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FEDERAL COMMUNICATIONS COMMISSION
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Before the
Federal Communications Commission
Washington, DC

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
	)	
Low-Volume Long Distance Users	)	CC Docket No. 99-249
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45

Comments of Level 3 Communications, LLC

Patricia Paoletta
William P. Hunt, III
Level 3 Communications, LLC
1025 Eldorado Blvd.
Broomfield, CO 80021

Andrew D. Lipman
Tamar E. Finn
Swidler Berlin Shereff Friedman, LLP
3000 K Street, N.W., Suite 300
Washington, DC 20007

November 12, 1999

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Executive Summary

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The Commission has been discussing removing implicit subsidies from access charges for more than three years. Lowering access rates over CALLS' additional five-year glide path prolongs an already extended process. Nor does the CALLS proposal drive access charges to their cost-based rates. The CALLS rate is far above the cost-based rates for the identical function of transport and termination of local traffic. Level 3 submits that its arms-length agreement with Bell Atlantic, which reduces over a twelve-month period the price of transport and termination to an eventual rate of $0.0015, and in some instances to $0.0012, is further evidence that access rates, and the CALLS-proposed rates, are above-cost and must be reduced.

Whether traffic originates from another state or a competitive carrier across the street, the transport and termination of traffic is functionally the same. The Commission's determination that transport and termination of local traffic is distinct as a legal matter from the transport and termination of access traffic results in inefficiencies and market distortions and discriminates in favor of local traffic. Level 3 therefore urges the Commission to reject the CALLS proposal, reverse its determination that there is a legal distinction between access and transport and termination, and take immediate action to reduce incumbent LEC access rates to forward-looking cost within the next three years. The Commission could achieve this goal by utilizing its newly developed cost model, requiring incumbent LECs to mirror TELRIC-compliant rates for the identical function of transport and termination of local traffic, or requiring incumbent LECs to submit cost studies as initially contemplated by the Commission's prescriptive backstop. Finally, once access rates are brought down to forward-looking costs, Level 3 recommends that all providers of telecommunications services be subject to cost-based transport and termination charges, regardless of the type of service or the protocol used.

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Comments of Level 3 Communications, LLC

Level 3 Communications, LLC ("Level 3"), pursuant to the Notice of Proposed Rulemaking issued by the Commission, hereby submits these comments on the access charge and universal service reform proposal submitted by the Coalition for Affordable Local and Long Distance Services ("CALLS").

I. Introduction and Summary

Level 3 commends CALLS for attempting to solve a problem that has stunted the growth of competition in local markets and the deployment of advanced services since the passage of the Telecommunications Act of 1996 ("1996 Act"). As a competitive provider of innovative telecommunications and information services, Level 3 supports efforts to develop rules that promote competition in telecommunications markets and customer choice.

Reducing incumbent local exchange carriers' ("LEC") access charges to cost-based rates and making universal service support explicit are critical competitive issues. The Commission has recognized the link between access charges, universal service, and local competition, calling the three reforms part of an interdependent "competition trilogy." Because inflated access rates have historically provided implicit subsidies to incumbent LECs, the Commission has committed to removing universal service support implicit in interstate access rates. However, the Commission has neither quantified implicit support, nor removed it from incumbent LEC access rates. This has permitted incumbent LECs to reap the implicit subsidies access charges contain; discouraged competitive LECs ("CLECs") from entering residential, rural and high cost markets; unnecessarily prolonged the subsidy flow from long distance to local service; and maintained incentives to structure new technologies to take advantage of the information service provider exemption from access charges. In sum, the failure to reduce access charges to cost-based rates has postponed realization of the economic benefits promised by the pro-competitive, deregulatory 1996 Act.

Unfortunately, the solution proposed by CALLS would retard the movement of access charges to cost, as required by the Commission's own policies and internationally accepted principles, including the World Trade Organization ("WTO") Reference Paper to the basic telecommunications agreement. The Reference Paper to the Fourth Protocol of the General Agreement on Trade in Services (commonly known as the basic telecommunications agreement) provides principles on the regulatory framework for basic telecommunications services. The United States was the leading advocate of the Reference Paper and adopted it in its WTO schedule of commitments. One of those principles governs "linking with suppliers providing public telecommunications transport networks or services in order to allow the users of one supplier to communicate with users of another supplier and to access services provided by another supplier ..." The term used in the Reference Paper is "interconnection" which would apply for specific application in the United States to access charges. Such interconnection, under the principles of the Reference Paper, is to be provided by an incumbent local exchange provider "in a timely fashion, on terms, conditions (including technical standards and specifications) and cost-oriented rates that are transparent, reasonable, having regard to economic feasibility, and sufficiently unbundled..." Thus, under principles that the United States adopted, and that are internationally accepted, access charges ought to be cost-oriented, and therefore, the Commission ought to identify then remove the subsidy in access charges.

The Commission has been discussing removing implicit subsidies from access charges for more than three years. Lowering access rates over CALLS' additional five-year glide path prolongs an already extended process. Nor does the CALLS proposal drive access charges to their cost-based rates. The target rate is far above the cost-based rates for the identical function of transport and termination of local traffic. Level 3 submits that its arms-length agreement with Bell Atlantic, which reduces over a twelve-month period the price of transport and termination to an eventual rate of \$0.0015, or \$0.0012 in some instances, is further evidence that access rates, and the CALLS-proposed rates, are above-cost and must be reduced.

Whether traffic originates from another state or a competitive carrier located across the street, the transport and termination of traffic is functionally the same. The Commission's determination that transport and termination of local traffic is distinct as a legal matter from the transport and termination of access traffic results in inefficiencies and market distortions and discriminates in favor of local traffic. Level 3 therefore urges the Commission to reject the CALLS proposal, reverse its determination that there is a legal distinction between access and transport and termination, and take immediate action to reduce incumbent LEC access rates to forward-looking cost within the next three years. The Commission could achieve this goal by utilizing its newly developed cost model, requiring incumbent LECs to mirror TELRIC-compliant rates for the identical function of transport and termination of local traffic, or requiring incumbent LECs to submit forward-looking cost studies as initially contemplated by the Commission's prescriptive backstop. Finally, once access rates are brought down to forward-looking costs, Level 3 recommends that all providers of telecommunications services be subject to cost-based transport and termination charges, regardless of the type of service or the protocol used.

II. CALLS' Target Per Minute Switched Access Rate Is Too High

Interstate access charges have subsidized local exchange rates since the Commission created the system in 1983. Although the Commission has acknowledged this subsidy, there was little need to eliminate it so long as incumbent LECs retained a monopoly in their local service markets. With the passage of the 1996 Act, the national competition policy changed and the Commission was charged with implementing the pro-competitive, market-opening policies of the 1996 Act.

Throughout its competition trilogy, the Commission recognized the need to remove implicit subsidies from access charges to make local competition work. Indeed, Congress required as much when it ordered the Commission to make universal service support explicit in Section 254. Three years after passage of the 1996 Act, the Commission has failed to identify or remove the universal service subsidies inherent in access charges.

The Commission's local competition rules establish that charges assessed by incumbent LECs for transport and termination of traffic must be based on forward-looking economic cost (using the Commission's total element long-run incremental cost, or TELRIC, methodology). However, the Commission has not extended this same principle to the charge imposed for origination and termination of long-distance traffic. Instead, "access charges" continue to be governed by a complex, archaic and inefficient set of separate rules.

When it first adopted local competition rules, the Commission recognized that a LEC's transport and termination of traffic is identical in function to its delivery of exchange access traffic:

> We recognize that transport and termination of traffic, whether it originates locally or from a distant exchange, involves the same network functions. Ultimately, we believe that the rates that local carriers impose for the transport and termination of local traffic and for the transport and termination of long distance traffic should converge.[1]

[1] *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996,* CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, ¶ 1033 (1996) ("*Local Competition Order*"), aff'd in part and vacated in part sub. nom. *Competitive Telecommunications Ass'n v. FCC*, 117 F.3d 1068 (8th Cir. 1997) and *Iowa Utils. Bd. v. FCC*, 130 F.3d 753 (8th Cir. 1997), aff'd in part and remanded, *AT&T v. Iowa Utils. Bd.*, 119 S. Ct. 721 (1999).

However, the Commission also concluded that as a legal matter, termination and transport of traffic is distinguishable from exchange access:

> as a legal matter, transport and termination of local traffic are different services than access service for long distance telecommunications. Transport and termination of local traffic for purposes of reciprocal compensation are governed by 251(b)(5) and 252(d)(2), while access charges for interstate long-distance traffic are governed by sections 201 and 202 of the Act. The Act preserves the legal distinctions between charges for transport and termination of local traffic and interstate and intrastate charges for terminating long-distance traffic.[2]

Level 3 submits that it is time for the Commission to reconsider this decision. Transport and termination of local traffic is technically and operationally identical to the terminating access services provided to interexchange carriers. A carrier brings its circuits to a "point of presence" where it delivers terminating traffic to the LEC which then routes traffic over its switches and trunks to the customer whose number was dialed. The switching and routing of the call is the same whether the call originated in a foreign country, in another State, or on a competing local network across the street from the LEC's office. The only difference is the rate. Because the Commission has maintained two separate legal regimes for the same functions, the price varies based on whether the call originates from the same local calling area or from outside that local calling area.

In the three years since the 1996 Act became law, the Commission has adopted rules that required price cap LECs to reduce their access rates from an average of three cents per minute to one

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2 *Local Competition Order* at ¶ 1033.

to two cents per minute.[3] Smaller independent LECs have much higher rates that average up to 5 cents per minute. The small reductions in access rates since the 1996 Act have been achieved by the Commission's adoption of a higher productivity, or X-Factor, applied to reduce price cap LEC access rates. Yet continued use of this means to reduce rates is in jeopardy unless the Commission can devise a justification for the current X-Factor that satisfies the scrutiny of the U.S. Court of Appeals for the District of Columbia.[4] If the Commission cannot satisfy appellate review, almost four years after the 1996 Act was passed, the Commission may not have made any progress toward bringing access rates down to cost.

Even if the Commission were to justify the 6.5% X-Factor, incumbent LEC access rates are above the average cost-based rates of $0.002 to $0.004 per minute that state commissions have adopted for the transport and termination of local traffic. Even the CALLS proposed rates, $0.0055 and $0.0065, which could conceivably not be achieved until 2005, are 40 to 200 percent greater than the average TELRIC-based rate for the identical function of transport and termination.

It is bad public policy to maintain two divergent pricing schemes where the Commission has determined that the transport and termination of traffic, whether long distance or local, involves the same network functions. The distinction between access and local traffic provides incentives for

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3 *Trends in Telephone Service*, Industry Analysis Division, Common Carrier Bureau, Federal Communications Commission, Table 1.2 (Feb. 1999).

4 *United States Telephone Ass'n v. FCC*, 1999 U.S. App. Lexis 9768, No. 99-1469 (D.C. Cir. May 21, 1999); *see also United States Telephone Ass'n v. FCC*, No. 9701469 (D.C. Cir. June 21, 1999) (Order granting Commission motion to stay the mandate until April, 2000).

incumbent LECs to impose inefficient trunking configurations on CLECs (one trunk for local, a second for access); for CLECs to classify traffic as local to avoid paying higher access rates; and for all providers to classify services as information services that are exempt from access charges. The distinction between local and long distance termination can be enforced only by intrusive and expensive investigations and audits of information supplied to LECs by their customers, which in practice means they will be enforced little and then only when it suits a LEC's business purposes.

When the Commission created the system of compensation for other carriers' use of LEC networks in 1983, it found that under prior industry practice, the Bell Companies were recovering costs in a different manner for various classes of services (MTS, open end FX, CCSA, WATS and ENFIA), even though each service used the plant of the Bell Company in the same manner. In 1983, the Commission had only Sections 201(a) and 205 on which to rely to establish a system of carrier's carrier charges to remedy discrimination and preference inherent in the carrier-initiated system of compensation that proceeded Part 69 access charges.[5] Over the past 15 years, such discriminatory practices have reappeared. The regulatory regime for carrier's carrier compensation now discriminates in favor of local over long distance traffic. It is time for the Commission to revise the carrier's carrier regime to remedy this discrimination and adopt competitively neutral regulatory policies.

[5] *MTS and WATS Market Structure*, CC Docket No. 78-72, Phase I, Third Report and Order, 93 F.C.C.2d ¶¶ 36-55 (1983).

The Commission has at its disposal the tools to fix the disparity between access and transport and termination rates. Level 3 urges the Commission to reverse its prior determination that the two regimes are legally distinct and to bring access charges down to cost-based rates. Under Section 201, the Commission has substantial latitude to decide that all intercarrier compensation should mirror Section 251's pricing principles. Although Section 251(i) provides that nothing in Section 251 should limit or otherwise affect the Commission's Section 201 authority, it does not prohibit the Commission from applying Section 251's rate standard to access charges. To the contrary, Congress implicitly directed the Commission to do just that by acknowledging that the Commission would adopt regulations to supercede the then-current access charge regime.[6]

Through its universal service proceeding, the Commission has also developed a tool that could help it make the practical, economic evaluation of the forward-looking costs of transport and termination. Earlier this year, the Commission recognized that the cost model it was developing to calculate the forward-looking cost of providing supported services could also be used to determine the levels of implicit support in interstate access rates.[7] Although the Commission cautioned that the model was "developed for the purpose of determining federal universal service support,"[8] it

[6] 47 U.S.C. § 251(g).

[7] *Federal-State Joint Board on Universal Service, Access Charge Reform*, Seventh Report and Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45, Fourth Report and Order in CC Docket No. 96-262 and Further Notice of Proposed Rulemaking, FCC 99-119, ¶ 129 (rel. May 28, 1999) ("*Seventh Report and Order*").

[8] *Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, FCC 99-306, ¶ 41 (rel. Nov. 2, 1999) ("*Ninth*

acknowledged that the forward-looking cost model estimates all forward-looking costs of the loop and port (intrastate and interstate) and local number portability (interstate).[9] The model therefore already estimates the national average interstate portion of loop costs, $5.203, currently recovered through the presubscribed interexchange carrier charge ("PICC"), carrier common line ("CCL") charge, and subscriber line charge ("SLC") access charge rate elements.[10] Because the same local exchange carrier plant is used to provide both local and access service, the model could therefore be used to estimate the interstate portion of the remaining access charge rate elements.

Alternatively, the Commission could require incumbent LECs to mirror rates for transport and termination where it finds that the state commission set the rates in compliance with federal TELRIC rules. Another option would be to accelerate the prescriptive backstop and require incumbent LECs to submit cost studies to justify access rates. A third-party audit of incumbent LECs should be conducted in tandem with the cost studies. If the auditors determine that the incumbent LECs have stranded investment that cannot be recovered by forward-looking costs, the Commission could create a non-traffic sensitive recovery mechanism, limited to a reasonable period of time but no longer than five years, that would permit incumbent LECs to recover such stranded costs from all competitors seeking to terminate traffic over the LECs' exchange facilities.

Report and Order").

9 *Ninth Report and Order* at ¶ 62.

10 *Ninth Report and Order* at ¶ 63, n. 189.

III. CALLS' Five-Year Glide Path Is Not Reasonable

In its May 1997 Access Charge Reform Order, the Commission determined that market pressures would force access rates to cost. One reason it made this determination was its concern that it would be a difficult and protracted task to identify and quantify what was an implicit subsidy and what was excess profit in prescribing access charges to cost-based rates. Notwithstanding this concern, the Commission adopted a prescriptive backstop in the event market forces failed. Specifically, the Commission found that incumbent LECs would be required to submit cost studies by February 8, 2001 if access rates did not decline to cost-based levels by that date.[11] The CALLS proposal would protect incumbent access charges from further reduction until 2005, four years after the Commission's prescriptive backstop is supposed to ensure that access charges are reduced to cost-based rates. The CALLS proposal is a step backward.

Congress' directive to remove implicit subsidies from access charges, embodied in the Commission's prescriptive backstop, has been reinforced by the U.S. Court of Appeals for the Fifth Circuit:

> We are convinced that the plain language of § 254(e) does not permit the FCC to maintain any implicit subsidies for universal service support. Therefore, we will not afford the FCC any Chevron step-two deference in light of this unambiguous Congressional intent.[12]

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[11] *Access Charge Reform,* CC Docket No. 96-262, First Report and Order, 12 FCC Rcd 15982, ¶ 267 (1997) ("*Access Charge Reform Order*"), aff'd sub nom. *Southwestern Bell Tel. Co. v. FCC*, 153 F.3d 523 (8th Cir. 1998).

[12] *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d , 393 412 (5th Cir. 1999) (reversing Commission decision to require incumbent LECs to recover universal service

A plan that reduces access charges to target rates that are above costs nine years after passage of the 1996 Act is not reasonable.

IV. CALLS Largely Reshuffles Costs and Does Not Succeed in Removing Both Implicit Subsidy and Excess Profit

A close examination of the CALLS proposal reveals that it is an exercise in cost-shifting with a net result that is revenue-neutral for the incumbent LECs that participate. It eliminates the PICC and CCL only by folding them into the SLC. It reduces local switching costs by moving 25% into the SLC. In order to achieve these cost shifts, CALLS increases the cap on the residential and single line business SLC to $7.00 by July 2003 and the multiline business SLC to $9.20 on January 1, 2000. CALLS' cost shifting does nothing to address the issue of whether the costs recovered in the PICC, CCL and local switching are forward-looking cost-based rates. In other words, CALLS assumes that the costs are justified and adjusts which party is paying them. This assumption is refuted by the Commission's cost model which shows that the national averaged interstate portion of loop costs recovered in the SLC is $5.203.[13]

CALLS also assumes that the $3.50 SLC is a subsidized rate well below costs in all markets. In a declining cost industry, the SLC may not be below cost in all markets. The appropriate level of the SLC should be determined by the market, and may very well be below $3.50 in competitive markets. Rather than solidifying for the next half decade an artificial, non-market rate, the

contributions from interstate access charges).

[13] *Ninth Report and Order* at ¶ 63, n. 189.

Commission should enforce the competition provisions in the Act and its rules to create the proper environment in which a market-based SLC may be achieved.

IXCs have long argued that incumbent LEC access charges contain excessive profit in addition to implicit subsidies. Rather than shifting these costs, Level 3 urges the Commission to require cost studies to justify any increase in end user rates. Once again, the Commission has signaled its <u>intent</u> to address implicit support in access charges as part of its Access Charge Reform Docket.[14] In adopting the *Ninth Report and Order*, Commissioners Ness,[15] Powell,[16] and Tristani[17] all expressed their willingness to tackle the access charge reform issue. The Commission must act to remove the subsidies implicit in interstate access charges.

CALLS classifies $650 million of current access charges as implicit universal service subsidies and proposes to move those subsidies from access rates into an Interstate Access-related Universal Service Fund ("IAUSF"). CALLS proposes to support this fund by assessing all

[14] *Ninth Report and Order* at ¶ 34.

[15] *Ninth Report and Order*, Separate Statement of Commissioner Ness, 2 ("I would have preferred to proceed concurrently with reform of high cost support and access charges. The two go hand in glove.").

[16] *Ninth Report and Order*, Separate Statement of Commissioner Powell, 2 ("Based on our action today, I am hopeful that the Commission can exercise similar courage as we work had to put together the other pieces of the subsidy puzzle, including access reform and rural high cost support.").

[17] *Ninth Report and Order*, Separate Statement of Commissioner Tristani ("I look forward to continued cooperation as we confront the other pieces of universal service reform, including adjusting interstate access charges to account for explicit support.").

telecommunications carriers and permitting the carriers to pass the assessment on to their end users. Although this aspect of the proposal is also a cost-shifting measure, Level 3 supports the intent of making subsidies explicit. Level 3 also recognizes that removing subsidies from interstate access charges will result in a further expansion of the explicit universal service fund, but should not result in a net increase in total subsidies.

V. CALLS Fails to Address Critical Implementation Issues

A. CALLS' Failure to Bring Packet-Based Services Into the Transport and Termination Regime Dooms the Proposal

Although the Internet uses dramatically different technology than the legacy voice telephony network, these two networks use the same underlying facilities to transport information. Regulatory policies fashioned for the old world of voice telephony therefore can have unintended impacts on the Internet and on new information technologies. One could argue that, on the face of its regulations, the Commission appears to be complying with Congress' "hands-off" the Internet directive[18] by refusing to regulate information service providers. However, the Commission has not complied with the spirit of Congress' directive because it has not yet adjusted its traditional voice common carrier policies to ameliorate the secondary effects some of its rules have on the growth of the Internet.

For example, under the Commission's traditional telephony access charge regime, while carriers must pay access charges to originate or terminate interstate "telecommunications services"

[18] 47 U.S.C. § 230(b).

over LEC facilities, providers of "information services" may use local telephone lines without paying access charges, even for services the Commission has characterized as jurisdictionally interstate.[19] Because of the enormous cost associated with paying access charges, these classifications influence how a company structures new products.

As use of new Internet- and packet-based networks continues to grow exponentially and overtake usage of the old telephone network, there is an urgent need to adopt new communications regulatory policies designed to promote the public interest in efficient and widespread deployment of these new technologies. The CALLS proposal recognizes the pressure that advanced packet-switched technologies will bring to bear on the access charge regime. However, rather than fixing the problem by including packet-based communications providers as participants, CALLS maintains the enhanced/information service exemption for packet-based voice traffic. The dangers inherent in this approach are obvious. Even by conservative estimates, traditional Internet traffic is expected to increase annually by 100-200%. In addition, some have estimated that by 2003 the usage of Internet Protocol ("IP") will surpass all other protocols and continue to grow.[20] Notably, IP growth is predicted not only for the transport of data traffic, but also for the transport of voice traffic. Some

[19] Adding further complication, businesses operating private networks as "end users" may route their interstate calls over local telephone lines without paying access charges.

[20] *Future Networks to Be Built for IP Traffic Shows Research* (July 27, 1999) (citing research by Ovum).

analysts estimate that the market for IP voice traffic is $480 million and will increase by a factor of 40, to $19 billion, by 2004. Any reform that fails to recognize and address this growth is doomed.[21]

While it has been reluctant to impose subsidy-ridden access charges on emerging communications service providers, including Information Service Providers ("ISPs"), the Commission's exemption has encouraged some companies to find new technologies to provide traditional voice and facsimile services that meet the definition of enhanced or information services in order to avoid the current access charge system. For fear of saddling emerging technologies with inflated access charges, the Commission has created incentives for companies to squeeze new technologies into ill-fitting regulatory boxes. Instead of focusing primarily on the types of new and innovative services consumers desire, providers are forced to structure their products to qualify for the enhanced services exemption in order to maintain lower costs. Yet by altering their products to fit the enhanced services definition, they are also forced to give up the key right of interconnection that providers of telecommunications services enjoy. This unduly complicates the integration of a seamless public network that delivers all types of information, including voice, video, and data.

Level 3 is <u>not</u> advocating application of the CALLS proposal to packet-based providers. As explained in more detail above, Level 3 submits that CALLS does not go far enough to bring access charges to cost. Saddling emerging Internet- and packet-based technologies with current access charges, or access charges as revised by the CALLS proposal, would slow the deployment of

[21] IDC, *IP Telephony Services: Market Review and Forecast, 1998-2004*, Press Release (September 1, 1999) available at http://www.idc.com/Press/default.htm.

Internet- and packet-based services to the detriment of consumers and the economy. However, Level 3 is equally concerned that regulatory policies that create a distinction between the rights and obligations of information and telecommunications service providers also stifle growth and innovation. The only solution to this dilemma is to bring carrier's carrier compensation rates down to cost and include all providers of communications services, regardless of the protocol used, in the system. However, because Internet technology blurs the traditional distinctions between local and long distance service, it is critical that the charges for transport and termination of traffic converge to LRIC before Internet and packet-based services are brought into this compensation regime.

B. CALLS Complicates, Rather than Simplifies and Streamlines, Current Archaic Access Charge Regime

The Commission's access charge regime requires an elaborate regulatory superstructure to support it. First, as discussed above, there is a set of classifications separating users of the PSTN who are "carriers" and pay access charges from those who are "end users" and pay local rates. Second, the Commission has a complex set of accounting rules, known as "separations," to allocate the costs and revenues of the LECs between interstate and intrastate services. These rules encompass a variety of arbitrary practices, such as the assignment of 25% of "loop" costs to the interstate jurisdiction, meant to keep local rates low and shift many costs of the local network to long-distance services. The accounting rules were designed under rate-of-return regulation and track the LEC's recovery of its embedded (book) costs, including depreciation. Third, the Commission adopted an alternative form of regulation, called price cap regulation, that now applies to the majority of all sizable incumbent LECs.

In theory, price cap regulation is divorced from rate-of-return consideration. In practice, many intricate accounting rules derived from the rate-of-return era remain in effect, such as prescription of depreciation rates and cost allocation for unregulated services. The impact of the two forms of regulation on prices charged for access differ dramatically. While the access rates of incumbent LECs subject to rate-of-return regulation still average five cents per minute, Commission reforms since passage of the 1996 Act have reduced price cap LEC average rates to one to two cents per minute. Adoption of the CALLS proposal would create a third set of rules governing incumbent LEC access rates that the Commission would have to administer. Rather than simplifying the access charge system, CALLS would make it even more complicated.[22]

In addition, the CALLS reforms could result in yet another implicit subsidy flow. Under Section 254(g), IXCs must charge averaged rates for interstate interexchange telecommunications services. Because the access charges of rural independent LECs are typically higher than those of the Regional Bell Operating Companies ("RBOCs"), this requirement establishes an implicit subsidy from RBOC to independent LEC end users purchasing long distance service. The CALLS proposal would further complicate the subsidy flow, and an IXC's ability to charge averaged rates, by inserting a third level of access charges into the system. Furthermore, although the CALLS access

[22] Because some state commissions direct incumbent LECs to mirror their interstate access charges, the administrative burdens that would result from the CALLS proposal would fall on state commission as well as the Commission.

charge reduction may be relatively significant with respect to a particular participant, because the reduction must be flowed-through to all purchasers of long distance services, the impact on end users' long distance rates is likely to be small.

VI. The Commission Should Reject the CALLS Proposal and Adopt Reforms that Ensure a Faster Transition to Forward-Looking Cost-Based Access Rates

Level 3 submits that although the CALLS proposal resembles a negotiated rulemaking, albeit one in which the Commission and other interested parties did not participate, it is neither a market-based nor prescriptive solution to the problem of inflated access rates. Level 3 pioneered a truly market-based solution to reducing incumbent LEC transport and termination rates to cost. Through arms-length negotiations, Level 3 and Bell Atlantic agreed upon an eventual rate of $0.0015, and in some instances to $0.0012, for the transport and termination of Local and Compensable Internet traffic.[23] To prevent major disruptions in either party's forecasting and planning, Level 3 and Bell Atlantic determined to gradually reduce current compensation rates to the target rate over a period of 12 months. Shortly after this landmark agreement, a second CLEC agreed to similar intercarrier compensation rates with Bell Atlantic. Level 3 submits that this rate, voluntarily negotiated between two parties at arm's length, is closer to an incumbent LEC's true cost of transporting and terminating

[23] The Parties' agreement defines "Compensable Internet Traffic" as "dial-up switched Internet Traffic that is originated by an end-user subscriber of one Party, is transmitted to the switched network of the other Party, and then is handed off by that Party to an Internet Service Provider which has been assigned a telephone number or telephone numbers within an NXX or NXXs which are local to the originating end-user subscriber." "Internet Traffic" is defined as "any traffic that is transmitted to or returned from the Internet at any point during the duration of a transmission."

traffic than the rates set by state commissions. Furthermore, while 12 months may be too short a time in which to reduce access charges to cost-based rates, five years is too long. Level 3 therefore proposes that the Commission adopt no more than a three-year transition to LRIC access. Once access charges are reduced to cost-based rates, Level 3 recommends that all providers of telecommunications services, regardless of the type of service or the protocol chosen, be included in the regime.

Respectfully submitted,

Tamar E. Finn

Andrew D. Lipman
Tamar E. Finn
Swidler Berlin Shereff Friedman, LLP
3000 K Street, N.W., Suite 300
Washington, DC 20007

Patricia Paoletta
William P. Hunt, III
Level 3 Communications, LLC
1025 Eldorado Blvd.
Broomfield, CO 80021

November 12, 1999

Certificate of Service

The foregoing Comments of Level 3 Communications, LLC were served on the following via hand delivery this 12th day of November, 1999.

Magalie Roman Salas, Secretary
Federal Communications Commissions
The Portals - TW-A325
445 Twelfth Street, S.W.
Washington, DC 20554

Chairman William E. Kennard
Federal Communications Commission
445 12th Street, S.W. - Suite B201
The Portals
Washington, DC 20554

Dorothy Atwood
Chief, Enforcement Division
Federal Communications Commission
Common Carrier Bureau
445 12th Street, S.W. - Suite 5A848
The Portals
Washington, DC 20554

Susan Ness, Commissioner
Federal Communications Commission
445 12th Street, S.W.
The Portals
Washington, DC 20554

Linda Kinney
Federal Communications Commission
445 12th Street, S.W. Suite 8-B115
The Portals
Washington, DC 20554

Harold Furchtgott-Roth, Commissioner
Federal Communications Commission
445 12th Street, S.W. - 8TH Floor
The Portals
Washington, DC 20554

William Bailey
Federal Communications Commission
445 12th Street, S.W. - 8TH Floor
The Portals
Washington, DC 20554

Michael K. Powell, Commissioner
Federal Communications Commission
445 12th Street, S.W. - 8TH Floor
The Portals
Washington, DC 20554

Kyle D. Dixon
Federal Communications Commission
445 12th Street, S.W. - 8TH Floor
The Portals
Washington, DC 20554

Gloria Tristani, Commissioner
Federal Communications Commission
445 12th Street, S.W. - 8TH Floor
The Portals
Washington, DC 20554

Sarah Whitesell
Federal Communications Commission
445 12th Street, S.W. - 8TH Floor
The Portals
Washington, DC 20554

Tamara Preiss
Federal Communications Commission
445 12th Street, S.W. - 5th Floor
The Portals
Washington DC 20554

Jane Jackson
Federal Communications Commission
445 12th Street, S.W. - 5th Floor
The Portals
Washington DC 20554

Yog Varma
Federal Communications Commission
445 12th Street, S.W. - 5th Floor
The Portals
Washington DC 20554

Rich Lerner
Federal Communications Commission
445 12th Street, S.W. - 5th Floor
The Portals
Washington DC 20554

International Transcription Service
1231 20th Street, N.W.
Washington, DC 20036

Larry Strickling
Federal Communications Commission
445 12th Street, S.W. - 5th Floor
The Portals
Washington DC 20554

Kathryn Brown
Federal Communications Commission
445 12th Street, S.W. - 8th Floor
The Portals
Washington DC 20554

Wanda Harris
Competitive Pricing Division
Federal Communications Commission
445 Twelfth St., SW
Fifth Floor, DS
Washington, DC 20554