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ATTORNEYS AT LAW

May 3, 2001

EX PARTE – Via Electronic Filing

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
The Portals
445 12th Street, S.W.
Washington, DC 20554

Re: CC Docket 96-45 (Rural Task Force Recommendation), and
CC Docket Nos. 00-256, 96-45, 98-77, and 98-166 (Multi-Association
Group Plan for Regulation of Interstate Service of Non-Price Cap Incumbent
Local Exchange Carriers and Interexchange Carriers)

Dear Ms. Salas:

Attached for the record in the above-captioned dockets is a copy of a letter sent yesterday to Dorothy Attwood, Chief, Common Carrier Bureau, responding to the letter from the NRTA, NTCA, OPASTCO, and USTA ("MAG") dated April 24, 2001.

In addition, on Tuesday, May 1, 2001, I spoke with Mr. Kyle Dixon, Legal Advisor to Chairman Powell. On Wednesday, May 2, 2001, I spoke with Mr. Jordan Goldstein, Legal Advisor to Commissioner Ness, Mr. Samuel Feder, Legal Advisor to Commissioner Furchtgott-Roth, Mr. Jack Zinman, Counsel to the Bureau Chief, and Mr. Eric Einhorn, Acting Deputy Chief, Accounting Policy Division, Common Carrier Bureau. The points contained in each of these presentations are summarized in the attached letter to Ms. Attwood and the ex parte filed Friday, April 27, 2001.

In addition, I made the point that the Commission cannot claim, to Congress or to anyone else, to have addressed reform of universal service until it has taken steps to replace implicit support in interstate access charges with explicit universal service support.

Ms. Magalie Roman Salas
May 3, 2001
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In accordance with the Commission's rules, a copy of this letter and the attachment are being filed electronically in the above-captioned docket.

Sincerely,



John T. Nakahata

JTN/krs

Attachments

c: Mr. Kyle Dixon
Mr. Jordan Goldstein
Mr. Samuel Feder
Mr. Jack Zinman
Mr. Eric Einhorn
Ms. Carol Matthey
Ms. Jane Jackson
Ms. Katherine Schroeder
Mr. Richard Lerner

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May 2, 2001

ATTORNEYS AT LAW

VIA HAND DELIVERY

Ms. Dorothy Attwood
Chief, Common Carrier Bureau
Federal Communications Commission
445 12th Street, S.W.
Room 5-C450
Washington, DC 20554

Re: CC Docket 96-45 (Rural Task Force Recommendation), and
CC Docket Nos. 00-256, 96-45, 98-77, and 98-166 (Multi-Association
Group Plan for Regulation of Interstate Service of Non-Price Cap Incumbent
Local Exchange Carriers and Interexchange Carriers)

Dear Ms. Attwood:

We are writing in response to the letter you received from the NRTA, NTCA, OPASTCO, and USTA ("MAG") dated April 24, 2001. That letter opposed an interim compromise proposal by AT&T, GCI, Sprint and Western Wireless to implement at least some form of explicit universal service support to replace support implicit in interstate access charges, to return SLC caps to the same levels as those applied to price cap LECs, and to recover the universal service contributions by the non-price cap carriers directly from their end user customers rather than transferring the recovery of those contributions to consumers all across the country -- most of whom are already paying their own local telephone company for its own universal service contributions. We will address each aspect of our proposal and respond to the MAG sponsors' objections. We will also suggest an alternative method for implementing High Cost Fund III immediately, although this alternative is far less preferred and does not achieve all the pro-competitive benefits of our principal proposal.

First, we proposed to increase the SLC caps for non-price cap carriers to the same levels as the caps for price cap carriers under the *CALLS Order*. MAG never explains why this reform is not separable from the other access changes it proposes. The Commission has already held in the *CALLS Order* that rates will be affordable and reasonably comparable -- and rejected arguments to the contrary by NRTA and NTCA among others -- even though it clearly recognized that there would be some end users who were charged SLCs at caps, while other end users were charged substantially less than the caps. Moreover, in attempting to justify failure to increase SLC caps, MAG parrots and cites comments by NASUCA that long distance carriers must be charged a portion of loop costs. The

Commission has repeatedly rejected this argument, including in both the 1997 *Access Charge Reform Order*¹ and the *CALLS Order*², finding that the end user is the cost causer and that therefore it is appropriate that end users in the first instance pay for the costs of the loop. The Commission's decisions in this regard have been upheld by the courts. See *Southwestern Bell Telephone Co. v. FCC*, 153 F.3d 523 (8th Cir. 1998); *NARUC v. FCC.*, 737 F.2d 1095 (D.C. Cir. 1984). MAG appears to suggest that SLCs should be capped at the rates actually charged by price cap LECs. Such a cap would itself be unworkable, as it would be difficult to determine the applicable price cap LEC rate to use as a cap, and ignores the fact that price cap LECs themselves will be geographically deaveraging SLCs as part of the *CALLS Order*. MAG raises no argument that should preclude immediate reform of SLC caps.

Second, we proposed that non-price cap LECs be required to recover their universal service contributions directly from their end users, rather than from CCL charges assessed on interexchange carriers. This is a reform that directly parallels actions taken by the Commission in the *CALLS Order*. MAG cites no reason why this reform should not be taken immediately, and no reason why it cannot be undertaken separately from the remainder of the access changes MAG seeks. To the extent implementation of a new line item were a concern, the amount could be billed together with the SLC, as was permitted for price cap carriers and as in fact has occurred for some price cap carriers.

Moreover, MAG conveniently ignores the real impact of placing recovery of these universal service contributions in CCL charges. For rural and non-rural end users served by price cap LECs, they are already paying their own LEC directly for that LEC's universal service contributions. For rural and non-rural end users of non-price cap LECs, however, the universal service contributions paid by their price cap LEC are charged to long distance companies, who must then -- because of the rate averaging requirements of Section 254(g) -- spread recovery of those contributions across the rates charged to all customers. Only a small portion of that non-price cap LEC's universal service contributions end up being recovered from that LEC's end users. On the other hand, rural and non-rural end users served by price cap LECs pay twice -- once for the contributions of their own LEC and an additional amount for the contributions by non-price cap LECs. There is nothing in law or good policy that mandates such an inequitable result. In addition, because the non-price cap LECs' universal service contributions inflate the CCL, recovering these charges through carrier-paid access charges exacerbates the competitive inequities in the long distance market created by Section 254(g), and serves as an additional disincentive to new long distance entrants expanding service into rural areas served by the non-price cap LECs. In the face of these strong policy considerations, MAG's attempt to hold this reasonable reform hostage to the unrelated access changes it seeks should simply be disregarded.

¹ First Report and Order, *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Transport Rate Structure and Pricing; End User Common Line Charges*, 12 FCC Rcd 15982 (1997).

² Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Low-Volume Long-Distance Users, Federal-State Joint Board on Universal Service*, 15 FCC Rcd 12962 (2000), Appeal Pending Sub. Nom., *Texas Office of Public Utility Counsel v. FCC*, No. 00-60434, U.S. Court of Appeals, Fifth Circuit.

Third, we proposed that High Cost Fund III be implemented immediately for all non-price cap LECs with a target traffic sensitive (i.e. not including CCL) switched access price of 1.6 cents per minute. We expressly proposed that this be a revenue neutral shift of revenue recovery from access into universal service, with the difference between the projected revenues under tariffs calculated pursuant to existing rules and projected access revenues that would be collected at a traffic sensitive switched access rate of 1.6 cents per minute being paid by competitively neutral, per line universal service support. Such a proposal would be consistent with RTF principles for High Cost Fund III.

MAG argues that this proposal would foreclose retaining rate-of-return regulation for non-price cap LECs. This is simply wrong. Our proposal has nothing to do with whether the Commission continues rate-of-return regulation or creates an incentive regulation system as a means of determining aggregate total revenue levels for non-price cap LECs. Selection of the target access price does not affect total revenue in the absence of loss of subscribers to competition. Our proposal instead focuses only on the structure of switched traffic sensitive access revenue between rates charged to long distance carriers and the universal service fund. The Commission can adopt our proposal and choose to adopt, not adopt, or modify their incentive regulation plan.

Our proposal does reject the notion that companies should be able to "opt out" of High Cost Fund III, which MAG would permit. MAG itself, through its proposal for rate averaging support, recognizes that support for traffic sensitive access is a legitimate component of universal service. Indeed, it is impossible to see how 254(g) toll averaging can be sustained unless there is some form of support for traffic sensitive access costs that are very high compared to the rest of the country. High Cost Fund III is, therefore, a necessary step to reconcile 254(g) with the rest of section 254, and consistent with the Commission's universal service principles, it should be competitively neutral and non-discriminatory. These policy concerns, however, apply equally regardless of whether a particular LEC elects incentive regulation or remains under rate-of-return regulation.

In addition, we would agree that implementation of our proposed interim High Cost Fund III probably makes it less likely that the Commission would select a Target Access Price for some rate-of-return carriers that would be higher than 1.6 cents per minute, although the Commission would clearly have the legal ability to do so. We believe selection of a higher price would simply reduce the sustainability of geographic rate averaging of long distance, and the incentives for new entrants in long distance to enter and serve these rural markets. In addition, a target access price of greater than 1.6 cents increases the magnitude of the access disparity the Commission would have to address in developing a comprehensive intercarrier compensation regime.

Moreover, MAG appears to believe that creating some form of rate averaging support or High Cost Fund III that would work in conjunction with today's access charge mechanisms for non-price cap carriers necessarily precludes changing that mechanism to be aligned with whatever mechanisms the Commission creates in the future. MAG is wrong. In fact, one would expect that the Commission would ensure that all its mechanisms work together at the time the Commission adopts new access charge mechanisms.

We also dispute MAG's contention that our proposed interim High Cost Fund III creates perverse entry incentives. Indeed, it is today's entry incentives that are perverse. Today, access revenue can be concentrated with a small handful of customers. If an entrant wins one of these customers -- and an entrant need not be an ETC to do so -- it will receive all of the large customer's access revenue. Under our proposal, because the High Cost Fund III would be distributed on a per line basis and only to ETCs, entrants would have an incentive to enter rural markets broadly and to seek ETC designation. It is ironic to see MAG fighting to preserve opportunities for "cream-skimming" by non-ETCs. Moreover, MAG's attempt to suggest that wireless carriers should not receive access universal service support when they *provide* competing interstate access service is directly contrary to the Commission's long established principle of competitive neutrality in universal service.

MAG does not even claim that our proposal could not be implemented. MAG knows it has the information necessary to implement the proposal, and that if the Commission requested that information it could be provided.

We recognize, however, that the Bureau has had concerns about implementation of our proposal for interim High Cost Fund III. Although we believe our initial proposal is far preferable, we therefore suggest a second alternative for the third step of our proposal. In lieu of establishing a target access price of 1.6 cents per minute, the Commission could direct that all projected CCL revenues be recovered from High Cost Fund III and be paid out as per line support. This alternative is far less satisfactory because it does not tackle the rate averaging issues for traffic sensitive access directly. Although this support would decline as SLC caps increased in the future, it would provide support for interstate allocated loop costs not recoverable from SLCs. The Commission could then address support for switched traffic sensitive access at a later date. We attach a draft proposed rule to implement this alternative HCF III proposal.

We continue to believe that, except as described above, these reforms can be undertaken without prejudice to any of the more complex and controversial proposals contained in the MAG plan. MAG has presented no substantial arguments as to why these proposals are not severable from MAG, and cannot or should not be undertaken now.

Finally, we address MAG's arguments for mandatory "pass-through" regulation of IXCs. The record clearly establishes that there is no basis in law or fact for this proposal. First, by reducing disincentives to enter areas served by non-price cap LECs because of the present disparity between price cap and non-price cap access rates, our proposal would encourage further competition in the provision of long distance service in areas served by non-price cap LECs. Moreover, the record on long distance prices since the adoption of the CALLS proposal is clear -- prices have declined substantially. According to the Commission's own report, the interstate long distance CPI dropped by over 7.6% between May 2000 and November 2000.³ The Commission's empirical data demonstrates that a "pass-through" requirement is unnecessary.

³ Statistics of the Long Distance Telecommunications Industry, Table 26, Industry Analysis Div., Common Carrier Bureau (Jan. 2001).

Ms. Dorothy Attwood
May 2, 2001
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We urge the Commission not to miss this opportunity to act. Universal service reform issues are never easy. But they can be better done when taken promptly and in a measured manner.

Sincerely,

A handwritten signature in black ink, appearing to read "John T. Nakahata", written in a cursive style.

John T. Nakahata

Counsel for AT&T, GCI, Sprint and Western Wireless

PROPOSED RULE IMPLEMENTING HCF III – ALTERNATIVE 2

§54.304(c) Interstate Access Universal Service Support for Areas Served by Non-Price Cap LECs – In any study area served by a non-price cap local exchange carrier, each Eligible Telecommunications Carrier (ETC) that provides supported service may receive Interstate Access Universal Service Support for Areas served by Non-Price Cap LECs (IAUSS-NPC) for each line it serves within that study area.

- (1) For each study area served by a Non-Price Cap LEC, the amount of IAUSS-NPC is calculated by taking the difference between the total projected carrier common line revenue requirement during the applicable tariff year, less universal service contributions to be paid pursuant to §54.706 during the applicable tariff year, and then dividing that difference by the number of total projected lines to be served by the incumbent LEC within that study area during the applicable tariff year.
- (2) The Administrator shall complete the determination of IAUSS-NPC for each study area and publish at least annually a schedule of IAUSS-NPC by study area prior to the start of the applicable tariff year on a date determined by the Chief of the Common Carrier Bureau. Notwithstanding the foregoing, for the tariff year beginning July 1, 2001, the Administrator shall complete its determination and publish its schedule of IAUSS-NPC by study area as soon as is practicable.
- (3) The Commission delegates authority to the Chief of the Common Carrier Bureau to collect such information as is necessary to implement this subsection, and to determine the timetable for such collections.
- (4) Definitions – For the purposes of this subsection,
 - (1) “non-price cap LEC” is an incumbent LEC other than a price cap LEC, as that term is defined in § 54.800(i);
 - (2) “applicable tariff year” is the tariff year during which service will be provided.
 - (3) “total projected carrier common line revenue requirement” is the amount of the carrier common line element revenue requirement as defined in §§69.501 and 69.502 for the applicable tariff year.

§69.105 [removed and reserved]