Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

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
	)	

BELL ATLANTIC COMMENTS ON FURTHER NOTICE

Edward Shakin

Michael E. Glover
Of Counsel

1320 North Courthouse Road
Eighth Floor
Arlington, Virginia 22201
(703) 974-4864

January 7, 2000

TABLE OF CONTENTS

I.	The Commission Should Update Its Previous Total Factor Productivity Study to Reflect the Most Recent Experience and Reduce the X Factor	2
II.	The Commission Should Reject The So-Called "Imputed X Study" Which Is Merely a Return To Rate of Return Regulation	5
III.	The Commission Should Reject the So Called "1999 Study" Because It Interjects Errors into the Productivity Calculation	9
IV.	The Commission Should Eliminate The CPD	12
V.	The Only Retroactive Adjustment Should Be to Allow Price Cap Carriers to Adjust Their Rates to Compensate for the Period of Time that the Current Unlawful 6.5 Percent X Factor was in Place	14
	Conclusion	17

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

In the Matter of	)	
	)	
Access Charge Reform	)	CC Docket No. 96-262
	)	
Price Cap Performance Review for Local Exchange Carriers	)	CC Docket No. 94-1
	)	

BELL ATLANTIC[1] COMMENTS ON FURTHER NOTICE

The Commission should reject the proposals in the Notice that would mistakenly inflate the so-called "X" factor in the existing price cap formula. Instead, it should reduce the current X factor to accurately reflect real world productivity results.

As an initial matter, rather than merely tinker with the current arcane scheme of regulatory formulas and Byzantine rate structures -- which substitutes the all too visible hand of the regulator for the invisible hand of the market -- the Commission should move toward a new regulatory regime that is tailored to the increasingly competitive market of today and tomorrow. That is precisely what the industry-consensus CALLS plan now pending before the Commission would do: It would thoroughly reform existing rate structures and transition quickly to a regime that allows the market to determine whether and by how much access rates should change.

To the extent the Commission instead retains its existing price cap regime for any

---

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

period, however, it should reduce the productivity factor currently in place to reflect actual market experience. Specifically, the Commission should simply use its own total factor productivity ("TFP") model – which was upheld by the court of appeals as a reasonable measure of productivity – to calculate a new offset based on current data and reduce the going-forward X factor to no more than four percent.[2] The Commission must also allow price cap carriers to adjust their rates to compensate for the period of time that the current unlawful 6.5 percent X factor was in place.

In contrast, the Commission should reject proposals that would erroneously inflate the productivity factor, much as the Court of Appeals concluded the Commission had in the Order that resulted in this remand proceeding. Here again, as in that prior Order, the proposals in the Notice would manipulate the relatively straight-forward results of a total factor productivity model through a series of complex and convoluted "adjustments" to generate an X factor that is well above the level reasonably dictated by the Commission's own data. None of those adjustments to increase the X factor are justified. Rather, because data for the most recent years demonstrates that productivity has *decreased* from prior levels, the current X-factor must be *reduced*.

I. The Commission Should Update Its Previous Total Factor Productivity Study to Reflect the Most Recent Experience and Reduce the X Factor

The Commission's own total factor productivity model -- which was upheld on appeal -- demonstrates that the current X factor should be reduced. In fact, updating the

[2] Bell Atlantic supports the CALLS proposal for an industry-negotiated settlement of access pricing issues. Consistent with the parameters of the Notice, these comments are for the appropriate price cap rules "in the event that the CALLS proposal is not adopted." Notice, ¶ 4

Commission's previous study to reflect the most recent productivity results requires a reduction to no more than four percent.

<u>The Court of Appeals invalidated only the Commission's effort to justify an increased offset</u>. In its previous Order, the Commission adopted a total factor productivity model, and used the results of that model to calculate annual productivity gains for the local exchange carriers that are subject to price caps. That portion of the decision was largely unchallenged.[3] What was successfully challenged was the Commission's manipulation of the results produced by its model when it came to actually calculating an X factor. Despite the fact that a simple five year average of the productivity figures generated by its model produced an X factor of 5.2 percent at that time -- a slight reduction from the X factor that had been in place for carriers that did not have earnings sharing – the Order instead increased the X factor to 6.5 percent. It was that increase in the size of the X factor that was challenged on appeal and that was rejected by the Court.

The Court found that none of the Commission's justifications for raising the X factor to 6.5 percent "holds water." *USTA v. FCC*, 188 F.3d 521, 525 (D.C. Cir. 1999). In particular, the Court rejected the argument that there is any upward trend in the X factor, holding instead that "the trend appears to be part of a cyclical pattern" with the underlying variables "thrashing about wildly." *Id.* at 526. The Court also rejected the decision to exclude certain years with relatively lower productivity from consideration and found that additional weight placed on AT&T's flawed alternative productivity study was "irrational." *Id.* In addition, the Court rejected the imposition of a so-called "consumer productivity

[3] There was a challenge to the Commission's use of total company data to calculate productivity, but, as discussed more fully below, that challenge was rejected by the Court.

dividend" as an add-on to the X factor indicated by the Commission's model. The Court found that the Commission "never explained" a basis for this arbitrary add-on. *Id.* at 527.

The Court of Appeals rejected the challenges to the Commission's underlying total factor productivity model. In particular, the Court found the Commission was justified in its reliance on total company data rather than interstate data given that "there is no obviously meaningful way to segregate LEC interstate and intrastate inputs because, as is undisputed, 'interstate and intrastate services are usually provided over common facilities.'" *Id.* at 528 (quoting 1997 Price Cap Order). The Court also upheld the decision not to attempt any reinitialization of rates beyond one year because "complete reinitialization would impair the supposed incentive advantages of price caps – which derive from firms' supposing that their efficiencies will not come back to haunt them." *Id.* at 530.

On remand, the Commission's own model requires a reduction in the current X factor. Based on the Court of Appeals decision, the task before the Commission here is limited and straightforward. It should determine an X factor based on the direct results of its own productivity model that was upheld on appeal. The only substantial change from the 1997 Order is the passage of time. In order to have the most accurate results, the Commission should use the most current data. That data results in an X factor of approximately 4.0 percent. Indeed, the updated data supports roughly the same X factor regardless of whether the Commission uses a five year average, an eight year average (covering the entire price cap period) or something in between. *See* F. Gollop, "Economic Assessment of the 1999 X-Factor Study Proposed By the FCC Staff" at Table 6, Attachment 2 to USTA Comments ("Gollop Report"); *see also* F. Gollop, "Technical

Report: Replication and Update of the X-Factor Constructed Under FCC Rules" (Attachment 6 to USTA Comments).

These results show a slight decline in the measured X factor from the data available in 1997. The fact that the X factor, as measured by the Commission's own model, has decreased in recent years demonstrates that with 20/20 hindsight, the Court of Appeals had it exactly right.

Moreover, any attempt to manipulate this data in order to justify retaining the current offset will only create the same type of problems that caused the Court of Appeals to overturn the previous Order. Indeed, several of the proposals now included in the Notice are virtually identical to proposals previously *rejected* by the Commission in the portions of that Order that were *upheld* on appeal. And the Commission rejected those types of manipulations based on sound economic principles which have not changed with the passing years.

II. The Commission Should Reject The So-Called "Imputed X Study" Which Is Merely a Return To Rate of Return Regulation

The most extreme of the proposals is the so called "imputed X" study. This is not a productivity study at all, but rather bases annual access charge reductions on a calculation of earnings -- in other words, it is retreat to a modified form of rate of return regulation.

In the earlier price cap review, the Commission sought comment on a similar method, at that time proposed by AT&T, called the "Historical Revenue Method." But the Commission appropriately rejected that option finding "compelling evidence" in favor of adopting an X factor based on historical total factor productivity. 1997 Order, ¶ 18. That decision was not challenged on appeal and there is no basis to revisit it here.

The Commission has already determined that setting an X factor by targeting to a particular rate of return was inferior because it "would create substantially similar incentives to those under rate-of-return;" and as a result "would not provide sufficient incentives for productivity growth." 1997 Order, ¶ 22. Moreover such a method "would re-create many of the administrative burdens of rate-of-return regulation" with no offsetting benefit. *Id.*

Nothing in the Notice's latest return targeting proposal fixes the infirmities previously identified by the Commission. As one economist explains, "the plan would eviscerate the Commission's attempted regulatory reform and institute in its place, traditional cost-plus regulation with a lag." Affidavit of William E. Taylor at ¶ 24 (Attachment 1 to USTA Comments); *see also* Affidavit of James Vander Weide at ¶ 20 (Attachment 5 to USTA Comments).

An earnings-based X factor also commits the fundamental error of relying on interstate-only cost data – another issue already considered and rejected by the Commission. In contrast to the issues before the Commission on this remand, that determination was *upheld* by the D.C. Circuit. As the Commission ruled and the Court agreed, there was no basis for the argument that "'interstate productivity,' as opposed to total company productivity, is measurable, or even economically well defined." *USTA v. FCC*, 188 F.3d at 528. That was so because "there is no obviously meaningful way to segregate LEC interstate and intrastate inputs because, as is undisputed, 'interstate and intrastate services are usually provided over common facilities.'" *Id.* (quoting 1997 Order).

Again, there is no basis for reversing those conclusions here. As Dr. Taylor explains, the "inability to define interstate TFP growth is not just a theoretical economic quibble" but makes the results of any interstate-only model economically meaningless. Taylor Affidavit ¶ 36; see also *id.* at ¶¶ 29-37.[4]

The imputed X model also carries additional baggage since it relies upon regulatory accounting measures of cost and profit. As Dr. Taylor explains, regulated earnings "do not pretend to measure economic profit and are notoriously poor proxies for it." Taylor Affidavit, ¶ 42. This is so not only because of the artificial split between inter- and intrastate earnings, but also because of "numerous accounting conventions that provide no forward-looking information regarding profit opportunities." *Id.* Regulatory accounting results are also inflated by regulatory depreciation rules which are based on asset lives "that are currently too long and have historically been too long." *Id.* Indeed, because of the overly long recovery periods, the Commission has been forced to create special amortizations above and beyond routine regulatory depreciation to cover equipment that has "rapidly declining" investment. *Prescription of Revised Percentages of Depreciation*, 103 FCC 2d 185, 189 (1985). *See also 1998 Biennial Regulatory Review – Review of Depreciation Requirements* at ¶ 13, CC Docket No. 98-137 (rel. Dec. 30, 1999) (reducing the minimum range of lives for switching equipment 25% -- from 16 years to 12 years). If accounting returns were adjusted to reflect an economically-based rate of return, the results are far below the levels cited in the Notice – 8.75 percent for the period 1991-95. Taylor Affidavit, ¶ 48.

[4] The long distance carriers' argument to justify why the Commission should attempt the impossible calculation of interstate-only productivity growth has been overtaken by changes in the facts. Their claim in the appeal was that interstate revenues grew faster than intrastate revenues. But access reform has shifted interstate access recovery away from relatively faster growing per-minute charges. Today both interstate access charges and intrastate charges are recovered primarily on a per-line basis.

Even if relying on interstate earnings as a basis for setting the X factor wasn't completely invalid as a matter of policy and economics (which it is), the model proposed in the Notice introduces additional flaws that further invalidate it as a legitimate policy tool.

In particular, the calculation of cost of capital is baseless. In the earlier Commission productivity model, capital costs were calculated based on a residual when other costs (labor and materials) were subtracted from total revenues. In contrast, the proposal here attempts to determine capital inputs based on changes in an external index that purports to be a proxy for the opportunity cost of capital. In other words, the proposal claims to use an index to mirror what carriers' financial returns would have been if they had invested their capital elsewhere. The theory is that cost of capital should move in sync with competitive returns to capital. The problem is that the theory is wrong and the measure is wrong.

The theory is wrong because the Notice fails to take into account all the components of capital. While one component of the cost of capital is indeed the opportunity cost of the firm, which may mirror competitive returns to capital, there are other components as well, including depreciation amortization, rental payments and taxes. The capital costs for these components are independent of any opportunity cost of capital. *See* Gollop Report at Section 1.d. As a result, the proposal "violates the most fundamental accounting and economic principles." *Id.* at Section 1.b.

Even for the portion of the cost of capital that is a true opportunity cost, the model is deficient because the measure is wrong. The proposed proxy is an index of grade Baa corporate bonds. By relying only on a proxy for the cost of debt, the model ignores the cost of equity or the relationship between the two. As Professor Vander Weide demonstrates, this failure also distorts the results. Vander Weide Affidavit, ¶¶ 9-10. In fact, the decrease in the cost of debt over time has been fully offset by changes in capital structure and the impact of the cost of equity. The proportion of equity versus debt has risen over time. Because the cost of equity has not fallen like the cost of debt, the overall cost of capital is roughly unchanged between 1991 and the present. *Id.* at ¶ 19, Table 8.

The model also assumes additional local exchange carrier revenues based on a stimulation in minutes as a result of lower prices. Regardless of the merits of that assumption, the calculation is flawed because the model assumes that these minutes will be costless. In reality, extra traffic means additional billing costs, repair and maintenance costs, and ultimately capital expenditures. These are real costs that are just assumed away in the economic modeling. *See* Taylor Affidavit, ¶¶ 50-51.

In sum, the imputed X study resurrects a proposal already rejected by the Commission, uses economically meaningless criteria and then misapplies them. Rather than respond to the Court's concerns about a failure of a legitimate justification, the proposal compounds the Commission's earlier mistakes.

III. The Commission Should Reject the So Called "1999 Study" Because It Interjects Errors into the Productivity Calculation

The Commission's second proposal, the "1999 Study" fairs no better under scrutiny. While this proposal is an improvement on the imputed X calculation because it at least is based on productivity and not regulated accounting earnings, the proposed "improvements" from the 1997 study are illegitimate and serve to invalidate (and inflate) the results. In fact, if the infirmities in this study are corrected, it actually confirms that the current offset must be reduced to no more than 4 percent.

Like the imputed X factor, the 1999 Study adjusts cost of capital based on an index of grade Baa corporate bonds. As a result, this proposal suffers from the same infirmities highlighted above with respect to use of that index as a proxy for actual capital costs in the imputed X factor proposal. This flaw alone completely invalidates any results from the proposed model.

The other proposed adjustments from 1997 model also serve to improperly inflate the X factor. Even if the model had an appropriate capital index, the very fact that the model proposes to rely on *any* capital index makes the model internally inconsistent. The model continues to rely on the Bureau of Labor Statistics ("BLS") data for US nonfarm businesses to calculate United States productivity growth (which is used as an offset to carrier productivity growth under FCC price cap regulation). But that data does not calculate the cost of capital based on a capital index. Instead, it measures the cost of capital based on an "internally calculated rate of return" – the cost of capital is merely valuation of the excess of revenues above costs. Such valuation is consistent with the Commission's prior TFP model. If the Commission were to change its measurement of the cost of capital for the local exchange carriers, consistency requires a similar index to measure cost of capital for the economy as a whole. *See* Gollop Report at Section 1.e. Otherwise, the study would compare apples and oranges, and the result would be invalid.

Another proposed change between the 1997 model and the proposed 1999 version is that the 1999 model excludes certain carrier costs from its calculation, thereby artificially driving up measures of past productivity. The costs in question are labor costs associated with separation payments made to workers leaving the employ of the carriers. The disallowance is "consistent only with the premise that [the staff] believes that the

LECs, if rational, cost-minimizing firms, should simply have fired the excess laborers" with no additional compensation. Gollop Report at Section 2. Not only is such policy cold-hearted, it is economically unsound and deviates from standard business practices for large business firms in the United States. As Professor Gollop explains, absent these payments it would "become increasingly difficult (i.e. expensive)" to hire quality workers. Gollop Report at Section 2. Clearly, the carriers making these payments believe that it is to their ultimate economic advantage to do so. Indeed, because the carriers are no longer regulated on a cost-plus rate of return system, that is the only logical assumption to make. Were the Commission to disallow these costs in the X factor calculations, it would in effect take credit for the carrier productivity gains without recognizing the costs associated with achieving those gains. Such an arbitrary disallowance is completely inconsistent with the economic theory behind using productivity as a measure in the first place.

The 1999 Study proposal also errs in substituting minutes for calls as a measure of carrier output. At a time when local exchange carrier revenues are increasingly moving away from per-minute charges, there is no justification for the artificial assumption that output is directly linked to minutes. Professor Gollop proposes instead a weighted measure of calls, minutes and line growth. In the alternative, should such a weighted measure prove unwieldy, Professor Gollop suggests lines as the superior measure because a majority of carrier revenues are tied to number of lines. Gollop Report, Section 3. In contrast, measuring output in terms of minutes would simply ignore the way in which local exchange carriers actually earn their revenue and produce an artificially inflated productivity figure.

The 1999 Study also includes several other errors. It purports to include a BLS index of nonfarm productivity. In fact, the details of the proposal use some other (unidentified) data series. Gollop Report at Section 4. It also adds data for SNET into its 1998 results, but excludes SNET from earlier runs. This inconsistency distorts comparisons of productivity growth across different years. There are several other errors in input data that Professor Gollop corrects in his review of the details of the proposed model. Gollop Report at Section 5.

Not surprisingly, when the errors in the 1999 Study are corrected, the results are similar to the update of the Commission's 1997 study. In fact, the corrected 1999 Study results are slightly lower (3.76 percent for a five year average and 3.29 percent for the full price cap period). *See* Gollop Report, Table 6. The general confluence of results, however, should give the Commission further comfort of reliability.[5]

IV. The Commission Should Eliminate The CPD

The end result of whatever model the Commission adopts should be used as the best measure of historical productivity growth to calculate a going-forward X factor. There is no justification to lard on an additional half percent (or any other amount) as a so called "consumer productivity dividend" ("CPD"). The Court of Appeals recognized that past justification for the CPD (based on the transition from rate-of-return to price cap regulation) no longer applies.[6] The Notice posits that the end of sharing provides new

[5] These results are also consistent with the results from USTA's own productivity model. *See Access Charge Reform*, CC Docket No. 96-262, Comments of USTA on Notice to Refresh the Record at 23 (filed Oct 23, 1998).

[6] If the Commission were to adopt the imputed X as the method to calculate the going forward X factor, presumably it would have to put in place a reverse CPD, lowering the X factor to account for the dampened productivity incentives associated with this rate-of-return like regulation.

justification, but this justification doesn't hold water. The data underlying the productivity studies has been updated through 1998. Most carriers eliminated sharing from their FCC price cap regulation since 1995, and the Commission completely eliminated sharing in 1997. Moreover, virtually all state price cap plans (relevant because a proper TFP study relies on total company data) have eliminated sharing even earlier. *See* Taylor Affidavit, ¶ 56. It makes no sense to suggest that additional productivity as result of this change is not reflected in the current data.

Even if there were some residual potential increase in productivity not reflected in recent data (which logically there should not be), there is no basis to isolate that one potential impact at the exclusion of other potential changes to productivity. The most significant of these is the growth of competition. Since the 1997 Order, the Commission has implemented rules on unbundled elements, resale discounts and other market opening requirements. In New York alone, Bell Atlantic has lost approximately 1.5 million lines to competitors. While there are some costs associated with these lines, the loss of significant numbers of customers means that the large fixed costs of the network must be recovered over a smaller customer base. The inevitable result is a downward push on expected future productivity. *Access Charge Reform*, CC Docket No. 96-262, L. Christensen, et al., "Updated Results for the Simplified TFPRP Model" at 10-11, attached to USTA Comments (filed Jan. 29, 1997) ("Under competition, the ILECs can expect to experience a decrease in total output growth," which in turn will "lead to a reduction in ILEC TFP growth"). Similarly, the recent (and contemplated) restructuring of access charges away from per-minute recovery to per-line recovery will have a downward pull on expected productivity. When price cap regulation was adopted in 1990, over 50% of interstate access revenues were recovered on a relatively faster growing per-minute basis. As a result of access reform restructures of rates, only 16% of Bell Atlantic's current interstate access revenues are recovered on a per-minute basis. *See Access Charge Reform,* CC Docket No. 96-262, Comments of William E. Taylor, Ph.D. at ¶ 48, attached to Comments of USTA (filed Oct. 29, 1999) ("changing a component of output to a slower-growing measure would require application of a lower X factor").[7] If the Commission were to attempt to adjust the X factor for trends not fully reflected in the historical data, it must include not only forces that would tend to increase productivity, but also those forces that would reasonably be expected to dampen future productivity growth.

V. The Only Retroactive Adjustment Should Be to Allow Price Cap Carriers to Adjust Their Rates to Compensate for the Period of Time that the Current Unlawful 6.5 Percent X Factor was in Place

One aspect of the Commission's previous Order that was commended by the Court was its decision not to "reinitialize" rates to reflect the impact of applying its new (erroneous) X factor for more than one year in arrears. Both the Court and the FCC understood that "extensive reinitialization would considerably aggravate" a perception that FCC regulatory policies lack consistency. *USTA v. FCC,* 188 F. 3d at 530. As a result, such a policy would "impair the supposed incentive advantages of price caps –

[7] While in the recent access reform Notice, the Commission has suggested that per-line growth is slower than per-minute growth, the Commission previously rejected an adjustment for the impact on productivity as too "speculative" because of offsetting potential productivity growth from demand stimulated by lower per-minute prices. *Price Cap Performance Review,* Fourth Report and Order, 12 FCC Rcd 16642 at ¶ 129 (1997). The Commission then failed to account for the fact that any demand stimulation would have a reduced impact on measured productivity growth due to the reduction in per-minute rates.

which derive from firms' supposing that their efficiencies will not come back to haunt them." *Id.*

It is surprising, then, that the Notice -- issued in response to that very Court order -- proposes an unprecedented reinitialization that would "look back" all the way to the beginning of price cap regulation. Such a capricious turnaround is without support. As Dr. Taylor confirms, the look-back contemplated in the Notice, "would seriously jeopardize the links between price cap regulation and improved incentives on the part of the regulated firm." Taylor Affidavit, ¶ 11.

In the past, the Commission has limited its look-back adjustments to correct supposed errors or for improvements in data. Here, the one and only adjustment that the Commission can and should make, consistent with its past policies, is to correct for the unlawful X factor in place since the 1997 order.[8]

Indeed, the Court recognized that should the Commission determine that the correct X factor is below 6.5 – as it must given the data before it – it would make an adjustment to current rates, not just to set a new baseline, but to retroactively make up for the revenues lost as a result of the prior Commission error. In this limited circumstance, retroactive ratemaking is accepted by the Courts. *See United Gas Improvement Co. v. Callery Properties, Inc*, 382 U.S. 223, 229 (1965) ("an agency, like a court, can undo what is wrongfully done by virtue of its [prior] order"); *see also Natural Gas*

[8] In particular, there is no basis for a look-back to capture past growth in a Q or G factor. In addition to other infirmities, such adjustments double count productivity growth already captured by the X factor. *See Access Charge Reform*, CC Docket No. 96-262, Comments of Bell Atlantic (filed Oct. 29, 1999).

Clearinghouse v. FERC, 965 F.2d 1066, 1073 (D.C. Cir. 1992). Indeed, the Court expressly recognized that "the FCC assertion that there could be a true-up of the rates charged during the pendency of a stay" was a basis for its decision to grant the FCC request to continue with the unjustified 6.5 percent X factor for a full year after the Court decision. *USTA v. FCC*, D.C. Case No. 97-1469, Order (June 21, 1999). As a result, the Commission must make that one (and only that one) adjustment based on past inaccuracies in the X factor.

While the entire excess reduction should be compensated, the need for a retroactive adjustment is especially important for the past collection of the consumer productivity dividend. There, the Commission reduced access charges beyond even what its own discredited adjustments to the productivity model suggested. Given that updates to the Commission model show that recent achieved productivity was even less than what the unadjusted model would have predicted, there is no justification for such an add-on to the results of the inflated adjustments.

At a minimum, consistent with the Court's remand, the Commission must compensate the price cap regulated carriers for its addition of a consumer productivity adjustment to its reinitialization reduction to access rates. The Court recognized that "no element of reinitialization based on the CPD will be appropriate in the absence of evidence linking productivity gains to the anticipation of sharings elimination." *USTA v. FCC*, 188 F.3d at 529. Of course, as the Court recognized, such backward looking anticipation is impossible because "the companies could not have responded to that incentive before its creation." *Id.*

Conclusion

If the Commission does not accept the CALLS proposal, it should adopt an X factor of no more than four percent, and adjust local exchange carrier rates upward to reflect the period when an unlawful 6.5 percent X factor was in place.

Respectfully submitted,

____

Edward Shakin

Michael E. Glover
Of Counsel

1320 North Court House Road
Eighth Floor
Arlington, VA 22201
(703) 974-4864

Attorney for the
Bell Atlantic telephone companies

January 7, 2000