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

In the Matter of	)	
	)	
	)	CC Docket No. 80-286
Jurisdictional Separations Reform and	)	
Referral to the Federal-State Joint Board	)	

JOINT COMMENTS

The National Exchange Carrier Association, Inc. (NECA), National Telephone Cooperative Association (NTCA), National Rural Telecom Association (NRTA), and Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO) submit these Joint Comments in response to the Commission's *Public Notice*[1] of the recent *Recommended Decision*[2] of the Federal-State Joint Board on Jurisdictional Separations (Joint Board).

The Joint Board recommends that the Commission impose a five-year "freeze" of all Part 36 category relationships and allocation factors for price cap carriers, and a "freeze" of allocation factors for rate-of-return carriers,[3] for the same five-year

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[1] Comment Sought on Recommended Decision Issued By Federal-State Joint Board On Jurisdictional Separations, CC Docket No. 80-286, *Public Notice*, DA 00-1865 (rel. Aug. 15, 2000) (*Public Notice*).

[2] Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, CC Docket No. 80-286, *Recommended Decision*, Federal-State Joint Board on Jurisdictional Separations Reform, FCC 00J-2 (rel. July 21, 2000) (*Recommended Decision*).

[3] The Joint Board explains that "'(f)reezing' category relationships means that the same category distribution percentages for each account in the base year of the freeze would apply to future account balances (*e.g.*, Account 2210). 'Freezing' jurisdictional allocation factors means that the same jurisdictional cost allocation percentages used in the base

period.[4] The Associations strongly support the Joint Board's view that "interim action is necessary to provide simplicity and stability to the separations process."[5] The Joint Board catalogs a host of sound reasons for implementing the freeze: predictability of separations results as new services and technologies are deployed in the marketplace; reduction of regulatory burdens during the transition from regulated monopoly to a competitive local telecommunications market; regulatory parity between incumbent local exchange carriers (ILECs) and competitive local exchange carriers (CLECs), which are not required under Commission rules to perform jurisdictional cost separations studies; and competitive neutrality during the transition to a competitive local marketplace.[6]

The Associations generally support the Joint Board's recommendations,[7] and <u>urge the Commission to adopt the interim freeze immediately</u>, taking into consideration the

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year of the freeze would be used for future jurisdictional cost allocations." *Recommended Decision*, para. 17.

[4] *Id.*, para. 2. The Joint Board-recommended freeze would be calculated using carriers' data from the twelve months prior to release of a Commission order on the *Recommended Decision*. The freeze would be mandatory for all carriers subject to the Commission's Part 36 rules, and would remain in effect for five years, or until the Commission takes additional action in response to a Joint Board recommendation, whichever occurs first. Further, the Joint Board recommends that, if the Commission finds that Internet traffic is jurisdictionally interstate in its current proceeding opened in response to the remand of the United States Court of Appeals for the D.C. Circuit on the Commission's *Reciprocal Compensation Ruling* (cite omitted), the Commission freeze the local dial equipment minutes (DEM) factor for the duration of the freeze at some substantial portion of the current year level, based on data from the same twelve month period referenced above.

[5] *Id*, para. 10.

[6] *Id.*, paras. 17-19.

[7] The Associations and other parties consistently have maintained that the Commission should immediately implement a freeze of separations factors, in particular because of the

suggestions presented herein. The Associations' comments address (1) freezing category relationships versus allocation factors, for rate-of-return carriers; (2) which twelve-month period to use in calculating the freeze of allocation factors; (3) removal of Internet-related usage from DEM; (4) development of allocation factors in cases where previously none were used by a carrier, including treatment of average schedule carriers converting to cost-based settlements; and, (5) treatment of carriers involved in mergers and acquisitions.

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effects of explosive growth in Internet traffic. Internet traffic has effectively rendered useless traditional jurisdictional allocation factors, now resulting in serious jurisdictional cost recovery distortions. *See*, for example, National Exchange Carrier Association *Petition for Interim Waiver of Section 36.2(a)(3) of the Commission's Rules* (May 8, 1998); and Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, *Comments*, NECA, NRTA, NTCA, and OPASTCO (filed jointly), CC Docket No. 80-286 (Mar. 30, 1999); and Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, *Comments of SBC Communications*, CC Docket No. 80-286 (Mar. 30, 1999); and *Comments of the United States Telephone Association*, CC Docket No. 80-286 (Mar. 30, 1999); and *Reply*, NECA, NRTA, NTCA, and OPASTCO (filed jointly), CC Docket No. 80-286 (Apr. 14, 1999); and *Reply Comments of SBC Communications*, CC Docket No. 80-286 (Apr. 14, 1999); and *Reply Comments of United States Telephone Association*, CC Docket No. 80-286 (Apr. 14, 1999); and Jurisdictional Separations Treatment of Internet Traffic, *Joint Reply to Opposition*, NECA, NRTA, NTCA, and OPASTCO (July 12, 1999); and Jurisdictional Separations Reform and Referral to the Federal-State Joint Board, *Letter to Magalie Roman Salas, Federal Communications Commission, from Richard A. Askoff, NECA*, Request for En Banc Meeting of the Full Separations Joint Board, CC Docket No. 80-286 (July 13, 1999); and Jurisdictional Separations Treatment of Internet Traffic, *Reply Comments of SBC Communications*, ASD 99-30, DA 99-912 (July 15, 1999); and *Letter to Lawrence E. Strickling, Federal Communications Commission from Richard A. Askoff, NECA* (Oct. 5, 1999) "Pending ultimate resolution of the difficult rate and cost recovery issues surrounding Internet traffic, it is essential that the proposed en banc meeting be convened quickly and an interim separations freeze, based on a representative historical period, be put into effect immediately."

I. A FREEZE OF ALLOCATION FACTORS AND A ONE-TIME OPTIONAL CATEGORY FREEZE ARE APPROPRIATE FOR RATE-OF-RETURN CARRIERS

The Associations strongly agree with the Joint Board that a freeze of jurisdictional allocation factors is appropriate for companies under rate-of-return regulation, but suggest that rate-of-return carriers should have the option to freeze categories on a one-time basis, as more fully described below. As the Joint Board recognized, "not freezing the category relationships for rate-of-return carriers . . . whose investment patterns may fluctuate more than those of price cap carriers from year to year, will retain maximum flexibility for recovering costs from . . . new plant investments (upgrades)."[8] A mandatory categories freeze may actually influence small carriers to forestall improvements in their networks, if they are limited in their ability to account for such improvements via separations. Similarly, as the Joint Board noted, companies risk the loss of universal service high cost support if category relationships are frozen.[9] Therefore, the Associations concur in the Joint Board conclusion that, "(w)hile a freeze of category relationships would further the goal of simplifying the separations process . . . the potential harm to rate-of-return carriers caused by such a freeze necessitates a factors-

[8] *Recommended Decision*, para. 21, citing *ex parte* communication of NECA on February 17, 2000 and of USTA on February 11, 2000.

[9] NECA and USTA each have also informed the Commission and Joint Board that a categories freeze may negatively affect some carriers' universal service high cost support. The Joint Board accordingly noted the potential inability of rate-of-return carriers to properly recover increased COE Category 4.13 and C&WF Category 1.3 investments because such increases would not be recovered through increased loop support under the Universal Service High Cost Loop formula, if these categories are frozen. *Id.*, para. 22.

only freeze for these carriers and outweighs the added simplification benefits of a categories freeze."[10]

Nevertheless, the Joint Board also notes that "when special circumstances warrant such action, rate-of-return carriers or the state commissions may seek Commission authority to freeze the category relationships."[11] The Associations recommend that the Commission allow rate-of-return carriers to elect, on a per-study area basis, a one-time option to freeze category relationships (in addition to allocation factors) at the initial effective date of the freeze. Any subsequent elections to freeze categories would require a waiver of Commission rules.

II. IF THE COMMISSION ADOPTS A TWELVE-MONTH DATA PERIOD, IT SHOULD USE DATA FROM CARRIERS' MOST RECENT ANNUAL COST STUDY AT TIME OF IMPLEMENTATION

The Joint Board observes that the record in this proceeding includes proposals by USTA and NECA that "a freeze would be calculated based on data from an average of prior years, 1995-1997."[12] The Associations here reiterate and continue to support those proposals as representing the best data to use for a separations factor freeze for rate-of-return carriers. However, if the Commission adopts the Joint Board recommendation to use carriers' data from the most recent twelve months, the Associations recommend using data from carriers' most recent annual cost study at the time of implementation of a

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[10] *Id.*, para. 24.

[11] *Id.*, note 55.

[12] *Id.*, note 69 (cite omitted).

Commission order. Such studies would be developed using data from not earlier than 1999 and not later than 2000. These factors would then be applied to subsequent studies for the duration of the freeze, *e.g.*, frozen factors developed from the 1999 cost study would be used for calendar year 2000 studies.[13]

III. THE ASSOCIATIONS RECOMMEND AN IMMEDIATE SEPARATIONS FREEZE, INCLUDING A LOCAL DEM ADJUSTMENT

With respect to DEM, "(t)he Joint Board recognizes that there have been increased intrastate usage patterns since 1995, as evidenced by the increase in local minutes."[14] Because of its continuing uncertainty about all of the reasons for these usage changes, however, the Joint Board recommends that the Commission "further develop the record . . . to determine what, if any, impact the growth in local minutes has had on jurisdictional allocations and consumers."[15] Noting the current Commission remand proceeding on *Reciprocal Compensation,*[16] the Joint Board

> recommends that, if the Commission finds that Internet traffic is interstate, the Commission freeze the local DEM factor for the duration of the freeze at some substantial portion of the current year level . . . . The precise percentage of the current year's local DEM should be established according to how much of a reduction in local DEM is warranted in light of any effects that Internet usage

[13] The Joint Board proposed that "carriers would no longer have to measure usage in order to develop jurisdictional allocation factors for interstate purposes, as frozen factors will be carried forward from year to year and used by carriers to calculate their separations results." *Id.*, para. 19.

[14] *Id.*, para. 28 (note omitted).

[15] *Id.*

[16] *Id.*, para. 29.

> has had on jurisdictional allocations . . . . Given the inadequate record on this issue, we cannot recommend with precision what portion of the current year level is appropriate for the freeze. . . . however, we would suggest, as a default estimate, freezing the local DEM at 95% of the current year level . . . .[17]

The Associations recommend implementation of the separations freeze, including a DEM adjustment, *immediately,* regardless of the pending Internet jurisdiction issue. There is no dispute that Internet traffic exhibits extraordinary operating characteristics, *e.g.*, exceptionally long holding times. While there may be some other factors that are influencing the increase in local usage presently being experienced, the Joint Board has recommended an estimated 5% reduction in local DEM to remove the anomalous Internet traffic conditions.[18] Thus, the Associations urge the Commission to immediately implement the separations freeze, and adopt the Joint Board recommendation for an adjustment to the local DEM factor, to be applied at the start of the interim freeze.

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[17] *Id.* (note omitted)

[18] A 1999 NECA study of 1998 carrier traffic data revealed Internet usage of approximately 18 percent. *Letter* from Gina Harrison, NECA to Dorothy Attwood, Federal Communications Commission, CC Docket No. 80-286 (Oct. 28, 1999). If the Commission determines, on the basis of additional data provided in this proceeding, that Internet traffic represents a greater percentage of local traffic than the 5% reduction to local DEM recommended by the Joint Board, carriers should be permitted to adjust DEM for that greater percentage amount.

IV. COMMISSION RULES MUST PROVIDE FOR DEVELOPMENT OF FACTORS IN CASES WHERE NONE PREVIOUSLY EXISTED

There will be instances where the development of allocation factors by rate-of-return carriers will be necessary, because previously none were used by the carriers. As the Joint Board recognized, and as discussed *supra,* a freeze of category relationships for rate-of-return carriers could limit their ability to recover costs from new plant investments through the separations process. However, in circumstances where a rate-of-return carrier adds new categories of investment where none previously existed, the *Recommended Decision* does not include provisions to calculate new separations factors. Also, companies that convert from average schedule to cost-based settlements after the initial freeze period would not have factors from the base year for use in their separations studies.[19] In these cases, the Associations recommend that the Commission permit rate-of-return carriers to calculate separations factors for new categories of investment using current period data. These new factors would then be frozen and used for subsequent cost studies. Absent this provision, rate-of-return carriers would be precluded from properly allocating costs for recovery in the proper jurisdiction.

[19] Average schedule companies do not perform jurisdictional cost separations studies, and, therefore, do not develop cost allocation factors. These companies report key demand units to NECA that are used in formulas that simulate cost company results for purposes of determining interstate access settlements.

V. IN TRANSACTIONS INVOLVING TRANSFER OF EXCHANGES, COMMISION RULES MUST PROVIDE FOR USE OF THE SELLER'S FACTORS, OR A ONE-TIME DEVELOPMENT OF FACTORS BY THE ACQUIRING COMPANY

The Joint Board recognizes that, "during the freeze, carriers may merge affiliated operations, or acquire from or sell exchanges to non-affiliated carriers."[20] As a method of consistent development and application of separations factors in these circumstances, the Joint Board recommends

> that a carrier selling or otherwise transferring exchanges to another carrier's study area continue to employ its pre-transfer frozen factors and, if applicable, category relationships. We recommend, however, that the acquiring carrier be required to recalculate its frozen factors and category relationships. The acquiring carrier should calculate new, composite frozen factors and category relationships based on a weighted average of both the seller's and purchaser's existing frozen factors and frozen category relationships. This weighted average would be based on the number of access lines in the transferred exchanges.[21]

While the line-weighted ratio advocated by the Joint Board will achieve the desired composite result when an acquiring company had the particular category of investment prior to acquisition of "new" exchanges, this methodology will not work if the acquiring company did not have such category of investment. The Associations therefore recommend that, in these circumstances, the Commission permit use of either the selling (transferring) company's factor, without pro-rating; or, in the alternative, a

[20] *Recommended Decision*, para. 33.

one-time calculation of a factor for the acquired exchanges, similar to the methodology used when no factor previously exists (see discussion, above).

VI. CONCLUSION

The Commission should take immediate action to implement an interim separations freeze, including an adjustment to local DEM. Immediate action is necessary because of the anomalous treatment of new services and technology under the Commission's existing separations rules. Those rules are outdated, as they were never intended to account for the present explosive growth in network usage occasioned by Internet traffic. Thus, until the Commission undertakes comprehensive separations reform, it must adopt the Joint Board's recommendation, and implement an interim freeze *now*.

The Associations applaud the Joint Board's recommendations for a freeze of allocation factors for rate-of-return carriers, and encourage the Commission to provide for a one-time category freeze as an option for these carriers. If the Commission adopts a twelve-month period for base data, it should use data from carriers' most recent annual cost studies at time of implementation. The Joint Board recommendation for a reduction in local DEM should be implemented at the start of the interim freeze. Commission rules must provide for development of factors in cases where previously none existed, including transactions involving transfer of exchanges and average schedule to cost conversions. The per-line ratio advocated by the Joint Board will not achieve its desired

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[21] *Id.*

result (a composite factor) if the acquiring carrier did not have the specific category of investment before the transaction.

As the Associations and others have consistently maintained, serious distortions of jurisdictional cost allocations are occurring *now*, and carriers experiencing extraordinary growth in network usage are being denied legitimate means of cost recovery. The interim freeze must be implemented immediately, taking into account the suggestions presented herein by the Associations.

Respectfully submitted,

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September 25, 2000

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I hereby certify that copy of the Joint Comments was served this 25th day of September 2000, by electronic delivery, hand delivery or first class mail, to the persons listed below.

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