results by using a full "g" in the common line PCI formula and adding the requirement that a LEC's total revenue from SLCs and PICCs be capped on a per line basis. This requirement can be satisfied by modifying the calculation of "maximum common line revenue at the last PCI update" in the annual filings.[44] These calculations ensure that common line revenues recovered by per line rates will increase by the average growth of all lines, as the Commission has proposed.

B. A One-Time Adjustment Should Be Made To The Common Line Basket PCI.

The LECs should be required to reduce their PCIs to the levels that would have resulted had the FCC incorporated a full g factor in the common line PCI formula that took effect in 1991. The same considerations that currently warrant instituting a full g, or cap on revenue per line, were also applicable back in 1991 when price cap regulation was first adopted. Ratepayers are entitled to the benefit of a full g factor back to 1991, just as they are entitled to the benefit of a full g currently. For similar reasons, a further one-time adjustment is also needed to remove the impact of multiline business lines having grown at a faster rate than primary residential and single-line business lines since January 1998.

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[44] The following modified calculations would be required:
1. Calculate existing SLC plus PICC revenue per line based on current (June 30) rates and prior base year demand quantities.
2. Multiply the revenue per line amount by current base year demand to obtain the maximum allowable SLC plus PICC revenue at the last PCI update.
3. Add revenue from other common line rate elements (June 30 rates times base year demand) to obtain maximum common line revenue at the last PCI update.
4. Adjust this amount by the PCI change, calculated with a full g, to obtain the new permitted price cap revenue.

V. PERMISSIVE DETARIFFING OF CLEC ACCESS CHARGES IN EXCESS OF ILEC RATE LEVELS WILL BEST SERVE THE COMMISSION'S GOALOF FOSTERING MARKET-BASED CONSTRAINTS ON RATES.

In its Fifth Report, the Commission also addressed AT&T's petition filed October 23, 1998 for a declaratory ruling confirming that under existing Commission rules and policies an IXC may elect not to purchase switched access services offered by CLECs.[45] As AT&T showed there,[46] and as the Commission itself has previously recognized,[47] these carriers possess powerful locational monopolies that insulate their rates from marketplace forces that might otherwise constrain their switched access pricing.[48] Although the Commission initially declined to regulate CLEC switched access rates, in the expectation that ILEC rates would discipline the rate levels of their putative "competitors," it made clear that it would revisit that conclusion if the events showed that CLECs are nonetheless imposing unreasonable access charges on IXCs.[49]

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45 Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers, CCB/CPD 98-63, Public Notice, DA 98-2250, released November 5, 1998.

46 AT&T Petition at 7-9; AT&T Reply, filed December 22, 1998, at 5-12.

47 Access Reform Order, ¶ 364.

48 See id., 12 FCC Rcd at 16141-42; Fifth Report ¶ 185 & n.465. While the Commission has expressed particular concern about the absence of effective marketplace constraints on CLECs' terminating access rate levels, it is likewise apparent that current market controls on those carriers' originating access rates are no more effective. For example, the appendices to AT&T's Declaratory Ruling Petition and Reply compared CLEC and ILEC originating access rates and showed that the former were as much as 1314% higher than the incumbents' corresponding charges. Significantly, while the CLECs raised various cavils regarding the computations of their charges, which the Fifth Report (¶ 187) found could not be resolved in the context of a declaratory ruling, none of those carriers demonstrated that its switched access rates were even equal to – much less below – the access charges of the ILEC in the same service territory.

49 See Access Reform Order, ¶ 342.

AT&T's Petition demonstrated that, contrary to the Commission's original expectations, a substantial number of CLECs have sought to tariff switched access rates at supracompetitive levels, i.e., in excess – and often far in excess – of the ILEC levels in the same service territories served by those CLECs. Moreover, based on their interpretations of the "filed tariff doctrine," these carriers have then asserted that AT&T and other IXCs are legally required to accept their switched access services and to pay their filed rates for the CLECs' switched access, no matter how excessive they may be – even where the IXC has not ordered such services from them. The Commission in the Fifth Report (¶ 189) agreed that, in light of the record compiled on the declaratory ruling petition, it should revisit its previous conclusions regarding the reasonableness of CLEC access rates. It also concluded (id., ¶ 88), in the exercise of the Commission's discretion, that these issues were better addressed in the context of a notice-and-comment rulemaking than through a declaratory ruling, and carried them over to the instant FNPRM.

The FNPRM correctly reaffirms the Commission's longstanding commitment to rely upon marketplace forces, in lieu of regulation, as the principal means for constraining rates.[50] Based on the current record, however, the Commission acknowledges (¶ 238) that it "may have overestimated the ability of the marketplace to constrain CLEC access rates." Although additional intervention is needed, the FNPRM proposes a variety of unduly complex, costly, and burdensome regulatory approaches to constrain CLEC pricing. In fact, there are simpler alternatives that would improve the effectiveness of marketplace forces, consistent with the Commission's preferred policy.

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[50] See FNPRM, ¶ 256 ("We strongly prefer not to intervene in the marketplace. . . unless intervention is necessary to fulfill our statutory obligation to ensure just and reasonable rates"); id., ¶ 238 (noting the Commission's preference "to seek a marketplace solution that might constrain CLEC access rates").

For example, the FNPRM seeks comment (¶¶ 250-252) on the desirability of adopting an nationwide plan to assess the difference between a CLEC's supracompetitive terminating access rate and a reasonable access charge upon the customer placing a call. As the FNPRM necessarily concedes (id.), no remotely similar "calling party pays" regime has to date been adopted except on a limited basis for some wireless services, and the Commission lacks information as to the cost and time required broadly to implement this procedure and related methods for notifying calling parties that they will be subject to such CLEC terminating access charges. Although the Commission should not preclude carriers from implementing such arrangements if they so elect, it likewise should not needlessly impose such an immensely complex scheme upon the entire industry.

As another alternative, the FNPRM (¶ 253) suggests mandating that CLEC originating and terminating access rates be set at the same levels. However, in view of the CLECs' bottlenecks for both originating and terminating access shown above, the benefit of any such "linking" between these access rates would be illusory.

Further, the Commission seeks comment on mandatory detariffing of all CLEC access charges. FNPRM, ¶ 246. As the Commission correctly points out (id.), such a procedure would effectively obviate the CLECs' present attempts to rely on the filed tariff doctrine to avoid negotiating with IXCs to reach agreement on mutually acceptable access charges.[51] While detariffing may restore marketplace constraints on CLEC access rates that are now lacking, it would also impose substantial, unnecessary burdens on both CLECs and their

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[51] The CLECs' overreaching and unfounded interpretation of the filed rate doctrine, rather than the doctrine itself, lies at the heart of the problem addressed by the FNPRM. As AT&T has already demonstrated (and as the Common Carrier Bureau has already acknowledged), an IXC is free to refuse a CLEC's switched access service even when the latter has tariffed that service. See AT&T Petition at 6-7; AT&T Reply at 8-12;

(footnote continued on following page)

access customers by invariably requiring them to negotiate contractual access arrangements in lieu of tariffs – even where the CLEC offers rates that are no higher, and possibly even lower, than ILEC rate levels. In the latter circumstances, both CLECs and IXCs may well prefer relying upon the convenience of the tariff mechanism. The mandatory detariffing proposal suggested in the FNPRM is thus far broader and more burdensome than required to achieve the goals of this proceeding, and raises other serious questions that are now pending on appeal.[52]

In sum, none of the proposals suggested in the FNPRM can be reconciled with the Commission's stated objective (FNPRM, ¶ 256) of using "the least intrusive means possible to correct any market failures" that affect CLEC access rates.[53] Instead, the Commission's objective can be fully served by encouraging CLECs to detariff their access charges, particularly where their rates exceed the corresponding ILEC charges in the same service area, thus leaving it for CLECs that elect to charge such supracompetitive rates to negotiate mutually acceptable arrangements with IXCs that desire to use their services.

Modifying the Commission's proposals in this manner will allow CLECs that choose to offer competitive access rates, and the IXCs that obtain access services from them, to rely

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MGC Communications, Inc. v. AT&T Corp., File No. EAD-99-002, Memorandum Opinion and Order, DA 99-1395, released July 16, 1999(Co. Car. Bur.),¶¶ 8-12.

52 See MCI Telecommunications Corp. v. FCC, No. 96-1459 (D.C. Cir. filed Nov. 7, 1997).

53 In addition to these proposals, the FNPRM (¶¶ 244-245) seeks comment on whether allowing IXCs to geographically deaverage their end user rates to reflect differences between the access rates levied by their local exchange carriers could effectively redress the problem of excessive CLEC access charges. AT&T agrees that such deaveraging could potentially provide appropriate marketplace signals to originating customers, who under current geographically averaged ratesetting are insulated from the excessive access rates charged by their selected local carrier. However, it is not apparent that such deaveraging would provide similarly effective marketplace signals for traffic such as

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on a simple and streamlined tariff filing mechanism as a convenient procedure for implementing and administering those charges and related regulations. This procedure would not, however, preclude such CLECs from negotiating commercial terms with access customers who elect to purchase their access services on a detariffed basis. Such limited retention of a "permissive" tariff mechanism would maximize efficiency and convenience in administering transactions between access providers and purchasers, while preserving the opportunity for those parties proceed on a commercial, non-tariffed basis.

Concomitantly, CLECs that prefer to impose supracompetitive access rates by tariff should, as the FNPRM proposes (¶¶ 247-249), be required to justify them in traditional, non-streamlined tariff review proceedings with full cost support.[54] Application of such a tariff review mechanism will thus limit the ability of these carriers to apply the filed tariff doctrine to coerce IXCs to order and pay unjustified and inflated rates for access. This approach will also create immediate and compelling marketplace incentives for these CLECs

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toll-free 800 calls originated by end users served by CLECs with supracompetitive excessive access rates.

[54] Requirements for cost support (including historical and projected service cost studies and estimates of the tariff's effects on traffic and revenues) are specified in Section 61.38 of the Commission's Rules, 47 C.F.R. § 61.38. See also 47 C.F.R. Part 32 (specifying accounts for revenues, expenses and investments); id. Part36 (specifying jurisdictional separation of Part 32 accounts); id. Part 64 (providing for removal of nonregulated costs); id. Part 69 (specifying access rate structure). In no event, moreover, should a CLEC proposing rates above the ILEC level in the same service area be permitted rely upon any "proxy" for its own costs (such as studies for NECA or another ILEC). Rather, the Commission should require CLECs to provide studies that reflect their own cost characteristics. For example, many CLECs serve only a few office parks or other sites in a wider geographic area, and impose minimum purchase commitments (such as 24 loops) on their customers; generic cost studies for the larger service area are unlikely to reflect these limitations in the CLEC's service.

to negotiate with their IXC customers to reach mutually acceptable detariffed arrangements for provision of access service.[55]

Finally, unlike the complex proposals described in the FNPRM, a permissive detariffing alternative can be implemented rapidly, and will directly affect only the minority of CLECs that insist on maintaining supracompetitive access rate levels. Thus, AT&T's proposal will provide immediate, and narrowly focused, relief from CLEC abuses of those carriers' access bottlenecks.

Accordingly, AT&T urges the Commission to dispense with the proposals addressed in its FNPRM, and instead to adopt AT&T's alternative described in these comments.

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[55] As the Common Carrier Bureau has already expressly recognized, IXCs are not obligated to order originating switched access from CLECs under tariff. See MGC Communications, Inc. v. AT&T Corp., supra. The FNPRM cites no legal basis for permitting or requiring any different result for terminating switched access service, and it is apparent that there is none. For example, Section 214 of the Communications Act (which the Commission has in all events forborne as to nondominant IXCs) has never been read to require a carrier to extend service into a given area. Similarly, Section 201(a) of the Act does not obligate carriers to establish a "through route" (i.e., physical interconnection) absent a Commission directive following a hearing; even then, Section 201(a) does not obligate a common carrier to purchase another carrier's services, as the CLECs attempt to claim. Accordingly, the Commission should confirm in this proceeding that, in the absence of an affirmative access order from an IXC for specific switched access services – e.g., presubscribed traffic, "dial-around" (1010XXX) calls, 8YY or other traffic – a CLEC may not route such traffic to an IXC's network or assess switched access charges for such traffic upon that IXC.

CONCLUSION

For these reasons, the Commission should allow LECs to deaverage their common line rates only once certain prerequisites have been met; allow Phase II pricing flexibility for switched services only upon a showing of substantial competition sufficient to curtail a LEC's market power; adopt the proposed q factor and g factor (revenue per line cap) modifications; make one-time downward adjustments to the traffic-sensitive and common line baskets' PCIs; and require CLECs whose rates exceed the incumbent's to justify those charges on a non-streamlined basis with full cost support or proceed on a detariffed (contractual) basis.

Respectfully submitted,

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GROWTH ADJUSTMENTS FOR LOCAL SWITCHING RATES
(Based on aggregate RBOC data)

	Interstate Access Min. (millions)	Local Switches	Minutes Per Switch (millions)	Growth in Min./switch (Q)	Earnings Ratio
1990	231,960	9739	23.818		13.0%
1991	246,710	9829	25.100	5.38%	15.1%
1992	262,188	9905	26.470	5.46%	21.6%
1993	278,173	9912	28.064	6.02%	31.9%
1994	298,342	9861	30.255	7.81%	37.4%
1995	334,982	9883	33.895	12.03%	40.9%
1996	362,603	9768	37.121	9.52%	43.8%
1997	386,567	9733	39.717	6.99%	48.7%
1998	408,988	9579	42.696	7.50%	52.5%
			Average:	**7.57%**	

Sources of data:

1) Interstate access minutes from FCC Statistics of Communications Common Carriers, Table 2.20.

2) Number of local switches from ARMIS 43-07 (Row 111), as reported in BPI (Business Planning, Inc.) Infrastructure Database 1999.

GROWTH ADJUSTMENTS FOR LOCAL SWITCHING RATES
(Based on aggregate RBOC data)

Impact of reinitializing local switching rates based on growth adjustment:				
Scenario	Average Annual Reduction A = Q/(1+Q)	Rate Adjustment Factor B = (1-A)^8	Local Switching Revenue C2 = B*C1	Local Switching Earnings Ratio [D+(1-G)(C-C1)]/E
1. No adjustment	0	1.0000	$2,798,143	52.5%
2. Full adjustment	7.04%	0.5578	$1,560,914	14.0%

Annual growth adjustment = 1 - Q/(1+Q)
Reinitialization based on 8 annual growth adjustments from 1991 to 1998,
Each growth adjustment reduces the LS rate by growth in minutes per switch based on the above formula.

RBOC return data for 1998:

Net return (D)	$1,012,108
Avg. net investment (E)	$1,927,085
Assumed marginal tax rate (G)	0.4

Sources of data:

1) Local switching data is for the "Traffic Sensitive-Switching" category (Column J) in ARMIS 43-04: Revenue - Row 4014, Avg. net investment - Row 8040, Net return - Row 8044, Earnings ratio - Row 8045 as reported in BPI (Business Planning, Inc.) Access Database (1999 edition) and the FCC ARMIS website.

LOCAL SWITCHING EXPENSES AND INVESTMENT								
($Thousands)								
		1992	1993	1994	1995	1996	1997	1998
Total operating expenses and taxes								
	Ameritech	$226,290	$200,652	$182,398	$158,658	$158,802	$157,148	$148,669
	Bell Atlantic North	$318,489	$286,632	$287,541	$263,211	$255,494	$256,700	$210,093
	Bell Atlantic South	$265,854	$174,867	$239,810	$236,653	$244,271	$219,618	$199,585
	BellSouth	$230,561	$217,773	$216,853	$218,878	$209,198	$201,678	$159,770
	SBC (SWBT)	$140,708	$119,225	$119,689	$122,049	$126,458	$131,232	$119,718
	SBC (PacTel)	$182,826	$157,502	$134,072	$132,839	$134,115	$141,943	$113,101
	US West	$209,644	$194,139	$208,819	$220,103	$222,699	$200,670	$137,888
	Total RBOC	**$1,574,372**	**$1,350,790**	**$1,389,182**	**$1,352,391**	**$1,351,037**	**$1,308,989**	**$1,088,824**
Average net investment								
	Ameritech	$444,244	$412,846	$336,614	$315,796	$314,607	$316,045	$314,277
	Bell Atlantic North	$609,434	$514,870	$477,565	$471,224	$473,342	$448,632	$326,218
	Bell Atlantic South	$564,692	$354,747	$473,782	$507,734	$499,124	$473,639	$311,609
	BellSouth	$499,222	$465,171	$445,909	$439,382	$439,766	$407,085	$310,867
	SBC (SWBT)	$331,461	$295,870	$276,472	$297,773	$287,384	$274,175	$138,274
	SBC (PacTel)	$359,764	$310,024	$271,725	$274,057	$290,356	$300,317	$208,604
	US West	$501,614	$462,338	$450,144	$479,523	$479,484	$413,045	$232,016
	Total RBOC	**$3,310,431**	**$2,815,866**	**$2,732,211**	**$2,785,489**	**$2,784,063**	**$2,632,938**	**$1,841,865**
Sources of data:								
	Total operating expenses and taxes from ARMIS 43-04, row 7351, column J.							
	Average net investment form ARMIS 43-04, row 8040, column J.							
	ARMIS data obtained from BPI (Business Planning, Inc.) Access 1999 database.							

ATTACHMENT C

LOCAL SWITCHING RATE-OF-RETURN

COMPANIES	1990	1991	1992	1993	1994	1995	1996	1997	1998
Ameritech	11.97%	13.32%	12.9%	22.3%	31.4%	44.2%	51.4%	53.3%	43.9%
Bell Atlantic North	13.09%	17.59%	33.4%	50.5%	58.7%	67.4%	68.6%	71.5%	79.3%
Bell Atlantic South	12.99%	12.23%	17.7%	21.0%	25.5%	26.3%	26.7%	33.2%	29.2%
BellSouth	14.05%	14.91%	20.9%	34.0%	39.5%	42.3%	45.9%	57.7%	67.8%
SBC (Pacific Bell)	13.55%	14.45%	22.0%	32.7%	45.9%	45.9%	48.0%	37.4%	31.3%
SBC (Nevada Bell)	14.70%	NA	21.3%	34.5%	37.6%	39.6%	41.2%	47.8%	56.5%
SBC (SWBT)	12.46%	16.11%	15.4%	25.3%	32.4%	32.8%	37.0%	51.6%	74.5%
US West	12.72%	16.85%	19.9%	24.1%	24.5%	25.0%	29.5%	38.8%	55.7%
Aliant			11.8%	20.5%	28.1%	31.8%	33.3%	37.5%	39.5%
CBT			15.4%	12.5%	20.0%	26.9%	30.7%	37.9%	21.9%
Frontier (Rochester)			24.8%	21.8%	18.9%	13.1%	22.7%	24.7%	42.9%
GTE (CONTEL)			5.6%	18.2%	19.1%	19.7%	26.5%	32.4%	27.4%
GTE			17.6%	22.7%	29.1%	34.0%	39.7%	45.3%	45.8%
SBC (SNET)			24.2%	31.8%	34.4%	41.9%	42.0%	55.4%	47.3%
Sprint (CENTEL)			12.4%	16.1%	23.1%	31.6%	31.9%	29.3%	19.6%
Sprint (United)			17.8%	22.8%	33.7%	36.4%	35.1%	32.6%	32.0%
Total RBOC	**13.03%**	**15.14%**	**21.6%**	**31.9%**	**37.4%**	**40.9%**	**43.8%**	**48.7%**	**52.5%**
Total LEC*			**20.5%**	**29.6%**	**35.1%**	**38.7%**	**42.0%**	**46.7%**	**49.1%**

***Includes all price cap LECs except Citizens, for which BPI data is incomplete.**

Source: ARMIS 43-04 (Row 8045, Column J) as reported in BPI (Business Planning, Inc.) Access Database (1999 edition) for 1992-1998. Data for 1990 and 1991 obtained from FCC ARMIS website.

ATTACHMENT D

TRUNK PORT DEMAND SUMMARY

COMPANY	RATE ELEMENT	UNITS DS0/DS1	1996 DEMAND	1997 DEMAND	Yr/Yr Growth	1998 DEMAND	Yr/Yr Growth
Ameritech	End Office Dedicated Trunk Ports	DS1	116,244	159,011	36.79%	129,736	-18.41%
Bell Atlantic-S	Dedicated Trunk Port	DS0	3,711,120	3,687,372	-0.64%	4,005,158	8.62%
Bell Atlantic-N	Dedicated Trunk Port	DS0	2,788,416	2,875,635	3.13%	3,008,330	4.61%
Bell South	Dedicated EO Trunk Port DS0/VG	DS0	234,679	162,370	-30.81%	189,268	16.57%
Bell South	Dedicated EO Trunk Port DS1	DS1	201,542	201,813	0.13%	202,282	0.23%
Pacific Bell	Dedicated Trunk Port	DS0	997,346	1,086,069	8.90%	2,215,607	104.00%
Nevada Bell	Dedicated Trunk Port	DS0	60,994	58,276	-4.46%	42,286	-27.44%
Southwestern Bell	Dedicated Trunk Port	DS0	2,037,956	2,016,106	-1.07%	2,186,657	8.46%
US West	E O Dedicated Trunk Port, Per Trunk for Trkside Svcs.	DS0	2,813,523	2,859,101	1.62%	3,035,925	6.18%
Total RBOC	Total DS0 Equivalent Trunk Ports	DS0	20,270,898	21,404,705	5.59%	22,651,663	5.83%
Total RBOC	Total Interstate Access Minutes (millions)		362,603	386,567	6.61%	408,988	5.80%

Sources of data:

1) Data on Trunk ports obtained from Rate Detail Files in TRPs associated with January 1, 1998, January 1, 1999 and July 1, 1999 interstate access filings.

2) Interstate access minutes from FCC Statistics of Communications Common Carriers, Table 2.20.

Q FACTOR GROWTH ADJUSTMENT FOR THE TRAFFIC-SENSITIVE PCI

The formula for the q factor shown in the text illustrates a general approach that can be further refined in various ways.

First, if the formula had the same format as the current common line formula, it would be written as:

$$PCI(t) = PCI(t-1)[1 + w[(GDPPI - X - Sq)/(1+Sq)] + Z/R],$$

where q is analogous to the g term in the common line formula, and S is an optional factor that represents the fraction of total revenue in the traffic-sensitive basket associated with local switching. If the q adjustment is intended to apply only to the local switching portion of the traffic-sensitive basket, the S factor can be included to scale down the impact of the q factor.

The FNPRM (¶ 220) requests comment on definition of the q factor. Because adoption of a q factor would have the effect of controlling the growth in LEC revenues (and from the IXC perspective, the growth in access costs), the q factor should be based on growth in billed volumes, as growth in revenue is directly related to the growth in billed volumes. Thus, if local switching is billed on a per minute basis, q should refer to the growth in local switching minutes. If local switching is billed via several rate elements (e.g., minutes, trunks, lines, etc.), q should be calculated as a weighted average of the growth rates for each local switching rate element in the basket. That is, the growth rate of each element would be weighted by its respective share of local switching revenues. If the growth adjustment is applied to the entire basket, q could be based on the average growth rate for all rate elements in the basket. For the purpose of reinitializing PCIs, q should be based on whatever rate elements were in effect since 1991, i.e., mainly per-minute charges.

Another possibility is that q could be calculated as growth in volume *per switch*, just as the g factor refers to growth in minutes *per subscriber line*. This approach would recognize that costs are likely to increase with the number of switches and would accommodate those LECs that need to add switches in order to handle increasing traffic volumes.