

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

In the Matter of	
<u>Access Charge Reform</u>	CC Docket No. 96-262
<u>Price Cap Performance Review for Local Exchange Carriers</u>	CC Docket No. 94-1
<u>Low-Volume Long Distance Users</u>	CC Docket No. 99-249
<u>Federal-State Joint Board On Universal Service</u>	CC Docket No. 96-45

**SUPPLEMENTAL COMMENTS
OF THE PEOPLE OF THE STATE OF CALIFORNIA
AND THE CALIFORNIA PUBLIC UTILITIES COMMISSION**

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The People of the State of California and the California Public Utilities Commission (California) hereby file these supplemental comments in response to the Public Notice, released on March 8, 2000, by the Federal Communications Commission (FCC) in the above-captioned proceedings.¹

¹ Public Notice, In the Matter of 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 Dockets 96-262, 94-1, 99-249 and 96-45), released March 8, 2000.

I. INTRODUCTION

In its Public Notice, the FCC seeks additional comment on the Coalition for Affordable Local and Long Distance Services (CALLS)² revisions to the CALLS proposal that was filed with the FCC on July 29, 1999. The FCC's Public Notice also seeks comment on the commitments made by the interexchange carrier (IXC) signatories to the revised CALLS proposal with respect to the ways in which they would pass on the benefits they would receive if the revised CALLS proposal were adopted.

For the reasons set forth herein, California concludes that the revised CALLS proposal, although better than earlier proposals, continues to fall short of providing a sound public policy solution to the complex issues of universal service, price cap regulation and access charge reform. As California has previously discussed in earlier comments, the CALLS proposal, even as revised, represents a major and unwarranted shift in the FCC's longstanding policy on universal service. While it is true that the revised proposal includes features that seek to benefit end use customers (and, in particular, primary residential line customers) by lowering certain charges and rates, at the same time, the proposal maintains or introduces new features that potentially cancel out or seriously erode these benefits. The revised CALLS proposal also contains a provision that would allow carriers subject to the federal price cap mechanism to request a lower end adjustment, thereby enabling such carriers to offset and/or delay the interstate access charge reductions touted by the proposal. Finally, the revised CALLS proposal, while citing the promises of AT&T and Sprint to

² CALLS members are AT&T, Bell Atlantic, BellSouth, GTE, Sprint and SBC.

reduce basic rates and/or eliminate minimum use charges on certain basic calling plans, does not provide any guarantee that these carriers will actually flow through these and other benefits.

In short, the FCC should carefully evaluate the benefits derived from the revised CALLS proposal relative to the burdens that it would place on end use customers. If, upon careful consideration, the FCC concludes that the revised CALLS proposal has merit, including the proposal's consistency with federal policy, the FCC should, at a minimum, make the following modifications:³

- (1) Reject CALLS' proposal to base federal universal service support on a negotiated and arbitrary measure of price cap ILECs' historical cost as opposed to the FCC's longstanding forward-looking cost approach
- (2) Refer to the Federal-State Joint Board on Universal Service to study and evaluate the ramifications of the revised CALLS proposal to extend universal service support to non-primary residential and multi-line business customers, particularly when, as here, CALLS' proponents have presented no evidence to suggest that price cap ILECs' non-primary residential and multi-line business rates and current SLCs do not cover their cost of basic service
- (3) Restrict both voluntary and involuntary SLC deaveraging under the CALLS proposal so that the percentage differences in SLC rate levels across zones are capped at the percentage differences in the rates for the price cap ILEC's deaveraged unbundled network elements (loop plus port) in those zones

³ The recommendations set forth in items (1)-(5) were fully discussed in California's Initial Comments, filed November 12, 1999, and Ex Parte Comments, filed January 24, 2000, in this proceeding. The recommendations set forth in items (1), (6) and (7) are discussed herein.

- (4) Restrict the permissible level of SLC deaveraging in conjunction with the distribution of universal service funding to ensure that total revenues to the ILEC for serving a customer (e.g., basic service rates, interstate SLC, CALLS-related universal service funding, and any other universal service funding, all of which may be deaveraged) do not outstrip a reasonable allocation of costs to such customers. Such above-cost revenue opportunities could shield price cap ILEC revenues from competitive pressure or, in the absence of significant barriers to entry, encourage inefficient entry due to artificial profit opportunities
- (5) Reduce an ILEC's recovery from the new universal service fund by an amount at least proportionate to the Price Cap Index reductions for the common line basket once target traffic-sensitive access rates are reached and traffic-sensitive common line, marketing, and transport interconnection charge rate elements are eliminated
- (6) Require that price cap signatories waive the Lower Formula Adjustment to interstate access rates for all tariff years during the life of the proposal
- (7) Require IXCs to demonstrate that access charge reductions, regardless of their magnitude and the number of price cap signatories, have in fact been flowed through to residential and business customers

In the sections that follow, California addresses the following key components of the revised CALLS proposal: (1) explicit funding of universal service; (2) price cap modifications under the revised CALLS proposal; and (3) commitments made by AT&T and Sprint pursuant to the revised CALLS proposal.

II. EXPLICIT UNIVERSAL SERVICE FUNDING

According to the revised CALLS proposal, incumbent local exchange carriers (ILECs), subject to federal price cap regulation and who elect to sign on to the proposal,

would revise the manner in which the interstate common line (i.e., CCLC and PICC), marketing, and TIC (CMT) revenues are recovered. Specifically, instead of being recovered from interexchange carriers, these “CMT” revenues would be combined (subject to certain limitations) with the existing interstate SLC into a single charge (combined SLC) and collected directly from end use customers.⁴ This combined SLC would be subject to a cap of \$6.50 for primary residential⁵ and single line business customers, a cap of \$7.00 for non-primary residential customers and a cap of \$9.20 for multi-line business customers.⁶ For UNE zones where the average common line revenue per line exceeds \$7.00 per line for residential lines and \$9.20 for multi-line business lines, price cap ILECs would qualify for funding from a new \$650 million interstate universal service fund paid for by end use customers. Support from the new fund would recover a portion of the revenues currently recovered from price cap carriers' interstate CMT rate elements.⁷

CALLS' proposal to shift recovery of a portion of interstate CMT revenues to a universal service fund would require a fundamental departure from the FCC's conclusion that universal service support should be based on a reasonable measure of an ILEC's forward-looking cost,⁸ with which California has previously agreed. As the FCC has

⁴ Modified Universal Service and Access Reform Proposal, Section 2.1.

⁵ Pursuant to the revised CALLS proposal, the FCC would initiate a proceeding, once the primary residential and single line business SLCs reach \$5.00, to ensure that future increases reflect higher costs in the UNE zone(s) where they would apply.

⁶ Modified Universal Service and Access Reform Proposal, Section 2.1.2, 2.1.3 and 2.1.4.

⁷ Modified Universal Service and Access Reform Proposal, Section 2.2.

⁸ Report and Order on Universal Service at ¶ 224-226, 232-249, 252, 291; Seventh report and Order on Universal Service at ¶ 11; Tenth Report and Order on Universal Service at ¶ 22.

explicitly recognized,⁹ not all interstate CMT revenues arise due to the provisioning of universal service as currently defined by the FCC. While the exact composition of interstate access revenues has become increasingly blurred since the interstate price cap mechanism broke the traditional link between rates and costs, it is fair and reasonable to conclude that interstate access revenues may have several components in addition to the forward-looking economic cost of providing access services. These include embedded access costs in excess of forward-looking costs, subsidization of below-cost services other than universal services, misallocated non-access costs (e.g., marketing costs), excess contribution to an ILEC's shared and common costs, and/or excess profits. California is of the opinion that without a detailed examination of the rates and costs of an ILEC's services in order to identify and isolate all of the causes of above-cost access charges, it is speculative and arbitrary to assume, as the CALLS proposal does, that all CMT revenues are recovered solely for the purpose of supporting universal service.¹⁰

Further, CALLS' proposal to extend universal service funding to all lines, including non-primary residential and multi-line business customers, would lead to a fund that is larger than needed. The FCC should consider carefully the ramifications of the revised CALLS proposal to extend universal service support to these classes of

⁹ In its Access Charge Reform Order, the FCC recognized that universal service costs included in interstate access are intermingled with other costs, including the forward-looking economic costs and the historical costs of interstate access services. The FCC recognized that it would not be able to quantify these universal service costs until such time as its forward looking economic cost model for non-rural ILECs had been completed. First Report and Order, In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing and End User Common Line Charges (CC Dockets 96-262, 94-1, 91-213 and 95-72), adopted May 7, 1997 ("Access Charge Reform Order") at footnote 16.

¹⁰ In addition, the CALLS proponents have not released the cost model used to derive the \$650 million fund so as to enable interested parties to examine what costs and other assumptions were factored in to producing this figure in order to determine its reasonableness and consistency with federal policy.

customers, particularly when, as here, CALLS' proponents have presented no evidence to suggest that price cap ILECs' non-primary residential and multi-line business rates and current SLCs do not cover their cost of basic service. At a minimum, this issue should be referred to the Federal-State Joint Board on Universal Service to study and evaluate the ramifications of expanding universal service support before the FCC determines whether to adopt this aspect of the revised CALLS proposal.

III. PRICE CAP MODIFICATIONS UNDER THE REVISED CALLS PROPOSAL

The revised CALLS proposal establishes a target rate of \$.0055 per minute for the traffic-sensitive interstate access charges (i.e., local switching and transport components of interstate access services) of each Bell Operating Company (BOC) and GTE tariff filing entity. The revised CALLS proposal also establishes a target rate of \$.0065 per minute for all other price cap ILEC tariff filing entities.¹¹ These target rates would be achieved through two means. First, an interstate X-factor of 6.5% would be applied to the traffic-sensitive access charges of price cap carriers at each annual price cap filing until the target rates are reached. Once target rates are reached, the X-factor would be equal to the GDP-PI. Second, to the extent traffic-sensitive access charge reductions resulting from application of the X-factor are less than \$2.1 billion in July 2000, price cap carriers would implement an additional one-time switched access charge reduction to reach \$2.1 billion.¹² CALLS is no longer recommending a permanent shift in 25% of a price cap carrier's interstate local

¹¹ Modified Universal Service and Access Reform Proposal, 3.1.2 and 3.1.3.

¹² Id., Section 3.2.1, 3.2.2, 3.2.3 and 3.2.4.

switching revenues to its CMT basket. However, according to the revised CALLS proposal, signatory price cap carriers would only waive the Lower Formula Adjustment to interstate access rates during the tariff year beginning July 1, 2000.¹³

California is concerned, under the revised proposal, with CALLS' proposed treatment of access charge reductions under the Lower End Adjustment clause of the federal price cap mechanism. As explained by the FCC, the Lower End Adjustment mechanism was created to ensure that LECs and their customers share fairly the risks and rewards of future productivity gains and that LEC price cap regulation produces rates of return within a zone of reasonableness.¹⁴ In other words, the Lower End Adjustment mechanism is intended to ensure reasonable returns for price cap LECs in light of unanticipated productivity changes. The interstate reductions contemplated by the revised CALLS proposal do not fall into this category. Specifically, by negotiating the \$2.1 billion reduction in interstate access charges effective July 1, 2000, the price cap signatories to the CALLS proposal are conceding that such reductions are anticipated and reasonable. The price cap signatories are also conceding that the risks associated with the proposal are acceptable. The same concessions are made by the price cap signatories as a result of negotiating the continued use of the 6.5% X-factor until interstate traffic-sensitive access charges have reached the negotiated target levels.

By allowing price cap signatories to request a Lower End Adjustment due to these negotiated rate reductions for tariff years beginning on July 1, 2001, the revised CALLS

¹³ *Id.*, Section 4.4.

¹⁴ FCC 95-133 at ¶ 7.

proposal could slow down the rate at which target interstate access charge levels are reached, if they are reached at all. Use of a Lower End Adjustment may even offset some of the reductions required under the revised proposal. As a result, signatory price cap carriers could realize the benefit from the revised CALLS proposal's new universal service fund and rate restructuring with only limited reductions in interstate access charges. To prevent this result, if the FCC should adopt the revised CALLS proposal, the FCC at a minimum should require that price cap signatories waive the Lower Formula Adjustment to interstate access rates for all tariff years during the life of the proposal.

IV. COMMITMENTS MADE BY AT&T AND SPRINT IN CONJUNCTION WITH THE REVISED CALLS PROPOSAL

On February 25, 2000, AT&T filed an ex parte submission with the FCC outlining the course of action that it would take, subject to certain conditions, if the revised CALLS proposal were implemented. California has a number of concerns with AT&T's "commitment" letter.

Specifically, AT&T commits to flow through access charge reductions to customers but only if two conditions are satisfied. First, no later than July 1, 2000, the FCC must provide at least \$2.1 billion in usage sensitive interstate access charge reductions. Second, no later than July 1, 2000, the FCC must eliminate the residential and single line business PICCs. Under the revised CALLS proposal, these conditions would necessitate that every single price cap carrier voluntarily sign the agreement. However, there is no basis upon which to conclude that this will occur.

AT&T also says that it will eliminate its Carrier Line Charge for residential and single line business customers whose PICCs are eliminated and says that it will flow through access charge reductions over the life of the plan. AT&T's letter, however, does not actually commit to reducing rates if the revised CALLS proposal is implemented. Similarly, while AT&T proposes to eliminate the minimum usage requirement on its residential interstate Basic Schedule for five years, AT&T reserves the right to work with the FCC to revise or eliminate this commitment after three years if market circumstances warrant. AT&T further notes that its commitment to eliminate this charge would no longer apply if one or more IXCs with a combined market share of at least ten percent of total interstate IXC revenues are permitted to maintain a minimum usage or other flat fee charge on a similar basic schedule or schedules. It is California's understanding that IXCs are not prohibited from pricing their basic schedules in a manner that requires a minimum usage charge today. As a result, AT&T's commitment is already ineffective.

AT&T's other commitments may also prove hollow. Specifically, AT&T says that it will modify its residential domestic interstate Basic Schedule usage rates, in conjunction with the elimination of the minimum usage requirement, no later than July 1, 2000. This modification, however, could well include rate increases offsetting any rate reductions resulting from eliminating the minimum usage requirements. Similarly, AT&T's commitment to maintain its 19 cent per minute One Rate Basic plan, with no monthly recurring charge and no minimum usage requirement for one year from the date it modifies its Basic Schedule rates, does not guarantee actual rate reductions.

To the contrary, the rates for this Basic plan could very well increase at the conclusion of the one-year period.

The promises made by Sprint to continue to offer a plan with no minimum fee also fail to guarantee that interstate access charge reductions will in fact be flowed through to consumers. This is because the per minute rates offered in these no-minimum fee plans could be higher than Sprint's current rates.

In short, the promises made by AT&T and Sprint are vague, equivocal, and full of loopholes. To the extent that the FCC concludes that the revised CALLS proposal should be adopted, the proposal should be amended to require IXCs to demonstrate that access charge reductions, regardless of their magnitude and the number of price cap signatories, have in fact been flowed through to residential and business customers.

V. CONCLUSION

For the reasons discussed, California urges the FCC to carefully evaluate the benefits derived from realigning access charges in the manner proposed by CALLS relative to the burdens that such realignment would place on end use customers. The FCC should also address the compatibility of the CALLS proposal with the universal service provisions of the 1996 Act and the orders adopted by the FCC in implementing

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those provisions. To the extent the FCC concludes that the revised CALLS proposal is adopted, the FCC should, at a minimum, incorporate the modifications recommended by California herein.

Respectfully submitted,

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April 3, 2000

CERTIFICATE OF SERVICE

I hereby certify that I have this day caused the foregoing document to be served upon all known parties of record by mailing, by first-class mail, postage prepaid, a copy thereof properly addressed to each party.

Dated at San Francisco, California, this 3rd day of April, 2000.

/s/ ELLEN S. LE VINE

Ellen S. LeVine