Before the
Federal Communications Commission
WASHINGTON, D.C.

In the matter of	)	
	)	CC Docket No. 94-1
Coalition for Affordable Local and Long	)	CC Docket No. 96-45
Distance Service (Calls)	)	CC Docket No. 99-249
	)	CC Docket No. 96-262
Modified Proposal	)	

FURTHER REPLY COMMENTS OF THE COALITION FOR AFFORDABLE LOCAL AND LONG DISTANCE SERVICE ("CALLS")

JOHN T. NAKAHATA
EVAN R. GRAYER
KAREN L. GULICK

HARRIS, WILTSHIRE & GRANNIS LLP
1200 EIGHTEENTH STREET, N.W.
WASHINGTON, D.C. 20036
(202) 730-1300

Attorneys for the Coalition for Affordable Local and Long Distance Service (CALLS)

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Summary

The Modified CALLS plan is a reasonable, balanced proposal to cut through the "Gordian knot" of universal service, access rate structure reform, and interstate access pricing reforms. The CALLS plan will preserve and enhance universal service, by finally getting on with the job of making universal service support explicit. It will bring down consumer bills. It is Internet-friendly, and will foster the growth of broadband networks and digital services. And very importantly, it will promote the rapid introduction of competition in all telecommunications markets.

Universal service reform, access charge rate structure, price cap reform, and their effects on consumers, especially on those consumers who make few long distance calls, have always been difficult issues for the Commission to address. CALLS has attempted, for the first time, to resolve all of these core issues in a comprehensive, fully integrated manner. The result is a reasonable and appropriate resolution of many competing policy interests. On many fronts – for example, the size of the universal service fund and access charge rate levels – the CALLS plan proposes solutions bounded by proposals contributed by other commenters in the this proceeding. CALLS also responded to concerns raised by commenters for, by example, generating greater up-front reductions and eliminating long distance minimum use fees.

The reasonableness of the Modified plan produces an especially sharp contrast with alternative "plans" proposed by Texas Counsel/CFA/CU and by ALTS/Time Warner. Although the Texas Counsel plan reduces subscriber line charges and eliminates PICC charges immediately, creating short term, static consumer benefit, it is a competitive and universal service disaster, which would in the longer run cost consumers

much more by sacrificing the benefits of competition. The ALTS/Time Warner proposal to slow the reduction in per minute charges gets competition policy backward. It is a naked attempt to keep per minute charges higher, thereby promoting investment in relatively inexpensive switches, while reducing incentives to invest in distribution alternatives to the incumbent LEC loops.

By adopting the CALLS plan, the Commission will dramatically lower consumer bills on July 1, 2000, secure universal service for rural and small town America, promote competition and choice in all telecommunications markets, and facilitate Internet development. The time to act on these very important matters is now. The Commission should adopt the CALLS plan as expeditiously as possible.

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The Coalition for Affordable Local and Long Distance Services respectfully submits these Further Reply Comments in response to the Commission's Public Notice seeking comments on the modifications to CALLS' comprehensive universal service and access charge reform proposal. [1]

As the Massachusetts Department of Telecommunications and Energy concluded previously, "[t]he CALLS plan presents a historic opportunity for the FCC in one stroke to promote several of the still-elusive goals of the Telecommunications Act of 1996."[2] The compromise CALLS presents ends the policy "gridlock" that has surrounded universal service and interstate access charges, and cuts this "Gordian knot" in a way that delivers substantial public benefits, including:

- Assuring affordable interstate rates for all Americans, particularly in rural and high cost areas and for low-income Americans;
- Promoting facilities-based competition and customer choice;
- Simplifying consumer bills;
- Promoting investment in and deployment of competing broadband-capable networks, particularly in rural and residential areas, and narrowing the "digital divide" in areas without local dial-up Internet access;
- Substantially resolving today's tension between universal service goals and an unregulated Internet, preserving both; and
- Providing investment stability during a crucial five-year period in the development of telecommunications competition.

[1] Public Notice, *Coalition for Affordable Local and Long Distance Service (CALLS) Modified Proposal,* CC Dkt. No. 96-262, CC Dkt. 94-1, CC Dkt. No. 99-259, CC Dkt. No. 96-45, (rel. March 8, 2000).

[2] Comments of Massachusetts Department of Telecommunications and Energy, at 2 (filed November 12, 1999) ("Massachusetts DTE").

More than four years after enactment of the Telecommunications Act, the Commission now has the opportunity to finish crucial elements of telecommunications reform. The time to complete the job has come.

I. THE REVISED CALLS PLAN STRIKES AN APPROPRIATE AND REASONABLE BALANCE, AND ITS COMPONENT PARTS ARE INTEGRAL TO THAT BALANCE

A. The Issues and Principles at Stake

Universal service reform, access charge rate structure reform, price cap reform, and their effects on consumers, especially those consumers who make few long distance calls, have always been difficult issues for the FCC to address. In substance and in practical result, these issues have been highly intertwined since access charges were first proposed in 1978 as a means to open competition in long distance markets: how should universal service be preserved and enhanced as markets are opened to competition,[3] what is the appropriate rate structure for access charges,[4] what are the appropriate rate levels[5] and what regulatory method should be used to assure appropriate rate levels for interstate access charges by incumbent local exchange carriers,[6] and how do changes in incumbent LEC interstate access charges affect the interstate retail long distance service rates

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3 MTS WATS Market Structure, *Third Report and Order*, 93 FCC 2d 241, ¶¶ 80-89 (1982) ("*MTS/WATS*").

4 *See*, *e.g.*, Access Charge Reform, *First Report and Order,* 12 FCC Rcd 15982 (1997) ("*First Access Reform Order*").

5 *See*, Price Cap Performance Review for Local Exchange Carriers, *First Report and Order*, 10 FCC Rcd 8961 (1995); Fourth Report and Order in CC Dkt. No. 94-1 and Second Report and Order in CC Dkt. No. 96-262, 12 FCC Rcd 16642 (1997).

6 *See*, Policy and Rules Concerning Rates for Dominant Carriers, *Second Report and Order*, 5 FCC Rcd 6786 (1990).

actually paid by consumers.[7] The first three of these issues are under the direct regulatory authority of the FCC. The last of these issues, the impact of changes in interstate access charges on retail long distance rates, has always been raised by parties seeking to determine whether and how access reform and price cap changes benefit consumers.

The CALLS proposal has attempted, for the first time, to resolve all of the core issues in universal service, access rate structure, and price cap reform in a comprehensive, fully integrated manner. As a result, the CALLS proposal reflects a careful balancing of policy interests. Although the Commission has the option to resolve these issues seriatim, attempting to address these issues as if each stood alone is not, as ALTS asserts, "the most appropriate way of reforming access charges, price caps and universal service."[8] Such an approach would likely lead to a series of ad hoc policy decisions in each docket that did not form a cohesive, pro-competitive, deregulatory policy framework.

In fact, the comments in this docket fully reflect the degree to which access charge reform, universal service reform, and price cap reform are inextricably interrelated. Access rate structures and universal service support mechanisms present

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7 Until 1995, when AT&T was declared a non-dominant carrier, AT&T was subject to price cap regulation that was structured to "pass-through" access charge reductions into lower regulated long distance rates. Subsequently, the Commission declined to impose a regulatory pass-through requirement on IXCs. *See*, *e.g.*, Price Cap Review for Local Exchange Carriers, *Fourth Report and Order*, 12 FCC Rcd 16642, ¶ 185 (1997). Nonetheless, in 1997, AT&T voluntarily committed to certain forms of "pass-through" to the basic schedule, contingent upon certain changes being adopted with respect to interstate access rates. *See*, Letter from Gerald M. Lowrie, Senior Vice President, AT&T, to Reed E. Hundt, Chairman, FCC, CC Dkt. 96-262, May 3, 1997.

8 Comments of the Association for Local Telecommunications Services ("ALTS") and Time Warner Telecom, at 2 (filed April 3, 2000).

two faces of the same policy question: how does the Commission support universal service, allow prices to reflect costs in order to promote investment, innovation, and entry, and maintain affordable rates that are comparable between rural and urban areas? At any given level of incumbent LEC cost recovery, this is a zero-sum debate: if universal service is larger, access rates, in particular flat-rate charges, can be lower; if universal service support is smaller, access rates must increase. To try to escape this zero-sum dilemma, some commenters argue that any rate structure changes that increase flat rates must also be accompanied by a review of overall incumbent LEC access revenue.[9] This attempt to redefine the problem demonstrates the dynamic interrelationship of these subsidy and pricing reform issues.

Moreover, these issues also can no longer be considered under the assumption that local exchange and exchange access service are, and will continue to be, monopoly services. The Telecommunications Act of 1996 directed markets to be opened to competition, and required incumbent local exchange carriers to interconnect with competing local carriers and to make their networks and services available to competitors through unbundling of network elements and resale.[10] Furthermore, Congress enacted a "pro-competitive, deregulatory" national policy framework that specifically required the FCC to forbear from regulations when market mechanisms become sufficient to achieve the statute's purposes.[11] Accordingly, in weighing the appropriate resolution of universal

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[9] Supplemental Comments of the National Association of State Utility Consumer Advocates, at 20 (filed April 3, 2000) ("NASUCA"); Comments of the Texas Office of Public Utility Counsel, Consumer Federation of America, Consumers Union, at 19 (filed April 3, 2000) ("Texas Counsel/CFA/CU").

[10] 47 U.S.C. § 251.

[11] 47 U.S.C. § 160.

service, access rate structure, and price cap reforms, the Commission must also consider the impact of such reforms on the prospects for broad-based market competition.

In addition, over the past four years, Internet growth has exploded and digital technologies are evolving as substitutes for traditional, circuit-switched telephone service. Digital subscriber lines, cable modems, and MMDS services all offer the prospect of "always-on", "all-you-can-eat" flat rate – not minute-based – telecommunications packages for consumers. These technological developments increase the urgency for the Commission to address longstanding issues of subsidy reform and access rate structures.

Thus the Commission today faces a series of very difficult dilemmas, all of which are highly intertwined:

- The Commission has recognized that the "patchwork quilt" of implicit subsidies that characterizes today's interstate access charge mechanisms cannot last. It must find a way to reconstruct universal service support mechanisms that can work with and in a competitive marketplace.[12]

- The Commission has recognized that changes in digital technology can erode today's implicit mechanisms for universal service support, but at the same time has said that it does not believe it should extend today's access charge system to Internet access.[13] The "patchwork" quilt of implicit subsidies cannot survive in the face of Internet expansion.

- The Commission has recognized, and its own universal service models show, that there are some parts of the country that can only be served at extremely high cost. At the same time, the Commission has expressed the concern that universal service not become so large that incentives to provide service efficiently are lost.

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12 Federal-State Board on Universal Service, *Report and Order*, 12 FCC Rcd 8776 (1997) ("*First Universal Service R&O*); *Seventh Report and Order*, 14 FCC Rcd 8077 (1999) ("*Universal Service Seventh R&O").*

13 Federal-State Joint Board on Universal Service, *Report to Congress*, 13 FCC Rcd 11501 (1998).

- The Commission has recognized that failure to establish an explicit, transparent, and competitively neutral universal service mechanism will create barriers to competitive entry in high cost areas.[14] But, more than four (4) years after passage of the 1996 Act, the Commission has yet to replace implicit universal service support in interstate access charges with an explicit, transparent, and competitively neutral universal service mechanism.

- The Commission has recognized that recovering non-usage sensitive costs, particularly loop costs, through usage-based rates is inefficient, harms consumers, creates barriers to entry in higher cost rural areas, and distorts competition by creating arbitrage opportunities in urban markets.[15] Yet the Commission also has expressed concern about the effect of additional flat-rated line charges on those consumers who make few, or no, long distance telephone calls.[16] To the extent that universal service charges become relatively large, the Commission also faces the prospect that either universal service charges on low volume consumers rise, or universal service becomes a "usage tax" robbing consumers of significant consumer welfare gains.

In other proceedings the Commission has drawn five principles for guidance in implementing the 1996 Act, all of which are equally applicable here:

- Rapid introduction of competition in all markets;
- Promotion of facilities-based competition, investment and innovation;
- Reduced regulation;
- Certainty in the market; and
- Administrative practicality.[17]

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14 *See, First Universal Service R&O.*

15 *See, MTS/WATS*, at ¶ 33; *First Access Reform Order,* at ¶ 36.

16 *See*, Low-Volume Long Distance Users, *Notice of Inquiry*, 1999 FCC Lexis 3420, CC Dkt. No. 99-249, FCC 99-168 (rel. July 20, 1999).

17 Implementation of the Local Competition Provisions of the Communications Act of 1996, *Third Report and Order and Fourth Further Notice of Proposed Rulemaking,* CC Dkt. 96-98, FCC 99-238, at Executive Summary (rel. November 5, 1999)..

B. The CALLS Response

The CALLS plans – original[18] and as modified[19] – are attempts by a significant group of both local exchange and interexchange carriers to achieve a comprehensive, balanced resolution of these competing policy interests. The original CALLS plan, filed last August, struck one balance between these competing interests and policy concerns. After CALLS members reviewed the comments and replies filed in response to the original CALLS plan, and considered the views of numerous other stakeholders including public interest groups and state public utility commissions, CALLS proposed its Modified plan. The modified plan, supplemented by specific, unilateral commitments by AT&T and Sprint as to long distance pricing plans for low volume consumers and long distance customer education proposes a different balance between these competing policy interests. In particular, the Modified CALLS plan, together with the long distance company pricing commitments, addresses concerns raised by public interest groups and state public utility commissions that the original CALLS plan might adversely affect low volume long distance users.

The reasonable and appropriate balancing of these competing policy interests under the Modified CALLS plan is even more apparent in light of the increase in local exchange competition in the wake of the 1996 Act. Four years after the 1996 Act, FCC

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18 *See*, Memorandum in Support of the Coalition for Affordable Local and Long Distance Service Plan (filed August 20, 1999) ("August 20 Memorandum").

19 *See*, Memorandum in Support of the Revised Plan of the Coalition for Affordable Local and Long Distance Service ("CALLS") (filed March 8, 2000) ("March 8 Memorandum").

statistics reflect that the percentage of the market served by recent entrants rather than incumbent local exchange carriers continues to grow. AT&T, Media One, Cox, Cablevision, and other cable operators are beginning to offer residential local telephone service over their own local exchange facilities. An FCC staff report recently estimated that by 2005, fully 50% of American households will be able to choose between their local cable operator and their local telephone company for voice telephone service.[20] These estimates show that the Modified CALLS plan, if adopted, could very well be the last nationwide interstate access price cap plan adopted by the FCC – with competition replacing price regulation in most parts of the United States.

Against this backdrop of increasing competition, the Modified CALLS plan offers benefits which include the following:

- *Consumers – both high volume and low volume long distance consumers – will reap significant benefits.* The Modified CALLS plan adopts lower initial primary residential subscriber line charges, eliminates residential presubscribed interexchange carrier charges, cuts per minute access charges in half (resulting in lower per minute long distance rates), eliminates minimum use fees from AT&T's basic schedule and maintains a minimum fee-free rate for Sprint low volume customers, and shields Lifeline customers against any changes in Subscriber Line Charges or incumbent LEC universal service fees. Moreover, consumers of all kinds benefit immediately because the price cap incumbent local exchange carriers have agreed to make additional reductions beyond those contemplated by the original CALLS plan.

- *The Modified CALLS plan promotes rapid introduction of facilities-based competition, investment, and innovation, particularly in lower density rural and residential areas where competition has been slow to develop.* By establishing a competitively neutral, transparent, and portable $650 million interstate access universal service fund to defray a portion of the costs of providing service to rural areas, and by allowing SLC caps to be deaveraged to allow end user charges to reflect their cost, the Modified CALLS plan

[20] *Telecommunications @ The Millenium: The Telecom Act Turns Four*, Federal Communications Commission, Office of Plans and Policy, at 10 (rel. February 8, 2000) ("Telecommunications Act @ the Millennium").

promotes investment in and competition between alternative distribution facilities (i.e. "loops", including wireless connections).

- *The CALLS plan combines both "self-help" through limited SLC deaveraging and national assistance to rural areas through a $650 million universal service fund*. The plan recognizes that it costs more to serve rural areas with fewer lines per square mile than to serve urban or suburban areas. Limits on SLC deaveraging and targeting of USF support ensure comparability.

- *The Modified CALLS plan reflects growing marketplace competition, for example, by using more stringent price regulation initially, but reducing the reliance on regulation as the plan moves forward.* In the first year, the Modified CALLS plan reduces switched access rates substantially more than called for under existing FCC rules. In later years, when competition is increasing, companies move into a nominal rate freeze as their average switched access rates reach applicable target rates.

- *The Modified CALLS plan mitigates the effect of regulatory distinctions between flat rate packet services and per minute switched access, and creates a regulatory transition compatible with the continued evolution of packet services.* The CALLS plan does this by cutting per minute access rates in half, and by almost entirely consolidating common line recovery into flat rated charges.

- *The Modified CALLS plan can be implemented immediately, without the years of follow-on rulemaking that have characterized the universal service implementation process to date.*

C. The Failure of Competing Proposals

The reasonableness of the Modified CALLS Proposal produces a sharp contrast to two alternative "plans" proposed by Texas Counsel/CFA/CU (Texas Counsel)[21] and by ALTS/Time Warner,[22] respectively. Although the Texas Counsel plan reduces subscriber line charges and eliminates PICC charges immediately, creating a short term, static consumer benefit, it is a competitive and universal service disaster which would in the longer run cost consumers much more by sacrificing the dynamic benefits of competition. The Texas Counsel plan creates no universal service funding to replace implicit universal

[21] Texas Counsel/CFA/CU, at 56.

[22] ALTS/Time Warner, at 4.

service support currently in interstate access charges. It provides for no geographic deaveraging of rates. In fact, the monthly flat rate charges produced by the Texas Counsel plan are so low that they are below the interstate share of their own prediction of forward looking loop and port costs. The Texas Counsel plan would not promote residential competition – it would instead slam on the brakes. The Texas Counsel plan rejects Congress' fundamental choice in 1996 – that competition delivers better value for consumers in the long run than do regulators.

The ALTS/Time Warner plan takes a different tack. The ALTS/Time Warner plan recognizes that some amount of universal service support is necessary, but "low-balls" the support necessary to replace implicit support. This creates a significant risk of shortchanging rural America, compared with the Modified CALLS plan. ALTS and Time Warner then propose to slow the reduction in per minute charges proposed by CALLS, to further hasten reductions in multiline business PICC charges, and to preclude geographic deaveraging of end user-paid SLC rates. This approach gets competition policy backward: it is a naked attempt to keep per minute charges higher, thereby promoting investment in and deployment of relatively inexpensive switches, while reducing incentives to invest in distribution alternatives to the incumbent LEC loops. Nowhere does ALTS, Time Warner, Allegiance, Focal, or any other commenting CLEC claim that the rates produced by the Modified CALLS plan would be predatory. Where, as here, incumbent LECs would be choosing to lower switched access rates dramatically by opting into the CALLS plan, attempting to prevent the participating price cap LECs from charging lower, non-predatory rates serves only to harm competition and consumers for the benefit of competitors.

II. CONSUMERS WILL SEE DIRECT AND IMMEDIATE BENEFITS UNDER THE PLAN

In initial comments on the modified plan, CALLS demonstrated that consumers will enjoy substantial benefits, beginning in the 2000-2001 tariff year.[23] Many commenters note that the modifications to the plan provide protections for low-volume consumers, and bring consumer rates down.[24] As articulated by Global Crossing, which did not subscribe to all facets of the plan, "there should be little doubt that most consumers will be better off with the modified plan than without it."[25] In short, while the initial CALLS plan created substantial consumer benefits from lower long distance rates and increased competition, particularly in rural and residential markets, the Modified CALLS plan ensures that the low-volume long distance consumers also share in the plan's benefits.

A. The Elimination of Minimum Use Charges Will Benefit Low-Volume Consumers

Zero-volume and low-volume long distance users will see dramatic reductions. Significantly, as part of the Modified plan, AT&T committed to eliminating their minimum use fees for basic schedule long distance customers and, in addition, to offer an

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23 Comments of the Coalition for Affordable Local and Long Distance Service ("CALLS") (filed April 3, 2000) ("CALLS April 3 Comments").

24 *See*, Further Comments of the Alliance for Public Technology, The Communications Workers of America, The National Association of Development Organizations, et. al., at 5-6 (filed April 3, 2000) ("APT/CWA/NADO") (approving of the lower SLC caps of the modified plan and the commitments by AT&T and Sprint to eliminate minimum use charges); Comments of the Enterprise Networking Technology User's Association, at 2 (filed April 3, 2000)(approving of "immediate access charge reductions that ultimately will be passed on to customers" and reductions in special access rates); Comments of the Iowa Utilities Board, at 2 (filed April 3, 2000)("The IUB commends the CALLS members for listening and responding to many of the concerns raised by the IUB and other parties.).

25 Comments of Global Crossing North America, Inc., at 12 (filed April 3, 2000).

alternative "one-rate" plan with no minimum use fee. Subject to certain conditions, Sprint will not impose a minimum use charge on at least one basic rate plan for the duration of the CALLS plan. Further, in their comments, MCI Worldcom and Global Crossing have now also committed to offer calling plans without minimum use fees.[26] Therefore, customers who make no long distance calls but today pay minimum use fees will see their monthly charges cut dramatically and will have a choice of "no-minimum" plans.

While most commenters recognize the benefits low volume consumers will enjoy when the commitments related to the minimum use charges are fulfilled, several claim that the commitments can be easily avoided, and are therefore illusory.[27] These commenters fail to take account of the fact that AT&T in particular fortified its commitments in an *ex parte* letter filed with the Commission on March 30, 2000.[28] In particular, AT&T's commitment to eliminate minimum usage requirements on its Basic Schedule is *not* contingent on whether other long distance carriers also eliminate minimum fees for Basic Schedule customers. In its letter to the Commission, AT&T committed to do the following, provided the Commission provides at least $2.1 billion in usage-sensitive interstate access charge reductions and eliminates the residential and single line business PICC by July 1, 2000, and that interexchange carriers are able to obtain the benefits outlined in the Modified CALLS plan:

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[26] MCI WorldCom Comments on the Modified CALLS Plan, at 2-3 (filed April 3, 2000); Global Crossing, at 12.

[27] Supplemental Comments of the People of the State of California and the California Public Utilities Commission, at 9-11 (filed April 3, 2000) ("California Commenters"); Comments of the Florida Public Service Commission on Alternate CALLS Proposal, at 2-4 (filed April 3, 2000).

[28] *See*, Letter from Joel E. Lubin, AT&T, to Magalie Roman Salas (March 30, 2000).

- Eliminate the minimum usage requirement no later than July 1, 2000 on its residential interstate Basic Schedule for 5 years, with the right to work with the Commission to revise or eliminate this commitment after 3 years if market circumstances warrant;

- Modify its residential domestic interstate Basic Schedule usage rates in conjunction with the elimination of the minimum usage requirement. Once it establishes these rates, it will not increase them for 1 year. AT&T will also notify every residential interstate Basic Schedule customer that these changes are taking place and advise those customers of other AT&T calling plans, including but not limited to the AT&T One Rate Basic plan, that may better serve an individual customer's needs;

- Maintain the AT&T One Rate Basic plan rate of 19 cents per minute at all times for domestic interstate calls from home, with no monthly recurring charge and no minimum usage requirement, for 1 year from the date it establishes revised Basic Schedule rates. If this plan is successful, AT&T will offer throughout the five-year life of the CALLS plan a calling plan with a single per-minute rate for domestic interstate calls from home, with no monthly recurring charge, and with no minimum usage requirement;

- When the residential and single-line business PICCs are eliminated as charges assessed to interexchange carriers, AT&T will eliminate the Carrier Line Charge, which is its PICC recovery mechanism, for these long distance customers;

- To the extent that AT&T realizes reductions in its access costs as a result of the reforms described above, it will, over the life of the plan, flow those savings through to residential and business customers.

These commitments address the concerns expressed regarding the previous AT&T commitments. For example, the Florida Public Service Commission expressed concern that AT&T's previous commitment was contingent on actions by other long distance carriers to eliminate minimum use fees.[29] California argued that because of this condition, "AT&T's commitment is already ineffective."[30] Whether these

[29] Florida PSC, at 3.

[30] California Commenters, at 10.

characterizations of the original commitments were accurate or not, AT&T's clarified commitments no longer pose these concerns.

B. The Benefits to Consumers from Lower Long Distance Prices Should Not Be Ignored

The CALLS plan will also benefit residential and business consumers who make use of long distance services. Some commenters continue to discount the importance of low long distance rates, and seem to define what is good for consumers solely in terms of low or non-existent fixed line charges. This myopic fixation on fixed charges in general, and the SLC in particular, is paternalistic and wrong. Since 1984 when the SLC was established, long distance rates in real terms have fallen 77%. Consumers have responded by purchasing much more long distance service, quadrupling their demand between 1984 and 1998. As these statistics demonstrate, *consumers have spoken with their pocketbooks.* If they did not value long distance service, they would not buy more as the price falls. By reducing per-minute access charges, the CALLS plan will reduce long distance bills substantially and give consumers more of what they want. As demonstrated in a detailed study of the CALLS plan by Joel Popkin & Company, this makes economic sense.[31] The current access system robs consumers of this choice to buy more or pocket the difference. By allowing the price of long distance service to better reflect its economic cost, the CALLS plan will dramatically increase consumer welfare.

While consumers have benefited directly from the 77% real reduction in long distance rates since 1984, they have received additional, and substantial, indirect benefits

[31] APT/CWA/NADO, at Appendix A, Stephen Pociask, "The CALLS Plan Revisited: A Quantification of Consumer Benefits" ("Updated Pociask Report"); *See also*, Robert W. Crandall and Jeffrey H. Rohlfs, "The Economic Case for the CALLS Proposal," at 3 (filed December 3, 1999).

as well. By making inexpensive long distance communications available to American industry, these reductions have helped to fuel the longest peacetime expansion of the U.S. economy – an expansion driven by improvements in communications and computing. New categories of business are thriving today that could not have existed if long distance rates were still at their 1984 levels, creating new jobs and higher incomes, and offering new and better products and services. The same consumer whom some parties are seeking to "protect" from flat end user charges may well have a job at Dell Computer, or telecommute from a rural home, or benefit from the explosion of toll-free services that has resulted from lower access charges and long distance rates.

C. The Plan Does Not Threaten Subscribership and The SLC Caps Are Reasonable

The Commission should not adopt the paternalistic view that consumers' demonstrated preferences as reflected in demand patterns should be denied in order to keep SLCs low. There is no evidence that higher flat rate charges harm subscribership levels. Indeed, the CALLS plan will likely lead to more Americans having a telephone precisely because it lowers long distance bills. As several studies have concluded, high toll bills are the leading cause of disconnection from the network.[32] Since 1984, as SLCs and PICCs have gone up and long distance rates have come down, subscribership levels

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[32] Chesapeake and Potomac Telephone Company's Submission of Telephone Penetration Studies, Formal Case No. 850 (filed October 4, 1993); Field Research Corporation, *Affordability of Telephone Service – A Survey of Customers and Noncustomers*, 1993 (study funded by GTE-California and Pacific Bell, mandated by the California Public Utilities Commission); Milton Mueller & Jorge R. Schement, *Universal Service from the Bottom Up: A Profile of Telecommunications Access in Camden, New Jersey*, 12 *Information Society* 3 (April 1996); John Horrigan & Lodis Rhodes, *The Evolution of Universal Service in Texas* (September 1995) (working paper, LBJ School of Public Affairs). *See also,* Milton Mueller, Jr., *Universal Service,* at 172 (1997).

have risen substantially.[33] By lowering access charges and therefore long distance rates – and by eliminating the minimum use charge – the CALLS plan will make it easier for people to remain on the network.

Moreover, the plan's SLC caps are reasonable, and do not threaten the affordability or comparability of services.[34] Most consumers will pay SLCs substantially below the applicable cap. And in many cases, even when incumbent LECs could charge rates at the cap under price cap rules, they will be constrained from doing so by increasing competition.

Texas Counsel/CFA/CU argue that Commission verification of SLCs should be based solely on the High Cost Proxy Model.[35] Limiting the information that the Commission can consider when verifying SLC caps would be arbitrary and premature. CALLS has committed to provide economic data associated with the provision of retail voice grade service because all retail costs, not just wholesale costs, should be considered when verifying caps for the SLC, which is a retail rate.

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33 "Past experience shows that the shift away from per minute access charges to flat charges has had an overall positive effect on telephone subscribership. In 1984, when the first SLCs were adopted, telephone subscribership was 91.8 percent. Due in part to the creation of the SLC and later the PICC, usage sensitive interstate access rates – and, in turn, long distance rates – have fallen, and subscribership has increased. By 1989, when residential SLCs first reached $3.50, telephone subscribership had risen to 93.3 percent. Today, with SLC and PICC-related charges totaling approximately $5.00 per month, and with additional charges for the Telecommunications Relay Service ("TRS") and number portability, telephone subscribership is over 94 percent." *See* CALLS Memorandum, at 16, *citing*, Alexander Belinfante, *Telephone Subscribership in the United States*, (Com. Car. Bur. Ind. Anal. Div. Rel. May 1999), at Table 1.

34 *See*, *for example*, Comments by the National Grange of the Order of Patrons of Husbandry, at 4 (filed February 24, 2000) ("National Grange") (calling the original plan's $7.00 cap sufficient to ensure that disparity between SLC rates will not affect the goal of universal phone service in rural areas).

35 Texas Counsel/CFA/CU, at 16.

D. The Elimination of Residential and Single Line Business PICCs Lowers Prices and Enhances Competition

Eliminating PICCs will also have a salutary impact on consumers. As demonstrated in earlier comments,[36] eliminating PICCs will encourage the development of local competition and lower end user prices by lowering transactions costs. Importantly, the choice between SLCs and PICCs does not raise the question of whether IXCs or end users should pay for using the loop.[37] Whether incumbent LECs recover their costs with a SLC or a PICC, the costs will ultimately be borne by end users. The real question is whether the costs will be recovered directly – and therefore more efficiently due to the elimination of transactions costs – or indirectly through the IXC.

In addition, contrary to claims made by NASUCA and others,[38] recovering costs through PICCs rather than SLCs tends to reduce competition. To the extent that the long distance companies average the PICC pass-through nationwide, rather than charging customers the specific PICC charged by that customer's LEC, pricing signals will be diluted for consumers choosing between the incumbent LECs and alternative suppliers of service.

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36 *See*, Comments of the Coalition for Affordable Local and Long Distance Service ("CALLS"), at 11-19 (filed November 12, 1999) ("CALLS November 12 Comments").

37 This false choice is presented by Texas Counsel/CFA/CU, at 26 ("Both the CALLS proposals anticipate the use of the loop by Interexchange Carriers (IXCs) without paying for it"); NASUCA, at 6 ("IXCs obviously benefit from the use of the loop and paying a fair price in exchange for a benefit is not a subsidy"). One commenter claims that the elimination of PICCs amounts to an implicit subsidy for long distance carriers and their customers in violation of section 254(e). Comments of the Vermont Public Service Board and the Vermont Department of Public Service on Revised Plan of the Coalition for Affordable Local and Long Distance Service, at 5-7 (filed April 3, 2000). As there are no incremental loop costs associated with carrying long distance traffic, incorporating the PICC into the SLC cannot be construed as a subsidy.

38 NASUCA claims that the "proposed shift of interstate costs from the PICC to the SLC eliminates that effectiveness of competitive choice." NASUCA, at 8.

Moreover, the fact that the long distance market is more competitive than the local exchange market does not subject PICCs to more competitive pressure than SLCs. Whether the incumbent LEC charges the end user or the IXC, the PICC charge is subject to the same amount of competitive pressure. All that can be competed away in the long distance market is the markup IXCs might charge for the transactions costs associated with passing the PICC through, not the underlying PICC charge itself.

In fact, because the indirect recovery through the PICC disassociates the customer's payment from the customer's choice, it makes it harder for consumers to correctly "internalize" this expense in their decision making. If a customer incurs a specific SLC charge when he or she chooses local service from an incumbent LEC, the consumer can reasonably compare that charge with the comparable charges for a CLEC's local service, and make an informed choice of local provider. But if a portion of the incumbent LEC charge for its local connection is recovered indirectly through a charge on another carrier's bill, and especially when that charge is averaged nationwide, the consumer will have great difficulty making a valid choice among local service providers. Indirect recovery of local loop costs through the PICC will thus interfere with informed customer choice and competition in the local market, without creating any additional competitive benefit in the long distance market.

E. The Plan Promotes Broadband Deployment and the Development of the Internet, Particularly in Rural Areas, by Creating a Portable Universal Service Fund, Deaveraging Rates, and Reducing Access Charges

Among the consumer benefits ignored by some commenters are the aspects of the plan that encourage development of broadband packet-based services. With no substantiation, NASUCA claims that CALLS "does nothing to promote advanced services in rural areas, and the Commission should not be misled by any claims to the contrary."[39] This bold and mistaken assertion suggests that NASUCA fails to appreciate the impact of the Commission's interstate access charge and universal service policies on all telecommunications networks. It also may explain why NASUCA and other groups have focused on issues such as the SLC to the exclusion of everything else.

CALLS will promote broadband deployment, particularly in rural areas, for four principal reasons. *First*, the CALLS plan provides interstate access related universal service to competing providers entering high cost areas. This funding will provide an incentive to these providers to build out networks in rural areas. As CLECs build their networks, they have an incentive to use architectures that will be compatible with broadband services. While the universal service funds cannot be used to support advanced services, the funding can be used to support the construction of underlying networks that will support advanced services, along with services included in the Commission's definition of universal service. The resulting competition will encourage incumbent LECs to upgrade their own networks in rural areas to avoid losing valuable customers attracted to broadband offerings of new entrants.

Second, the plan's deaveraging and access charge reforms similarly promote CLEC entry and thereby encourage broadband deployment in rural areas. Entry is much more likely in any market if providers believe they can recover their costs. Currently, incumbent LECs "support" services in rural areas with revenues from urban areas, from business customers, and from interstate access charges. Since CLECs cannot obtain a sufficient amount of this support by serving a rural area, it is often not economically

[39] NASUCA, at 8.

rational to enter. By deaveraging rates and replacing implicit support from access charges with an explicit and portable universal service fund, the plan promotes entry, and therefore broadband deployment.

Third, as detailed in earlier comments,[40] the CALLS plan is an important step forward in the debate over the Commission's exemption of enhanced service providers from an obligation to pay interstate access charges. Since interstate access charges will no longer contain the current levels of universal service support, universal service goals will be assured under the CALLS plan notwithstanding the exemption. The reforms will head off the collision of two of Congress's most important policy goals: promoting advanced services and protecting universal service. Packet-switched products such as Internet telephony can grow and thrive without threatening to undermine universal service goals. By enhancing Lifeline support and creating a $650 million explicit fund, the CALLS plan therefore substantially reduces today's tension between universal service goals and an unregulated Internet by preserving both.

Furthermore, the debate over the exemption will become far less crucial because the CALLS plan reduces access rates to half the current levels. With substantially less money at stake, the ESP exemption will likely become a less important – and less contentious – issue. Telecommunications providers considering building out packet switched networks will no longer have to factor in substantial regulatory risks associated with potential elimination of the exemption.

Fourth, if CALLS is adopted, dial-up access to the Internet will be less expensive for consumers in rural areas who must dial long distance to reach an ISP. Even as

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[40] CALLS November 12 Comments, at 7-8.

broadband services are deployed, dial-up access will remain a significant means for reaching the Internet. There remain, however, parts of the United States that lack local dial-up Internet access. By lowering the cost of long distance service, the CALLS plan reduces the cost for consumers in these remote areas to reach the Internet and participate in e-commerce and other benefits of the Internet age.

F. The Plan's Mechanisms for SLC Deaveraging Both Promote Competition in Local Markets and Maintain Affordable and Comparable Rates

Deaveraging not only promotes broadband deployment – it will encourage competition in voice telephony markets as well. The CALLS plan provides for the deaveraging of SLCs, but by establishing caps, it also ensures that rates will be affordable and comparable throughout the country. The deaveraging provisions therefore represent a balance between two of the most defined policy goals of the 1996 Act: promoting competition and keeping rates affordable and comparable. Like so many other provisions of the plan, the deaveraging measures represent a careful and reasonable balance of competing policy interests.

Both the National Grange and the National Association of Development Organizations ("NADO") – two prominent rural groups – agree that the balance is appropriate, and that the SLC caps will keep rates comparable and affordable.[41] For example, with respect to the initial CALLS plan, the National Grange commented that, "[t]he proposed SLC rate cap of $7.00/month in the CALLS proposal is sufficient, in our view, to assure that the disparity between SLC charges in urban and rural areas will not

[41] *See*, National Grange, at 4; Reply Comments of the National Association of Development Organizations, at 5-6 (filed December 3, 1999).

be so great as to substantially affect the goal of universal phone service in rural areas." This is only more true with a SLC cap of $6.50, as proposed in the Modified plan.

Texas Counsel/CFA/CU contend, however, that the deaveraging provisions of the CALLS plan amount to "discriminatory pricing" and are "inconsistent with actual market practices and social policy in the Act of 1996. . . ."[42] This criticism ignores that one of the principal policy goals of the 1996 Act is to promote competition. Competition simply will not develop in areas in which incumbents charge rates significantly below cost.[43] Although the deaveraging provisions do not permit SLCs in high cost areas to reflect costs perfectly (due to the competing policy considerations), rates and costs will be more closely aligned than they are today.

The California Commenters asks the Commission to modify the deaveraging provisions "so that the percentage differences in SLC rate levels across zones are capped at the percentage difference in the rates for price cap incumbent LECs deaveraged unbundled network elements (loop plus port) in those zones."[44] These restrictions already exist: in the absence of voluntary price reductions, it is not possible under the plan to maintain a greater percentage difference among deaveraged SLCs across zones than the percentage difference in the rate levels for the corresponding UNEs. These provisions include the requirement that incumbent LECs deaverage UNEs as a condition of deaveraging SLCs, and the "reverse cascade," which, in the absence of additional, voluntary price reductions, requires incumbent LECs to recover a greater proportion of

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[42] Texas Counsel/CFA/CU, at 40.

[43] *C.f.*, ALTS/Time Warner, at 10.

[44] California Commenters, at 3.

revenues from low cost zones.[45] Existing Commission precedents also constrain voluntary reductions to preclude anti-competitive practices such as predatory pricing.

G. The Overall Consumer Benefits of the Plan Are Significant

The overall consumer benefits of the modified CALLS plan are even greater than under the original plan. Joel Popkin & Company estimates that the modified CALLS plan will generate $7.4 billion in annual benefits to residential and business customers when compared to today's rates.[46] Popkin had estimated that the original plan would yield $5.3 billion in annual consumer benefit – so the modifications have improved consumer welfare by an additional 40%. Residential consumers receive the bulk of these benefits. Compared to the original CALLS plan, residential customers will receive an increase in benefits of 54%, mostly due to the reduction in caps for residential SLCs. Business users will see a 37% increase in benefits, predominantly due to reductions in special access rates that were not included in the initial CALLS plan.

While each of the component parts of the plan make sense as a careful and sometimes complex balance of competing policy interests, the plan as a whole is an unqualified win for consumers. As the Popkin quantifications demonstrate, consumers - both low and high volume - will enjoy direct bottom of the bill savings. The plan will also benefit consumers in ways that are not so easy to quantify, and therefore were not taken into account in the Popkin study. These include the benefits of widespread local competition in residential markets and enhanced broadband deployment. The

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45 *See*, proposed Rule 69.152(q)(7). In addition, a uniform rather than a proportionate "u" factor to reconcile UNE loop and port prices with CMT revenues also means that participating price cap LECs will maintain proportionately higher prices for urban areas. The "u" factor is defined at proposed rule at 61A.3(aaa).

46 *See*, Updated Pociask Report.

Commission should take account of all these benefits - quantifiable or not - in evaluating the plan.

III. THE UNIVERSAL SERVICE PROVISIONS REASONABLY IMPLEMENT THE MANDATES OF SECTION 254

A. The Commission Should Establish the $650 Million Universal Service Fund

Several commenters reassert that the $650 million universal service fund is, alternately, inadequate or excessive, but their criticism in fact confirms that CALLS' proposed $650 million access USF support is a reasonable compromise. As discussed at length in the Memorandum proposing the initial CALLS plan,[47] in the initial Reply Comments,[48] and in the Memorandum proposing the Modified plan,[49] there are several reasons why a $650 million fund, considered together with other aspects of the CALLS plan, is appropriate. First, the fund's size was bounded by estimates made on the record in the universal service proceeding.[50] In fact, the last round of comments proves this point conclusively. US West estimates a fund size of $1.2 billion, and claims that this

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47 August 20 Memorandum, at 24-28.

48 Reply Comments of the Coalition for Affordable Local and Long Distance Service ("CALLS"), at 10-14 (filed December 3, 1999) ("December 3 Replies").

49 March 8 Memorandum, at 8-10.

50 *See*, August 20 Memorandum, at 25. The United States Telephone Association estimated that then-current interstate common line rates contained $3.9 billion in implicit universal service support. Comments of the United States Telephone Association on the Further Notice of Proposed Rulemaking, CC Dkt. No. 96-45 and CC Dkt. No. 96-262 (filed July 23, 1999). Rogerson and Kwerel of the FCC estimated $1.9 billion in implicit universal service support, assuming that residential SLCs were capped at $6.50 per month. "A Proposal for Universal Service and Access Reform," William Rogerson and Evan Kwerel, CC Dkt. Nos. 96-45 and 96-262 (filed May 27, 1999). On the other hand, the HAI model projects a forward-looking estimate of implicit support in interstate common line elements at approximately $250 million. HAI Model Version 5.0a, CC Dkt. No. 96-45. This model used SLC caps of $7.00 for residential and single line business lines and $9.20 for multiline business lines. It also used FCC Common Inputs as of March 10, 1999.

estimate is conservative.[51] Texas Counsel/CFA/CU recommends that no fund be established at all. And ALTS/Time Warner calls for a universal service fund of $300 million.[52]

The fact that the proposed amount of rural and high cost universal service funding was arrived at through negotiation, bounded by estimates in the record of the universal service proceeding, rather than through a proxy model methodology, does not make it less reliable or illegitimate. Indeed, the fact that a substantial number of carriers who must provide service in the marketplace – including the high cost carriers – support this amount of funding, as part of the overall CALLS plan, gives a greater degree of real-world assurance that this amount, implemented as part of the overall CALLS plan, will not be excessive. It is important to note, in this regard, that the CALLS members include companies on all sides of the debate: AT&T and Sprint who, with MCI and other IXCs, pay the majority of universal service contributions, local companies that have historically been "net-payers" of universal service contributions, and companies such as BellSouth, GTE, and Sprint who provide service in higher cost areas and therefore are generally net recipients of universal service support.

Second, the $650 million fund should be considered an interim estimate. The Commission will be able to observe the results of the $650 million interim universal service fund in the marketplace in order to have the benefit of real-world experience and data before making any further determinations. Due in large part to regulatory distortions, it has proven to be extraordinarily difficult to finalize the access-related

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51 Comments of US West, Inc., at 5, n10, 8 (filed April 3, 2000).

52 ALTS/Time Warner, at 19.

universal service fund, with current Commission deliberations having consumed over four years without even an initial resolution. The Commission will be in a much better position to determine the final amount of support required once it gets the ball rolling and establishes this reasonable interim fund.

Third, the $650 million fund should give the Commission comfort, as it is consistent with the Commission's cost model. Several commenters argue that universal service support calculations should be based on "forward-looking" estimates of costs in accordance with the proxy cost model the Commission adopted in November to allocate funds among states to support intrastate rates.[53] For example, Level 3 alleges that the model must be used for the purpose of sizing universal service support. It is important to note, however, that the Commission has not yet determined the amount of implicit support in interstate access charges or used the model for that purpose.[54] As stated in the Declaration of Joel Lubin, which was attached both to the CALLS initial Memorandum and the initial Reply Comments, the Commission's high cost-proxy model supports the $650 million estimate.[55] Therefore, although some CALLS members do not endorse using the cost model as a method for determining interstate access related universal service funding, it is another indicator that an interim $650 million interstate access universal service fund is reasonable.

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53 *See*, *for example*, Level 3, at 6.

54 *See*, Federal-State Board on Universal Service, *Ninth Report and Order*, 14 FCC Rcd 20432, ¶ 19 (1999) ("*Universal Service Ninth R&O*") (establishing a high cost fund based on relative costs between states).

55 Bell Atlantic, BellSouth, GTE, and SBC do not support use of a model to calculate universal service support, and together with Sprint do not join in the citation of AT&T's model-based calculations.

B. Universal Service Distributions on the Basis of UNE Zones is Reasonable and Pro-Competitive

US West argues that instead of distributing universal service support to higher cost UNE zones, the Access USF proposed by CALLS should be targeted to “density zones” with less than 5 lines per square mile.[56] In essence, US West argues that Access USF support should be distributed based on smaller geographic units than UNE zones. US West’s proposal would create a mismatch between UNE loop rates, universal service support, and deaveraged SLC rates that the CALLS plan seeks to avoid. This mismatch would effectively barricade some areas from UNE loop-based entry and exacerbate regulation-based arbitrage. The CALLS plan more reasonably balances the Commission’s pro-competition and universal service goals than does US West’s proposal.

US West ignores the fact that there is nothing in the proposed CALLS plan that fixes the boundaries of UNE loop deaveraging zones. US West could, under the CALLS plan, create a highly targeted universal service distribution in its states simply by proposing and securing adoption by the state commissions of highly targeted, and highly deaveraged, UNE loop deaveraging zones. US West, however, wants to have its cake while eating its competitors' as well: US West wants to receive highly deaveraged universal service support, but to charge highly averaged UNE loop rates.

The asymmetry between universal service support and UNE loop zones would have undesirable competitive side effects. Highly averaged UNE loop prices place competitors seeking to enter lower cost markets using UNE loops at an artificial competitive disadvantage. This will be especially true in any market in which an

56 US West, at 5.

incumbent LEC is granted Phase I pricing flexibility for common line and local switching charges.[57] On the other hand, in rural areas, the mismatch between UNE rates and support zones means either that highly deaveraged support will flow to eligible telecommunications carriers purchasing lower priced, highly averaged UNEs, or a mechanism could be needed to apportion universal service payments between the UNE purchaser and the UNE seller. When the Commission has established such an apportionment, it has been challenged.[58] For these reasons, the better solution for the fund is to have UNE rates and universal service support determined according to the same boundaries.

In contrast to US West, MCI argues that the $650 million in universal service support should be targeted in greater proportion to areas that have higher multiline business SLCs, rather than to areas that have lower multiline business PICCs. While MCI's approach would lead to lower average multiline business PICC rates sooner, multiline business PICC rates will fall dramatically in any event under the modified CALLS plan, dropping almost 50% by July 2001 and almost 90% by July 2002. MCI's concern about multiline business PICC rates will rapidly be rendered moot. Moreover, MCI's approach to universal service would exacerbate the objections of US West, because US West has relatively lower PICCs than several other price cap companies,

57 Phase I pricing flexibility would permit US West to enter into contract tariffs for common line and local switching charges.

58 *See*, AT&T Petition for Reconsideration, CC Dkt. 96-45 (filed January 3, 2000).

including GTE, Bell Atlantic and BellSouth, meaning US West would likely lose universal service support under MCI's proposed distribution methodology.[59]

The CALLS plan proposes a balanced approach: UNE rates, deaveraged SLC rates, and Access USF support are all determined according to the same geographic zones. This creates a consistency among unbundled loop rates, incumbent LEC retail prices, and universal service support that will promote competition and support universal service. This is supported by other commenters, including ALTS.[60]

C. The CALLS Plan Reasonably Applies Universal Service Support to Reduce Multiline Business PICCs

Under the CALLS plan, both universal service funding and increased revenues from the caps on the primary residence and single line business SLCs are first used to offset usage-based carrier common line charges. Next, they are applied to reduce multiline business PICC charges, and finally, to permit geographically deaveraged reductions in multiline business SLCs. This progression is reasonable and appropriate. The rate "cascade" in the CALLS proposal follows the same order as current FCC rules. It focuses first on eliminating usage-based rates that are inconsistent with the manner in which underlying costs are incurred and which disproportionately harm consumer welfare. Then it works toward eliminating multiline business PICCs, which are averaged by long distance carriers and therefore transfer money from businesses in lower cost

59 In addition, MCI WorldCom's proposal to lower the support benchmark from $7.00 would not necessarily result in greater support flowing to study areas with higher multiline business PICCs.

60 Comments the Association for Local Telecommunications Services, at 7-8 (filed November 12, 1999).

states to businesses in higher cost states. The proposal permits deaveraging of SLCs within an incumbent LEC only after these other two money flows have been eliminated.

US West argues that this "cascade" precludes it from meeting competition. US West can still meet competition through voluntary reductions of urban SLCs below their price caps. In addition, once US West meets the Commission's requirements for Phase I SLC pricing flexibility, US West could enter into contracts with customers that specified the SLC rates that would apply, without regard to the price caps. Both voluntary reductions and contract tariffs will allow US West to meet its competition.

D. The CALLS Plan Complies with Section 254

Several commenters claim that the CALLS plan is inconsistent with provisions of the 1996 Act. CALLS has responded to these arguments in the previous comment round. For the Commission's convenience, we summarize those responses below.

1. *The Plan Does Not Violate Section 254(k)*

A federal court of appeals has already addressed this issue in a final order in this docket not subject to appeal, and has held that section 254(k) "is not implicated" by rules that permit incumbent LECs to use SLCs to recover loop costs.[61] CALLS cited to and explained this decision in its initial comments and reply comments.[62] Amazingly, commenters have again claimed that section 254(k) prohibits the use of a SLC to recover loop costs, without even attempting to address the contrary precedent. This is especially troubling because Texas Counsel –– one of the parties promoting the losing claim – was the appellant in the case.

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61 *Southwestern Bell Telephone Company v. FCC*, 153 F.3d 523, 559 (8th Cir. 1998).

62 CALLS November 12 Comments, at 12-14.

Section 254(k) provides:

> A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition. The Commission, with respect to interstate services, and the States, with respect to intrastate services, shall establish any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.

In the case, Texas Counsel challenged provisions of the May 1997 Interstate Access Charge Order that increased caps on multiline business and non-primary residential SLCs. Telephone service to multiline business and non-primary residential lines were – and are – included in the definition of universal service. In many parts of the country, multiline business SLCs, and to a lesser extent non-primary residential SLCs, recover all interstate allocated common line costs associated with service to multiline business or non-primary residential lines.

In the appeal, Texas Counsel argued that section 254(k) precluded recovery of all of the costs of multiline business and non-primary residential lines through SLCs. It reasoned that doing so would cause universal service to bear an unreasonable portion of the joint and common costs.[63] The Commission, in its brief before the Eighth Circuit, countered that "[t]he SLC is a method of recovering loop costs – not an allocation of costs between supported and unsupported services. Thus, section 254(k) simply does not speak to whether the Commission may raise the SLC cap."[64] The Eighth Circuit agreed with the Commission, holding that, "[b]ecause the SLC is a method of recovering loop

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[63] The Commission has defined universal service to include service to multiline businesses and non-primary residential lines. *See*, *First Universal Service R&O*, at ¶ 96.

[64] Brief of the FCC at 148, *Southwestern Bell v. FCC*, Nos. 97-2618 *et. al.*, (filed October 28, 1997).

costs, not an allocation of those costs between supported and unsupported services, § 254(k) is not implicated."[65]

The SLC does not amount to an allocation of costs between supported and unsupported services because both local service and access to interexchange service are supported services included in the definition of universal service, as that term is used in section 254(k). Among other things, the term "universal service," as defined by the Commission when it implemented section 254, includes local service and "the use of the loop, as well as that portion of the switch that is paid for by the end user . . . necessary to access an interexchange carrier's network."[66] Therefore, the SLC, which is a mechanism for recovering the interstate allocated costs for use of the loop, as well as that portion of the switch that is paid for by the end user necessary to access an interexchange carrier's network, does not cause "services included in the definition of universal service [to] bear [] more than a reasonable share of the joint and common costs of facilities used to provide those services."[67]

2. *The CALLS Plan Is Fully Consistent With Section 254(g)*

Section 254(g) provides that rates charged by providers of interexchange telecommunications services shall be no higher in rural and high cost areas than in urban

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65 *Southwestern Bell*, at 559.

66 *See, First Universal Service Order*, at ¶ 76.

67 47 U.S.C. § 254(k); Several commenters also rehash the argument that SLCs violate the Supreme Court's command in *Smith v. Illinois Bell*, 282 U.S. 133, 148-149 (1930). As discussed in the CALLS initial Reply Comments, at 26-27, this argument has also been soundly rejected by a United States Court of Appeals. *NARUC v. FCC*, 737 F.2d 1095 1112 (D.C. Cir. 1984). The D.C. Circuit rejected the contention that *Smith* barred recovery of interstate allocated loop costs through a fixed line charge, holding that "[the *Smith* Court] did not hold that the FCC must order recovery of costs allocated to its jurisdiction through usage-based charges." *NARUC*, at 1112.

areas, and that rates be no higher in one state than in another.[68] Previously, NRTA/NTCA suggested that this section would apply to the SLCs charged by incumbent LECs as structured under the CALLS plan.[69] Though they have abandoned that position in this round of comments, another commenter revives their strawman argument.[70]

Section 254(g) expressly applies to interexchange service, not to exchange access. PICCs cover loop costs that are incurred by the incumbent LEC. The fact that the recently created PICC results in those costs now being passed on to the IXC (which subsequently recovers them through end-user pass through charges) does not forever transform loop costs – which are costs of local exchange or exchange access services – into a charge for interexchange service. Thus, incorporating the PICC into the SLC does not "evade" either the letter or the spirit of section 254(g).

Having failed with their first argument, NTCA/NRTA return in this comment cycle with issues affecting rural and rate of return carriers that are beyond the scope of this docket.[71] It is important to note, however, that customers of rural and rate of return carriers today are assessed PICC-pass through charges by the interexchange carriers.

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68 47 U.S.C. 254(g). Section 254(g) provides: "Within 6 months after the date of enactment of the Telecommunications Act of 1996 [enacted Feb. 8, 1996], the Commission shall adopt rules to require that the rates charged by providers of interexchange telecommunications services to subscribers in rural and high cost areas shall be no higher than the rates charged by each such provider to its subscribers in urban areas. Such rules shall also require that a provider of interstate interexchange telecommunications services shall provide such services to its subscribers in each State at rates no higher than the rates charged to its subscribers in any other State."

69 Comments of the National Rural Telecom Association and National Telephone Cooperative Association, at 5-9 (filed November 12, 1999)("NRTA/NTCA").

70 Vermont PSB and DPS, at 8**.**

71 "The modified CALLS proposal . . . is by its terms, inapplicable to NTCA and NRTA members or other rate-of-return local exchange carriers." NRTC/NTCA, at 2.

When the IXCs eliminate PICC pass-through fees, these customers will likewise see a drop in their telephone bill, saving them approximately $120 million per year.[72]

3. *The Statute, Case Law, and FCC Decisions Permit Collection of Universal Service Contributions As An Explicit Line Item*

Texas Counsel/CFA/CU reiterate their argument that collection of universal service contributions by the incumbent LEC through an explicit end user charge violates section 254(d) of the Act.[73] Specifically, they complain that "[i]f subscribers are forced to pay a line item surcharge then telecommunications service providers are not contributing."[74] This argument misreads the Act, ignores the Fifth Circuit's decision in *Texas Office of Public Utility Counsel v. FCC*, and overlooks the FCC's orders implementing the Fifth Circuit's decision.

Section 254(d) simply states that "[e]very telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and non-discriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service."[75] Nothing in section 254(d) prohibits any telecommunications carrier from recovering its universal service contributions from its customers, and the Commission has never interpreted the

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72 Updated Pociask Report, at 17-18.

73 Texas Counsel/CFA/CU, at 37-39. Previously, the National Association of State Utility Consumer Advocates had joined in this argument, though they have not done so in this round of comments. *See*, Comments of the National Association of State Utility Consumer Advocates at 20 (filed November 10, 1999).

74 Texas Counsel/CFA/CU, at 37.

75 47 U.S.C. § 254(d).

Act to limit such recovery.[76] Given that the revenues of telecommunications carriers are derived one way or another from customers, the statute cannot be read to support a distinction between direct end user charges and recovery that is incorporated into a carrier's other rates. Thus it is a fallacy for Texas Counsel/CFA/CU to suggest that the elimination of implicit subsidies and creation of an explicit funding mechanism "shifts the entire cost of universal service onto end users."[77] As the source of IXC revenues, consumers inevitably cover that economic cost, whether it takes the form of an express charge or a component of another rate element.[78]

End users charges for universal service are also consistent with the Fifth Circuit's recent ruling in *Texas Office of Public Utility Counsel v. FCC*[79] and with the Commission's implementation of that decision. The Fifth Circuit reversed FCC rules that required price cap carriers to obtain any recovery of universal service contributions through adjustments in carrier-to-carrier interstate access charges. The court held that this requirement constituted "implicit" rather than "explicit" universal service support contrary to section 254(e).[80]

In implementing that decision, the Commission permitted price cap incumbent LECs to begin recovering universal service contributions through an express line-item

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[76] *See*, *Universal Service First R&O*, at ¶ 855. *See also*, Federal-State Joint Board on Universal Service, *Twenty-First Order on Reconsideration*, CC Dkt. No. 96-45, FCC 00-118, at ¶ 11 (rel. April 11, 2000).

[77] Texas Counsel/CFA/CU, at 37.

[78] Texas Counsel/CFA/CU may simply prefer that such costs remain hidden to the consumer, as they argue: "The law does not say funding must be explicit to the customer, it says it must be explicit to the provider." Texas Counsel/CFA/CU, at 38.

[79] *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5th Cir. 1999).

[80] *Id*, at 425.

charge to end users.[81] Therefore, the CALLS plan does not grant price cap LECs additional means of recovering universal service contributions other than those already permitted under now-existing Commission rules.

IV. THE MODIFIED CALLS PRICE CAP PLAN ASSURES THAT ACCESS RATES WILL FALL, WHILE ALSO PROMOTING THE COMMISSION'S COMPETITION POLICIES

As an integrated part of the CALLS plan, the modified price cap plan reduces total access charges in a manner designed to further the plan's overarching goals: promoting rapid, facilities based competition; increasing incentives for investment and innovation by both incumbent LECs and entrants; reducing regulation through increasing reliance on marketplace competition over time; and increasing certainty through a stable, five-year price cap plan. This proposal does not further any one of these policy interests at the cost of another, but instead attempts to find a reasonable balance amongst these competing public policy interests.

To strike this balance, CALLS proposes a price cap regulation mechanism that has several interrelated features:

- All X-factor reductions from common line and switched access rate elements are targeted to reduce local switching and transport rates to target rates of $0.0055 per minute for the RBOCs and GTE, $0.0065 per minute for most mid-sized price cap LECs, and $0.0095 for companies serving only extremely rural areas.[82]

[81] Federal-State Joint Board on Universal Service, *Sixteenth Order on Reconsideration* in CC Dkt. No. 96-45, *Eighth Report and Order* in CC Dkt. No. 96-45, and *Sixth Report and Order* in CC Dkt. No. 96-262, FCC 99-290, at ¶ 33 (1999) ("*Universal Service Sixteenth Order on Reconsideration*").

[82] *See*, Valor/CALLS Joint *Ex Parte* letter to Larry Strickling, Chief Common Carrier Bureau (filed April 14, 2000). In the most rural areas, to the extent that the target rate is reached prior to June 30, 2004, price cap reductions using an X-factor of 6.5% will continue for the CMT basket until the earlier of when CCL is eliminated or June 30, 2004.

- Once local switching and transport rates reach their target rates, the X-factor in the price cap formula is set equal to inflation (not 0 as some commenters appear to suggest).[83]

- Participating price cap LECs will make an up-front reduction to their price caps for local switching and transport by a percentage of local switching revenue (approximately 40% of local switching revenue) such that total per minute access rates, including carrier common line charges, local switching charges, and transport charges, fall by $2.1 billion.

- Special Access rates will also continue to be reduced by applying an X-factor of 3% in 2000, and an X-factor of 6.5% from 2001 until 2003.

As if jointly seeking to illustrate the reasonableness of the CALLS plan, ALTS and Level 3 attack the CALLS plan from diametrically opposing sides. Level 3, on the one hand, criticizes the CALLS plan for not immediately seeking to reduce access rates to levels reflecting reciprocal compensation rates.[84] ALTS/Time Warner and CPI, on the other hand, criticize the CALLS plan for too rapidly reducing local switching and transport rates.[85] Level 3 declares that "market forces have failed to reduce ILEC access rates,"[86] while ALTS/Time Warner argues "it is simply too early in the development of competition for the Commission to abandon its reliance on competition to drive down access charge prices…."[87]

The modified CALLS proposal steers a middle course between these two opposing viewpoints. By targeting X-factor reduction to average traffic sensitive rates,

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83 *See,* NASUCA April 3, 2000 Comments, at 5, 9.

84 Comments of Level 3 Communications LLC, at 7-9 (filed November 12, 1999); *see also,* Level 3 (April 3 Comments), at 2-3. This presumes access rates are above forward looking cost, which may not be true for all rate elements and for all carriers. *See* Reply Comments of Sprint Corporation, at 7 (filed December 3, 1999).

85 ALTS/Time Warner, at 9-10.

86 Level 3, at 3.

87 ALTS/Time Warner, at 8.

and by taking an additional, voluntarily-agreed upon reduction of local switching revenues to yield a $2.1 billion minute of use rate reduction on July 1, 2000, the modified CALLS proposal reduces access rates substantially. This substantial reduction in per minute access rates, when passed through to toll rate reductions as AT&T and Sprint have committed, creates a substantial increase in consumer welfare.[88] However, by not reducing those rates to the extent proposed by Level 3, the CALLS proposal reduces the risk that regulation could force per minute rates to predatory levels.[89]

MCI, NASUCA, CPI, and Texas Counsel/CFA/CU argue that although the CALLS plan reduces total access revenue below the levels that would otherwise result in July 2000, the modified CALLS plan will result in consumers directly or indirectly paying higher total access charges over time than would occur under "current rules."[90] This argument is misleading because of its hidden assumptions. First, because the D.C. Circuit reversed and remanded the last X-factor order to the FCC for further consideration,[91] it is not at all clear what the correct baseline X-factor would be.[92] Second, inflation will vary. Inflation today is lower than when the Commission adopted the last access charge order in 1997, but it has increased over the last year. MCI's

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88 *See,* Comments of Alliance for Public Technology, Communications Workers of America and National Development Organization, at Appendix A, Stephen Pociask, "An Assessment of Consumer Welfare Effects of the CALLS Plan" (filed November 16, 1999).

89 Neither ALTS nor Focal argues that a $0.0055 per minute average traffic sensitive for the RBOCS and GTE would be a predatory rate.

90 MCI WorldCom, at 9; Comments of the Competition Policy Institute on the Revised CALLS Proposals, at 2, 4-5; NASUCA, at 10; Texas Counsel/CFA/CU, at 9-10.

91 *United States Telephone Ass'n v. FCC*, 188 F.3d 521 (D.C. Cir. 1999).

92 CALLS members differ in their proposals as to the appropriate level of the X-factor and productivity.

projections demonstrate this point precisely. MCI significantly overstates X-factor reductions under the "current rules" case and significantly understates the CALLS "upfront" additional reduction because inflation is 2.02%, not 1.4% as indicated in MCI's calculations. Recent increases in gasoline and oil prices are likely to further increase inflation. Indeed, depending on the rate of inflation, the CALLS plan could result in lower total price cap incumbent LEC revenues over 5 years than would result from X-factor reduction of 6.5% every year for 5 years, even excluding access revenue reductions resulting from increased competition resulting from the CALLS plan.

The static comparisons that these commenters make ignore the most significant marketplace development over the next five years – increasing local competition. A variety of analysts and the Commission staff itself have forecast increasing competition, even in residential markets.[93] In its report "Telecommunications Act @ the Millenium," the Commission's staff projects that fully half of American cable households will have a choice between the incumbent LEC and a local cable operator as suppliers of voice grade telephone service.[94] Increasing competition – particularly increasing residential competition – will increase market pressure on these rates.

Even if aggregate access revenues theoretically can be higher under the CALLS plan than under today's rules frozen in place, the CALLS price cap plan is more consistent with and tailored to promoting the development of competition in the local exchange market. Under CALLS, price reductions are disproportionately taken in the

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93 *See*, e.g., Tod Jacobs, "Bell Atlantic, GTE & Bell Atlantic-GTE Pro Forma," Sanford C. Bernstein, Inc. Conference Call Handouts, at 8 (January 4, 2000); Scott Cleland, "Telecom Competition Update: Seeing the Forest, Not the Trees," Legg Mason Research Report (April 3, 2000).

94 Telecommunications Act @ the Millenium, at 10.

first two years, with substantial initial reductions in excess of those that would flow from an X of 6.5% alone. This "front-end loading" of price reductions means that prices will be reduced most sharply in the initial years, when residential and small business competition is least developed. In later years, when competition in residential and small business markets should be growing significantly, the price caps are frozen (subject to exogenous adjustments) and additional price reductions at that point will be driven by the marketplace.

The CALLS plan's shift to a flatter rate structure further increases the likelihood that marketplace-driven reductions will occur during the later years of the plan. By targeting X-factor reductions to switched access rates and making additional upfront price reductions in switched access rates, the CALLS price cap plan promotes competition by creating a "flatter" rate structure, with flat rate end user charges comprising a greater proportion of total access recovery. NASUCA, Texas Counsel, and CPI, in criticizing the fact that CALLS creates a flatter rate structure, wholly ignore the procompetitive benefits of the flatter structure by simply presuming that loop facilities will never be subject to competition. As the FCC staff report recognized, this presumption is not reasonable even for residential customers – broadbased residential competition will be increasing dramatically over the next 5 years.

The flatter rate structure that results from CALLS promotes competition in three ways. First, it stops using regulation to drive down common line rates that may already be below even forward looking cost in many areas. Half of price cap companies today recover less in common line revenues per line than the interstate share of HCPM-projected loop and port costs plus marketing.[95] When common line price caps fall below the forward looking costs of loop and port and associated retail costs, regulation creates barriers to entry and stymies competition.

Second, a flat rated, end user focused rate structure encourages investment in alternative loop facilities, whether wireline or wireless. NASUCA and CPI attempt to turn this economic reality on its head by arguing that shifting rate structure proportionately toward flat rates “shields” charges from competition. What NASUCA and CPI ignore is that open entry by facilities based carriers precludes “shielding” any revenues from competition. Instead, a flatter rate structure focuses and rewards competition in loops, where entry is less prevalent, rather than competition in switches and transport facilities, where the costs of entry are much lower and where competition is most prevalent today.

Third, CALLS' flatter rate structure closes the gap between today's access rates and the even more flat rate prices that are likely to result as companies migrate from circuit-switched network technology toward packet-based networks. This will facilitate the development of packet-based services as a substitute for traditional circuit switched telephony and will improve the range of choices available to consumers. This further increases the prospects for market-driven, competition-based price reductions in the later years of the plan.

These pro-competitive benefits of a flatter rate structure also refute ALTS' and Focal's arguments that there is no rational basis for focusing price cap reductions on switched access rates rather than spreading those reductions uniformly across common

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95 *See*, chart attached to Letter of John T. Nakahata to Magalie Roman Salas dated February 10, 2000.

line and switched access rates.[96] Nowhere does Focal, ALTS, or any other CLEC argue that the rate caps for switched access under the CALLS plan are predatory. In fact, ALTS/Time Warner's alternative plan embraces the CALLS plan's target rates for switched access.

ALTS/Time Warner and Focal get off on the wrong track in part because they assume that the X-factor under CALLS is still supposed to be a measure of productivity changes. As previously explained, however, CALLS uses the 6.5% X-factor to prescribe the glidepath from current rates to the switched access target rates because it is a rate of aggregate revenue reduction that the industry had already incorporated into existing financial projections and business plans.[97] The level of productivity, the appropriate method for calculating productivity, and whether productivity changes are uniform across incumbent LEC rate elements, are irrelevant to the CALLS proposal.

Both the Commission and the antitrust laws are clear that the goals of competition policy are to protect competition, not competitors. Neither ALTS nor Time Warner articulates a harm to competition. Instead, as ALTS/Time Warner make plain, their concern is protecting a "major source of CLEC revenues" because "the vast majority of

[96] ALTS/Time Warner, at 8-9; Focal at 9-10; *See also*, Comments of Cincinnati Bell Telephone Company and Broadwing Communications Inc., at 5-6 (filed April 3, 2000) ("CBT"), and Global Crossing, at 11 (claiming that tandem transport rates should receive at least their proportionate share of reductions to ensure that plan is competitively neutral). As existing Commission rules prohibit charging predatory rates or otherwise engaging in anticompetitive pricing practices, the Commission should permit incumbent LECs to determine which rates to lower.

[97] August 20 Memorandum, at 36-37; CALLS December 3 Replies, at 47-48; Cincinnati Bell/Broadwing and Global Crossing similarly err by assuming that the X-factor under the CALLS plan still measures productivity, as opposed to simply describing a glidepath for aggregate access price changes. CBT at 2-3; Global Crossing at 2, 8-9. As such, previous studies regarding the appropriate way in which to measure productivity for mid-size LECs do not bear on the appropriate level of X for the purposes of creating a glidepath to an access price freeze.

the access revenues associated with these [large and medium sized business] customers is in the form of per minute access charges."[98]

ALTS is correct in its observation that "only facilities-based competition can ultimately render regulation unnecessary."[99] But ALTS/Time Warner, Focal, and Allegiance critically and carefully ignore where competition has developed to date, and where it has not. Time Warner, Focal, and Allegiance all serve urban business markets.[100] The competition that the CALLS plan seeks to promote is competition outside these narrow markets – competition for residential and small business customers across the country. If the "pro-competitive, deregulatory" approach of the 1996 Act is to succeed, facilities-based competition must be widely promoted, not just in urban business markets.

Texas Counsel/CFA/CU and NASUCA propose changes in price regulation that would distort and impede competition in a different way, for the sake of justifying low end user fixed rate line charges. Texas Counsel/CFA/CU would flash cut over $4 billion in line charge reductions based on their projection of nationwide forward-looking

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98 ALTS/Time Warner, at 10.

99 ALTS/Time Warner, at 3.

100 Time Warner's website, for example, lists 23 "cities" in which it provides service. *See*, http://www.twtelecom.com/TimeWarnerCities/index.html. Time Warner Telecom's 1999 10-K (annual Report) describes Time Warner Telecom as focusing on "metropolitan areas that have high concentrations of medium- and large-sized businesses" and states that the company historically "has focused its sales and marketing efforts on such businesses." *See*, http://www.twtelecom.com/Investor/67512-gd.pdf. Focal's website similarly shows 20 cities/urban areas in which it provides or is developing service. *See*, http://www.focal.com/about_/service_areas_fr.html. Allegiance, in its comments, states that it serves 36 major metropolitan areas. According to Allegiance's 1999 10-K (Annual Report), "With a strategy focusing on the central business districts and suburban commercial districts in these areas, Allegiance plans to address a majority of the non-residential access lines in most of its targeted markets."

costs.[101] This proposal, and its underlying analysis, is greatly flawed. For example, Texas Counsel/CFA/CU use all of the existing high cost funding – the vast majority of which goes to non-price cap carriers – to offset interstate allocated line costs for price cap companies.[102] This application of federal universal service support is simply wrong. The adjustments Texas Counsel/CFA/CU propose for second residential lines are likely already accounted for in the HCPM methodology, which uses all lines geocoded by customer location as an input to the model calculations. Furthermore, the Texas Counsel/CFA/CU extrapolate their conclusions from analysis of a single state.[103] This is implausible as a basis for nationwide access rate level decisions.

Texas Counsel/CFA/CU also inaccurately characterize the FCC as having decided that "[f]orward-looking economic costs must be the basis for establishing prices."[104] Although the FCC has used forward-looking costs as the basis for prices for carrier-to-carrier interconnection and unbundled network element prices,[105] the Commission has not decided that forward looking costs should be used to determine total interstate recovery.

Finally, the availability of the Lower Formula Adjustment Mechanism ("LFAM") does not mean consumers will be "robbed" of the benefits of reductions after the first

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[101] Texas Counsel/CFA/CU, at 57. Although the comments purport to use the FCC Hybrid Cost Proxy Models, in order to reach their desired results, those results are then adjusted further based on hypothetical impacts of second line growth. These adjustments appear to "double count" second lines, because the FCC HCPM uses all lines, including multiple residential lines, as inputs. Even the portion that goes to price cap carriers does not offset costs recovered today through those carriers' interstate access rates.

[102] Texas Counsel/CFA/CU, at 21. Even the portion that goes to price cap carriers does not offset costs recovered today through those carriers' interstate access rates.

[103] Texas Counsel/CFA/CU, at 21.

[104] Texas Counsel/CFA/CU, at 13.

[105] These matters are on review before the Court of Appeals.

year. LFAM only applies where the interstate rate of return falls below 10.25%, not the full, authorized 11.25% level, and the vast majority of price cap LECs are above that level. MCI's principal objection – that LFAM could increase multiline business PICC charges – will be rapidly reduced as the multiline business PICC rates themselves fall.

Legal issues aside, the Texas Counsel/CFA/CU proposal is also bad competition policy. The Commission should recognize that when it is projecting forward looking cost, there is a risk that its projections will be wrong. If Texas Counsel/CFA/CU are wrong in their assumptions about the average level of forward looking loop and port costs, then setting prices and common line recovery at those low levels would erect a substantial barrier to entry which the market could not be expected to correct. On the other hand, if the Commission permits prices to be above the forward-looking costs projected by Texas Counsel/CFA/CU, and actual costs are as low as they project, competitive entry by other facilities-based providers can be expected to bring prices down toward cost. Texas Counsel/CFA/CU invite the Commission to set access rate levels using the "visible hand" of regulation based upon the Commission's omniscience. The Commission should decline such an invitation.

The CALLS plan's price cap proposal strikes a reasonable balance between and among the Commission's competing policy objectives. It reduces usage rates without driving them to predatory levels, which increases consumer welfare and economic efficiency without harming competition. It maintains price regulation as a means to check market power, retaining the efficiency incentives inherent in price cap regulation. It targets price cap reductions in a manner that promotes investment in loop-substitute distribution facilities, increasing the likelihood that competition will both drive future price decreases for consumers and permit greater deregulation. No other commenter has put forward a plan that attempts to reconcile this diverse range of Commission policy objectives. For this reason, the CALLS plan's price cap proposals are reasonable and the Commission should adopt them in time for implementation by July 2000.

V. NEITHER THE TEXAS COUNSEL/CFA/CU ALTERNATIVE NOR THE ALTS/TIME WARNER ALTERNATIVE REASONABLY BALANCES THE FULL RANGE OF PUBLIC POLICY CONCERNS

Two parties, Texas Counsel/CFA/CU and ALTS/Time Warner offer “alternative” plans to the modified CALLS plan. Neither plan is as comprehensive as the CALLS plan. Both of these alternatives will do little or nothing to help address the core issues of universal service reform that the Commission must resolve. Both of the alternatives also would hobble the development of broad-based local telecommunications competition, especially outside of central business districts. Both alternatives should be rejected, and both highlight the reasonable public policy balance underlying the CALLS plan.

A. Texas Counsel/CFA/CU

The Texas Counsel/CFA/CU plan is clearly a plan framed with only one goal in mind – driving residential SLCs to the lowest possible levels. In its plan, Texas Counsel/CFA/CU would reduce all subscriber line charges by $1.00, remove all PICC charges from consumers' bills (although leaving a $0.50 per line PICC on all long distance carriers which somehow, inexplicably, is not passed on to consumers), cut incumbent LEC revenues by $4 billion before applications of the next X-factor adjustment, and continue X-factor reductions targeted to reduce switched access to $0.0055 per minute. The plan creates no additional universal service support to replace support currently implicit in interstate access rates.

Among its other defects, this plan fails even minimally to address universal service concerns. The widely acknowledged reality, reflected by the Commission in its methodology underlying the new federal intrastate high cost fund, is that rural areas with low teledensities are much more costly to serve than dense urban areas. This plan appears to assume that as long as incumbent LECs serve both rural and urban areas, rates can be sustainably set on the basis of average cost, and that such a result can be sustained economically even as new competitors enter to compete only in the urban markets. The FCC has already recognized in creating the new intrastate high cost fund that subsidy-through-averaging is unsustainable and ultimately must be replaced with explicit universal service support. Texas Counsel/CFA/CU appear to be proposing a policy premised on the continuation of monopoly, even when the evidence is that competition is advancing, particularly in urban and business markets. The Commission should decline this invitation to hang up on rural America and aggravate the Digital Divide.

To make matters worse, the Texas Counsel/CFA/CU plan would result in residential SLC rates that are well below costs and even below the interstate share of HCPM estimated forward looking loop and port costs in every wire center in the country.[106] This means that, according to the HCPM, the prices proposed under the Texas Counsel/CFA/CU plan would create a barrier to entry in every market in the country.

These results alone combine to make the Texas Counsel/CFA/CU plan a competitive disaster for the country. Rural, small town Americans and residential consumers in all areas would be denied the new services and better values that

106 The Texas Counsel/CFA/CU plan would result in a primary residential SLC of $2.50, which is less than 25% of loop and 15% of port costs projected by the HCPM.

competition will likely bring. In the 1996 Act, Congress fundamentally rejected this vision of guaranteeing low prices through a tightly regulated monopoly.

The bottom line on the Texas Counsel/CFA/CU plan is to use regulation artificially to lower per line charges at the expense of:

- Squelching residential competition;
- Precluding any explicit universal service support for high cost areas, guaranteeing that those areas will have no competitive choices for telephone service and no market-driven infrastructure investment;
- Preventing the growth of competition and thereby ensuring a need for long-term, continued regulation;

This bottom line ultimately harms, rather than helps, a more competitive telecommunications future in which rural and urban Americans see greater services, and expands, rather than closes, the Digital Divide. The Texas Counsel/CFA/CU plan does not reasonably accommodate the range of public policy interest with which the Commission must grapple.

B. ALTS/Time Warner

Although ALTS/Time Warner come at their proposal with different objectives, they also fail to protect universal service, close the Digital Divide, or promote the type of broad-based competition that will benefit residential consumers and permit deregulation. ALTS/Time Warner would establish a universal service fund of $300 million, as compared with $650 million under CALLS. They would permanently cap the primary residence SLC at $4.35, reduce access charge by a one-time reduction of $200 million split between common line and switched access charges (as opposed to a $700 million reduction under the CALLS plan). ALTS would also use X-factor reductions to reduce

CCL and multiline business PICC charges, on the one hand, and switched access rates on the other, on a 50/50 basis.

This plan also has several obvious shortcomings. First, ALTS shortchanges rural America – areas not generally served by ALTS members – by "low-balling" universal service support to the low end of the range of estimates in the record. Second, a clear result of ALTS' plan is to slow per minute access rate declines from what would occur under the CALLS plan. This is not in the public interest. It would mean higher long distance bills for consumers, with a significant loss in consumer welfare compared to the CALLS plan. The only beneficiaries of such a proposal would be ALTS members, who would have a higher price umbrella for their own access rates. Third, by maintaining a "one-size-fits-all" SLC cap, ALTS further dampens any prospects for investment in rural competition. Notably, rural consumer commenters – such as the National Grange and the National Association of Development Organizations – have filed in support of the CALLS proposal, notwithstanding higher SLC caps.[107]

It is significant that nowhere does ALTS challenge as predatory the per minute rates permitted under the Modified CALLS plan. Indeed, ALTS embraces these rates in its alternative plan. The Commission should decline ALTS invitation to manipulate price caps and rate structures to hold up an otherwise falling price umbrella. The ALTS plan is fundamentally anti-consumer and anti-competition.

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107 National Grange (filed February 24, 1999); NADO (filed November 12, 1999, December 3, 1999, and April 3, 2000).

VI. THE COMMISSION SHOULD NOT BE DISTRACTED BY ISSUES THAT HAVE NO SUBSTANTIAL NEXUS TO THIS DOCKET

Several commenters suggest that the Commission must resolve issues that are truly tangential to the matters presented in this docket. These are essentially "me too" pleadings, and the Commission should decline the invitation to remove them from consideration within their proper dockets.

A. Payphones

Several commenters raise issues unique to the pay telephone industry.[108] Seeking to "piggy-back" on the CALLS proposal, they invite the Commission to "[use] the opportunity presented by the CALLS proposal to clarify that pay telephone access lines should be treated as single line business lines rather than multiline business lines for purposes of the [PICC]."[109] In addition, they request either that the PICC and SLC be entirely eliminated for pay telephone lines,[110] or that the PICC presently assessed on pay telephone lines be combined with the SLC and assessed directly on the location provider.[111] Resolution of these issues is not central to adoption of the CALLS proposal. Furthermore, commenters themselves recognize that these are live issues pending in another proceeding.[112] These issues can and should be resolved in that docket.

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108 Comments of American Public Communications Council (filed April 3, 2000); Supplemental Comments of One Call Communications, Inc. ("Opticom") (filed April 3, 2000), and Comments of Operator Ccommunications, Inc. (filed April 3, 2000).

109 OCI, at 2.

110 APCC, at 2.

111 OCI at 3, 7; Opticom, at 1,7.

112 Opticom acknowledges that it has made these same requests in its comments responding to the Commission's *Payphone PICC Notice*. Public Notice, *Commission Seeks Comment on Specific Questions Related to Assessment of Presubscribed Interexchange Carrier Charges on Public Payphone Lines*, DA 98-845 (May 4, 1998). *See*, Comments

B. CLEC Access Charges

Several commenters assert that the Commission should not proceed with the CALLS proposal unless it is able simultaneously to resolve access charge and universal service reform for CLECs.[113] This proceeding, however, addresses the interstate access rates charged by incumbent LECs, historically part of the mechanism carriers have used to maintain universal service, and how these universal service mechanisms can be rendered explicit, consistent with the requirements of the 1996 Act. The issue of whether CLEC rates, particularly rates for access, should be capped or otherwise subject to some form of regulation, does not raise universal service concerns, nor does it relate to price cap regulation for incumbent LECs. Accordingly, CLEC access charge issues and this proceeding are not intertwined and can be decided separately.

C. High Cost Universal Service Fund

NTCA/NRTA request that if the Commission adopts the proposed $650 million portable interstate access universal service fund, it simultaneously lift the cap on the existing high-cost universal service support fund.[114] The cap is a limitation that the Commission imposed on universal service for high cost support, and it primarily affects support for non-price cap carriers. Accordingly, any decision concerning the high cost cap is beyond the scope of this proceeding.

Continued . . .

of One Call Communications, Inc., Assessment of Presubscribed Interexchange Carrier Charges on Public Payphone Lines (filed May 26, 1988).

113 Comments of the Rural Independent Competitive Alliance, at 2,5 (filed April 3,2000); Comments of Allegiance Telecom, Inc., at 3,4 (April 3, 2000).

114 NTCA/NRTA, at 14.

VII. THE CALLS PLAN HAS BEEN SUBJECT TO OPEN AND ROBUST PUBLIC DEBATE

The CALLS plan is a product of open debate. It has its genesis as a compromise agreement among carriers of historically divergent views and economic interests. The fact that the CALLS members have reached accord on the difficult and far–ranging issues addressed by the CALLS plan is itself a powerful reason to support implementation of the CALLS plan and, here, the adversarial nature of the parties has served the ultimate beneficiary – the consumer – well. The Coalition has sought participation and input from the fullest array of sources, talking with anyone who sought to do so.[115] Indeed, in order to facilitate a full vetting of its proposals, CALLS and its members have voluntarily filed extensive supporting materials, such as complete draft rules and economic analyses. The March 8 modifications – a slower, primary residential SLC cap progression and large upfront access rate reductions, well in excess of those required under current rules – are a direct response to the comments and suggestions of public interest groups, end users, state commissions, and Commission staff. The agreement of numerous parties with diverse interests has always, and rightly, been viewed by the Commission as a factor favoring the adoption of a rule, in conjunction with the Commission's independent determination that the adoption of the rule would advance important public interest goals.

Although the CALLS proposals were developed and advanced by CALLS members, the original and modified plans have been subject to, and benefited from, full formal public comment at the Commission. After the original proposal was submitted,

[115] Although Allegiance Telecom claims to have been "deliberately excluded" from the negotiations process, this simply is not true. Allegiance, at 2. Over the course of the last 13 months, Allegiance has never requested to meet with CALLS to discuss the proposal.

36 comments and 25 reply comments were received. More recently, the Commission sought additional public comment on the revised plan, and 39 further comments have been received. This proceeding has met and exceeded all legal requirements for rulemaking proceedings, and full notice has been given of the entire scope of the CALLS proposal.

In particular, the Commission should give no weight to allegations by MCI WorldCom that the CALLS members have sought improperly to link the outcome of the CALLS plan to issues raised in other dockets. In addition, while CALLS welcomes the Commission's continued informal consultation with the Federal-State Joint Board on Universal Service ("Joint Board"), in ways that do not delay adoption of the plan beyond July 1, 2000, no formal referral of issues to the Joint Board is warranted or required. The time for action is now.

A. CALLS Has Not Tied The Outcome of This Proceeding to Other Dockets

In its comments, MCI WorldCom states: "The suggestion has been made that CALLS members have attempted to tie the outcome of the CALLS plan to issues raised in at least two separate proceedings.[116] The record in this docket reflects literally hundreds of *ex parte* presentations by a diverse group of parties, including presentations by CALLS and CALLS members, MCI, and numerous other proponents and opponents of the CALLS plan. Such presentations are consistent with the Commission's rules governing permit-but-disclose rulemaking proceedings.[117] Concerning the resolution of the two proceedings raised – rulemakings concerning a "use" restriction for certain UNEs

[116] MCI WorldCom, at 5. MCI WorldCom does not substantiate these allegations.

[117] 47 C.F.R. § 1.1206.

and the depreciation rules – the CALLS Coalition has no position. Individual CALLS members have taken strong – and opposing – positions on the record in those dockets. Those matters are under consideration in separate dockets, and they should be resolved on the merits in those dockets.[118] The separateness of these matters, and the impossibility of a CALLS Coalition position, is only underscored by the diversity and polarity of the views of individual CALLS members expressed, appropriately, in those other dockets.[119] The Commission should adopt the CALLS proposal based on its own merits and solely on the basis of information in this record.

B. The Commission Has Fulfilled the Requirements of Section 254(a)(1)

The universal service issues implicated in this docket – the removal of implicit subsidies from interstate access charges and the creation of explicit support mechanisms – have twice been formally referred to and reported on by the Joint Board. In addition, the State members of the Joint Board have had full opportunity to consult with the Commission.[120] Several commenters suggest, however, that the Commission should consult further with the Joint Board before adopting the CALLS Plan. In addition, the

[118] In the Matter of 1998 Biennial Regulatory Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, *Further Notice of Proposed Rulemaking*, CC Dkt. 98-137; CC Dkt. 99-117; AAD File No. 98-26 (rel. April 3, 2000); In the Matter of Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Dkt. No. 96-86, *Third Report and Order and Fourth Further Notice of Proposed Rulemaking* (released Nov. 5, 1999).

[119] Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, CC Dkt. No. 96-98, *Fourth Notice of Proposed Rulemaking*, Comments of Sprint Corporation (filed January 19, 2000); Comments of AT&T Corp. (filed January 19, 2000); Comments of GTE (filed January 19, 2000); Comments of BellSouth (filed January 19, 2000); Comments of SBC (filed January 19, 2000).

[120] The Commission has twice sought comment on the CALLS proposals, both of which included the same universal service provisions, and the State members of the Joint Board have filed comments on the plan. Supplemental Comments of the State Members of the Federal-State Joint Board on Universal Service (filed April 3, 2000).

California Commenters request that one aspect of the CALLS plan be referred to the Joint Board.[121] CALLS has no objection to informal consultation, but strongly objects to any further delay in this proceeding that would preclude implementation of the plan by July 1, 2000.

Section 254(a)(1) required the Commission, within a month of the passage of the Telecommunications Act, to refer "a proceeding to recommend changes in any of its regulations in order to implement sections 214(e) and [254]…" to a new Joint Board on universal service.[122] The Commission referred its Universal Service NPRM to the Joint Board,[123] which returned with a recommended decision addressing "a new set of universal service support mechanisms that are explicit and sufficient to address the universal service support principles enumerated in the statute…."[124] A second referral followed in July 1998, and more specifically directed the Joint Board to consider issues which the CALLS Plan now addresses. The referral posed the following question:

> To the extent that federal universal service reform removes subsidies that are currently implicit in interstate access charges, whether interstate access charges should be reduced concomitantly to reflect this transition from implicit to explicit support, and

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121 California Commenters, at 7; Specifically, the California Commenters request a referral "to study and evaluate the ramifications of the revised CALLS proposal to extend universal service support to non-primary residential and multi-line business" lines. *Id*, at 3. As indicated previously, service to multiline business and non-primary residential lines is included in the definition of universal service. Thus, the provision of support is not novel and does not warrant referral to the Joint Board. *Universal Service First R&O*, at ¶ 96.

122 47 U.S.C. 254(a)(1). *See also*, 47 U.S.C. § 410(c).

123 In the Matter of Federal-State Joint Board on Universal Service, *Notice of Proposed Rulemaking and Order Establishing Joint Board*, 11 FCC Rcd 18092 (1996).

124 In the Matter of Federal-State Joint Board on Universal Service, *Recommended Decision*, 12 FCC Rcd 87 (1996).

> whether other approaches would be consistent with the statutory goal of making federal universal service support explicit.[125]

The referral also inquired about the appropriate methodology for determining support amounts.

In its Second Recommended Decision responding to this referral, the Joint Board found that "it is within the Commission's jurisdiction to determine what … implicit support [there] is [in interstate access rates] and what action the Commission should take to make that support explicit."[126] The Joint Board proposed a series of principles to guide the Commission's determination – for example, that reductions in interstate access rates should inure to the benefit of all consumers – but ultimately referred back to the authority of the Commission to take the actions now contemplated by the revised CALLS plan.

As a practical matter, then, the universal service issues under consideration here have twice been before the Joint Board. Because the Joint Board has had full opportunity to address these issues, and because further delay in access charge reform will only defer consumer benefits and delay competition, CALLS believes that no additional referral, or extended informal consultation, is warranted at this time.[127]

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125 In the Matter of Federal-State Joint Board on Universal Service, *Order and Order on Reconsideration*, 13 FCC Rcd 13749, 13752 (1998).

126 In the Matter of Federal-State Joint Board on Universal Service, *Second Recommended Decision***,** 14 F.C.C. Rcd 24744**,** 24755, ¶ 23 (1998).

127 Although the Commission has discretion in making referrals, unlike the referrals contemplated by section 410(c), subsequent referrals under section 254(a)(1) are permissive but not mandatory. Section 410(c) establishes the Separations Joint Board and provides that "[t]he Commission *shall refer any proceeding* regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations . . .and . . .*may refer* any other matter . . . to a Federal-State Joint Board." 47 U.S.C. 410(c)(emphasis added). Section 254(a), establishing the Federal-State Joint Board on Universal Service also uses mandatory language, though it is only with regard to a single referral to the Joint Board (within one month of enactment) and

VIII. CONCLUSION

More than four years after enactment of the Telecommunications Act of 1996, the CALLS plan presents the Commission with a clear choice. The CALLS plan proposes a reasonable, balanced proposal to cut through the "Gordian knot" of universal service, access rate structure reform, and interstate access pricing reforms. The CALLS plan is consistent with the Commission's major policy objectives:

- The CALLS plan will preserve and enhance universal service, by finally getting on with the job of making implicit support explicit;
- The CALLS plan promotes the rapid introduction of competition in all telecommunications markets;
- The CALLS plan promotes facilities-based competition, investment, and innovation;
- The CALLS plan is Internet-friendly and will foster the development of broadband networks and digital services;
- The CALLS plan will reduce regulation by fostering competition;
- The CALLS plan will create certainty in the marketplace where currently there is none;
- The CALLS plan can be implemented immediately;
- The CALLS plan will benefit consumers both through immediate price reductions and long term growth of competition.

The CALLS plan presents the Commission with a stark choice. The Commission can either move forward and adopt CALLS' comprehensive, integrated plan, or it can remain mired in endless debate. The Commission can adopt a plan that will yield

Continued . . .

the Joint Board's recommendations back to the Commission (within nine months of enactment). Other sections contemplate the *possibility* of further recommendations from the Joint Board, but do not mandate them. 47 U.S.C. 254(a)(2) and (c)(2)("The Joint Board *may*, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms.")(emphasis added).

substantially lower consumer bills on July 1, 2000, secure universal service for rural and small town America, promote competition and choice in all telecommunications markets, be Internet and broadband friendly, or the Commission can hew to a status quo that the Commission itself has called unsustainable.

When the FCC counsels foreign regulators, it advises them that even though pro-competitive reforms have some unpopular elements, the benefit to the national economy from open, competitive telecommunications markets is overwhelming. This advice is no less true at home. Adopting the CALLS plan will increase competition, increase economic value, and promote continued innovation of e-services supported by state-of-the-art communications networks. But unlike many foreign situations, the CALLS plan also cuts consumer charges immediately. The CALLS plan gives the Commission the opportunity to heed its own advice, without having to swallow strong medicine. The Commission should adopt the CALLS plan, and promptly implement it by July 1, 2000.

Respectfully submitted,

By:__________________________________

John T. Nakahata
Evan R. Grayer
Karen L. Gulick

HARRIS, WILTSHIRE & GRANNIS LLP
1200 EIGHTEENTH STREET, N.W.
WASHINGTON, D.C. 20036
(202) 730-1300

Attorneys for the Coalition for Affordable Local and Long Distance Service (CALLS)

April 17, 2000

Mark C. Rosenblum
Judy Sello
AT&T CORP.
Room 1135L2
295 North Maple Avenue
Basking Ridge, New Jersey 07920
(908) 221-8984

Gene C. Schaerr
James P. Young
SIDLEY & AUSTIN
1722 Eye Street, N.W.
Washington, DC 20006
(202) 736-8000

COUNSEL FOR AT&T CORP.

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

Of counsel:
Michael E. Glover

COUNSEL FOR THE
BELL ATLANTIC TELEPHONE
COMPANIES

M. Robert Sutherland
Richard M. Sbaratta
BELLSOUTH
Suite 1700
1155 Peachtree Street, N. E.
Atlanta, Georgia 30309-3610
(404) 249-3386

Gary M. Epstein
Richard Cameron
LATHAM & WATKINS
1001 Pennsylvania Avenue, N.W.
Washington, D.C 20554
(202) 637-2200

COUNSEL FOR BELLSOUTH CORP.

Gregory J. Vogt
WILEY, REIN & FIELDING
1776 K Street, N.W.
Washington, D.C. 20006
(202) 719-3240

John F. Raposa
GTE Service Corporation
600 Hidden Ridge, HQE03J27
P.O. Box 152092
Irving, TX 75015-2092
(972) 718-6969

Gail L. Polivy
GTE Service Corporation
1850 M Street, N.W.
Washington, DC 20036
(202) 463-5214

COUNSEL FOR GTE SERVICE CORP.

Alfred G. Richter, Jr.
Roger K. Toppins
Michael J. Zpevak
Thomas A. Pajda
SBC Telecommunications, Inc.
One Bell Plaza, Room 3003
Dallas, Texas 75202
(214) 464-5307

COUNSEL FOR SBC COMMUNICATIONS, INC.

Jay C. Keithley
Leon M. Kestenbaum
Peter N. Sywenki
Richard Juhnke
SPRINT CORPORATION
1850 M St., N.W., 11th Floor
Washington, D.C. 20036
(202) 857-1030

COUNSEL FOR SPRINT CORP.