HARRIS,
WILTSHIRE &
GRANNIS LLP

1200 EIGHTEENTH STREET, NW
WASHINGTON, DC 20036

TEL 202.730.1300 FAX 202.730.1301
WWW.HARRISWILTSHIRE.COM

ATTORNEYS AT LAW

August 28, 2001

Ms. Jane E. Jackson
Chief, Competitive Pricing Division
Common Carrier Bureau
Federal Communication Commission
445 12th Street, SW
Washington, DC 20554

Ms. Katherine Schroeder
Chief, Accounting Policy Division
Common Carrier Bureau
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: CC Docket Nos. 96-45, 98-77, 98-166 and 00-256

Dear Ms. Jackson and Ms. Schroeder:

On behalf of AT&T, GCI and Western Wireless, I am writing to respond to several points raised by representatives of the Multi-Association Group (MAG) in ex partes dated August 9, 2001, and August 20, 2001[1] and by representatives of several incumbent LECs in an ex parte dated August 7, 2001.[2]

First, although MAG states that it is reviewing its plan in light of the decision of the United States Court of Appeals for the Fifth Circuit in *COMSAT Corp. v. FCC*, 250 F.3d 931 (5th Cir. 2001) ("*COMSAT*"),[3] that decision clearly precludes the Commission from adopting MAG's Track B proposal.

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1 "The MAG Plan and Access Reform", filed as an attachment to a Letter from William F. Maher, Jr., Halprin, Temple, Goodman & Maher, to Magalie Roman Salas, Secretary, FCC, CC Docket Nos. 96-45, 98-77, 98-166 & 00-256 (Aug. 9, 2001) ("MAG CCB ex parte"); "MAG Plan Overview", filed as an attachment to a Letter from William F. Maher, Jr., Halprin, Temple, Goodman & Maher, to Magalie Roman Salas, Secretary, FCC, CC Docket Nos. 96-45, 98-77, 98-166 & 00-256 (Aug. 9, 2001) ("MAG Overview ex parte"); "The MAG Plan Has Major Public Policy and Consumer Benefits," filed as an attachment to a Letter from William F. Maher, Jr, Halprin, Temple, Goodman & Maher, to Magalie Roman Salas, Secretary, FCC, CC Docket Nos. 96-45, 98-77, 98-166 & 00-256 (Aug. 20, 2001) ("MAG Aug. 20 ex parte").

2 Letter from Lisa Zaina, Wallman Strategic Consulting, LLC, to Magalie Roman Salas, Secretary, FCC, CC Docket Nos. 96-45 & 00-256 (filed Aug. 7, 2001) ("Wallman ex parte").

3 MAG Overview ex parte at 1.

Under its Track B proposal, MAG asks the Commission to allow ILECs to elect to remain under rate-of-return regulation, subject only to increased SLC caps. MAG Track B does nothing further to attempt to identify remaining implicit support in interstate access charges and to either eliminate that support or to convert it into explicit universal service support. MAG does not argue that implicit support would not continue to exist. It simply proposes to maintain indefinitely the remaining implicit support flows for Track B companies.

In *COMSAT*, however, the Fifth Circuit reiterated that the "'FCC cannot maintain any implicit subsidies' whether on a permissive or mandatory basis." *COMSAT* at 939 (*citing Texas Office of Pub. Util. Counsel v. FCC*, 183 F.3d 393, 425 (5th Cir. 1999)). By failing to identify and make explicit the universal service support implicit in access charges by Track B companies, MAG Track B would directly contravene the Fifth Circuit's holding. Universal service reform cannot be optional.

Second, with respect to multiline business SLCs, MAG asserts (without support) that raising those caps to $9.20, the same level as for the price cap LECs, including the smaller rural price cap carriers, would result in "rate shock."[4] There is no evidence to support this claim. In 1998, the multiline business SLC cap moved from $6.00 to $9.00 for the price cap LECs, including for rural areas in which the SLCs themselves actually moved from $6.00 to $9.00.[5] That shift did not cause major consumer dislocations. In any event, the proposal merely equalizes SLC caps between the highest cost price-cap rural areas and the highest cost non-price cap rural areas.

Third, MAG asserts that "the Commission should not view all common line costs in excess of those recovered by SLCs as implicit support to be excised from access charges."[6] MAG's logic is incorrect and contrary to the Commission's previous findings. SLCs are capped so that only a portion of common line costs are recovered from end users, with the remainder recovered through carrier common line charges ("CCLs") even though common line costs are not an incremental cost of access. MAG acknowledges as much when it states, "Compared to price cap LECs, many non-price cap LECs have high common line costs that may not be recovered through SLCs."[7] Although some MAG members may still cling to the position that traffic sensitive recovery of non-traffic sensitive loop costs is appropriate, the Commission, in its *1997 Access Reform Order*, expressly found otherwise:

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[4] MAG CCB ex parte at 1.

[5] Inflation adjustments increased this cap to $9.20, where it was subsequently frozen. *See Access Charge Reform*, 12 FCC Rcd. 15982 (1997) ("*1997 Access Reform Order*") (increasing multiline business SLC cap to $9.00, with an annual increase for inflation), *aff'd sub nom., Southwestern Bell v. FCC*, 153 F.3d 523 (8th Cir. 1998); *Access Charge Reform*, 15 FCC Rcd. 12962 (2000) ("*CALLS Order*") (amending 47 C.F.R. § 69.152 to cap the multiline business SLC cap at $9.20), *pets. for rev. pending sub. nom., Texas Office of Pub. Util. Counsel, et al. v. FCC,* 5th Cir. No. 00-60434 (and consolidated cases) (filed June 26, 2000).

[6] MAG CCB ex parte at 2.

[7] *Id.*

> "costs of interstate access should be recovered in the same way that they are incurred, consistent with principles of cost-causation. Thus, the cost of traffic-sensitive access services should be recovered through corresponding per-minute access rates. Similarly, NTS cost should be recovered through fixed, flat-rated fees."[8]

The Commission in that same order found the CCL charge to be an implicit subsidy, stating:

> "[b]ecause NTS [non traffic sensitive] costs, by definition, do not vary with usage, the recovery of NTS costs on a usage basis pursuant to our current access charge rules amounts to an implicit subsidy from high-volume users of interstate toll services to low-volume users of interstate long-distance services";[9] and

> "the current per-minute CCL charge that recovers loop costs represents an economically inefficient cost-recovery mechanism and implicit subsidy."[10]

MAG cannot now wish away the fact that the CCL charge is "the manipulation of rates for some customers to subsidize for affordable rates for others,"[11] and therefore constitutes an implicit subsidy that cannot be maintained under *COMSAT*.

Fourth, MAG objects to the creation of a "High Cost Fund III – Local Switching" ("HCF III – Local Switching") stating there is no economic basis for limiting local switching charges to $.0025 per minute.[12] Such a subsidy is necessary because, as MAG points out in the same paragraph, "the local switching costs of many non-price cap LECs do not reflect such [scale] economies" as compared with the price cap LECs.[13] These high local switching costs contribute significantly to high overall access charges in the non-price cap areas, which discourages carriers from serving rural areas because of the requirement of toll averaging. Even after line ports are reallocated to common line as we have proposed, NECA switching rates would still range from a low of $.005/ minute to a high of $.017/minute.[14] The size of this range makes the nationwide policy of geographic toll averaging unsustainable. In addition, in order to bring the overall average traffic sensitive (switching and transport) access charge into the same range as for price cap LECs, the local switching must be subsidized to a lower rate in order to offset the fact that transport costs for non-price cap LECs are, on

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8 *1997 Access Reform Order* at ¶ 24.

9 *Id.* at ¶ 6.

10 *Id.* at ¶ 69.

11 *Texas Office of Pub. Util. Counsel*, 183 F.3d at 406.

12 MAG CCB ex parte at 2.

13 *Id.*

14 Under current tariffs, NECA's local switching rates range from $.007238 in Band 1 to $0.024128 in Band 8. The RCC Plan proposes that the Commission create a default proxy of 30% for the line port reallocation. 30% was the proportion of end office switching costs assigned to line ports in the Commission's Hybrid Cost Proxy Model.

average, higher than for price cap LECs. Contrary to MAG's assertions, HCF III – Local Switching is not "arbitrary and burdensome,"[15] but is a logical, well-targeted means of implementing the Rural Task Force recommendations with respect to High Cost Fund III.

In its recommendations, the Rural Task Force stated "High Cost Fund III is needed, in part, to respond to a disparity of access rates between Rural Carriers and non-Rural Carriers."[16] The Rural Task Force further explained, "These disparities [between the access rates charged by price-cap (primarily non-Rural) and rate-of-return (primarily Rural) local exchange companies] can cause significant pressures on interexchange carriers to geographically deaverage toll rates."[17] In the RCC Plan, HCF III – Local Switching is expressly targeted to alleviate what the Rural Task Force described as "the conflict between these pressures and the requirements of Section 254(g) to maintain geographically averaged toll rates."[18] HCF III – Local Switching in the RCC Plan therefore implements the recommendations of the Rural Task Force by reducing interstate access charges to support the nationwide policy of rate averaging in a sustainable manner - the same objective served by the Rate Averaging Support (RAS) MAG proposed for companies electing Track A.

It is therefore surprising that MAG now criticizes the RCC Plan for "creat[ing] forms of 'universal service' support that serve only to subsidize lower rates for IXCs but do not benefit consumers."[19] In its proposal for Track A Rate Averaging Support, MAG itself proposed additional universal service support to offset both CCL and traffic sensitive access charges.[20] In promoting its own plan, MAG itself recognized that high access charges curb long distance competition, stating "In high cost markets, like many rural areas, long distance carriers have strong incentives not to serve consumers due to higher access rates."[21] MAG therefore touted lowering of access charges as a consumer benefit, stating "The [MAG] Plan goes beyond simply calling for enforcement of section 254(g); by lowering access charges, the Plan makes it much easier for long distance companies to comply with the law. This will give consumers more carriers and calling plans to choose from."[22] This consumer benefit - which is more comprehensively delivered under the RCC Plan than MAG Track A because the RCC Plan provides universal service support to all non-price cap LECs - flows from increased competition and is

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15 *Id.*

16 RTF Recommendation at 30.

17 *Id.* at 31.

18 *Id.*

19 MAG Aug. 20 ex parte.

20 *See* Petition for Rulemaking of the Multi-Association Group, Exhibit 1 at 1-17 (filed Oct. 20, 2000) ("MAG Plan").

21 "Consumer Benefits Multi-Association Group Plan," available at http://www.usta.org/mag_consumer_benefits.html.

22 *Id.* In addition, in their 1998 Reply Comments in CC Docket No. 98-77, MAG members NRTA and NRTC stated: "Using a federal universal service mechanism [to reduce high rural access rates] would be manifestly appropriate, since the geographic rate averaging requirement is imposed as a component of the Act's universal service provisions." Reply Comments of National Rural Telecommunications Association and National Telephone Cooperative Association at 23 (filed September 17, 1998) ("NRTA/NRTC Comments").

independent of any consumer benefits from lower long distance prices due to access charge reductions. As will be discussed further below, MAG's proposals for regulations to require "pass through" and to ban minimum charges are both unnecessary and unwise.

MAG's criticism of HCF III – Local Switching as lacking an economic basis is particularly ironic because MAG's proposed RAS and its associated Carrier Access Rate themselves lack a cogent economic basis, and are merely judgments by MAG about the level of a comparable carrier-paid traffic sensitive access charge. MAG's own explanation for its $.016 Carrier Access Rate is unsound. MAG's comparison between the reduction in access rates for price cap LECs under CALLS and the traffic sensitive reductions for non-price cap LECs ignores the fact that price cap LECs were making real revenue per unit reductions, not just reallocations between USF and carrier-paid access charges, both under the *CALLS Order* and in prior years.[23] MAG also conflates common line subsidies, which support the non-traffic sensitive costs of providing service in high cost areas, with support for the higher traffic sensitive costs of rural, rate-of-return companies. It also ignores the fact that non-price cap LECs have not yet undertaken a number of necessary rate structure reforms, such as the "catch-up" reforms identified in the RCC Plan and the recovery of additional common line costs from flat-rated charges rather than CCL charges.[24] Any comparison between price cap LEC and non-price cap LEC average traffic sensitive charges, and reductions thereto, can therefore only be made after implementation of "catch-up" reforms and at least some of the SLC reforms. To do otherwise irrationally ignores the impact of the 1997 price cap LEC reforms in making the comparison between the reduction in usage sensitive charges under the *CALLS Order* and the reductions necessary to make proportionate reductions to usage sensitive charges for the non-price cap LECs.

HCF III – Local Switching, as proposed by the RCC Plan, is a more targeted subsidy for traffic sensitive access charges than MAG's proposed RAS, as HCF III – Local Switching would not subsidize special access and does not preclude entry by competing transport carriers to provide special access, or dedicated or common transport. Once all other RCC Plan reallocations have also been made, the $.0025/minute brings the NECA average access rate to $.0095/minute and, excluding subsidy payments, to the same level as for small price cap LECs with extremely low teledensity.

$.0095/minute is a reasonable target for total average NECA access charges because it is consistent with the range of comparability in carrier-paid average traffic sensitive charges adopted by the Commission for the price cap LECs. Adopting some other target, such as MAG's proposed carrier access rate of $.016/minute, requires the Commission to justify the use of yet another number instead of its existing targets.

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23 *See* MAG Plan, Exhibit 1 at 1-7 (describing the Carrier Access Rate).

24 The *1997 Access Reform Order* reduced price cap LEC average usage sensitive charges by increasing the cap on the multiline business SLC, raising the SLC cap for non-primary residential lines, and creating the presubscribed interexchange carrier charges. None of these changes has occurred for non-price cap LECs, and traffic sensitive common line recovery has not been converted to non-traffic sensitive recovery through any other access reform for the non-price cap LECs.

It is also critical to recognize HCF III – Local Switching does not reduce ILEC switching *cost recovery* to $.0025/minute. Non-price cap LECs continue to recover their entire local switching revenue requirement, with the revenues split between a USF-paid HCF III – Local Switching and the carrier-paid local switching access charge. MAG's criticism of the RCC Plan appears to confuse total recovery of local switching costs, which is not reduced, with the creation of a subsidy so that carrier-paid local switching charges (and thus total carrier-paid access charges) can be reduced in areas where they would be extremely high.

MAG suggests that HCF III – Local Switching is unnecessary because of the existing local switching support.[25] This is backwards, as HCF III – Local Switching is complementary to Local Switching Support. Local Switching Support replaced DEM Weighting, which supported costs that, but for the DEM weighting formula, would have been assigned to the intrastate jurisdiction to be recovered through intrastate rates. The same high switching costs for small rate-of-return LECs that justified the creation of Local Switching Support to defray the intrastate portion of costs also justify the creation of HCF III – Local Switching to help defray the interstate portion of those costs.

Fifth, MAG argues that the TIC should not be reallocated to common line because the TIC reflects costs of interexchange transport services.[26] This characterization of TIC costs is not accurate, and also is not dispositive. Although the TIC was originally derived from allocated costs in order to meet the equal unit charge rule, in 1997 the FCC required all LECs, including non-price cap LECs, to reallocate costs associated with specific transport facilities from the TIC to the facilities elements.[27] For non-price cap LECs, certain costs associated with multiplexers and dedicated trunk ports used in connection with the tandem switch were allowed to remain in the TIC, but the bulk of the TIC is now comprised of residual costs that incumbent LECs were not able to reallocate to transport facilities.[28] The Commission has already proposed to reallocate the costs of multiplexers and dedicated trunk ports to new facilities rate elements, just as was done for the price cap LECs.[29] Excluding those costs, the TIC would contain no costs of specific transport facilities that should be paid by the IXC purchasing the transport service. If there are identifiable facilities costs in the TIC today, they can and should be reallocated to the appropriate facilities elements, and all remaining residual TIC revenue requirements should be reallocated to common line for non-traffic sensitive recovery. Indeed, the FCC must require any identifiable facilities costs to be reallocated to facilities elements in order to comply with the mandate in *Competitive Telecommunications Ass'n v. FCC*, 87 F.3d 522, 536 (D.C. Cir. 1996) ("*CompTel*").

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25 MAG CCB ex parte at 2.

26 *Id.* at 2.

27 *1997 Access Reform Order* at ¶¶ 214-23.

28 *Id.* at ¶¶ 219, 221.

29 *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, 13 FCC Rcd. 14238 ¶¶ 67-68 (1998) ("*1998 Access Reform NPRM*").

MAG offers no logical, non-arbitrary reason why residual, non-identifiable TIC costs should be recovered from end users/USF for price cap LECs, but for non-price cap LECs these same non-identifiable costs should be recovered through a per-minute surcharge on use of local switching. Nor does MAG explain how failure to implement a cost-based rate structure could comply with the mandate in *CompTel*. The fact that price cap LECs in part eliminated the TIC through application of X-factor reductions does not provide a basis for distinction. As the Commission recognized in 1997, targeting of X-factor reductions effectively spread the TIC costs to the non-targeted elements, which predominantly were common line elements.[30] The *CALLS Order* then reduced switching and transport charges further, while not reducing common line rates, thus further spreading these residual TIC costs into common line.[31] Shifting recovery of non-identifiable TIC costs to common line for non-traffic sensitive recovery is the only solution that is logically consistent with both the *1997 Access Reform Order* and the *CALLS Order* treatment of TIC costs for price-cap LECs.

In the Wallman ex parte, a group of incumbent LECs inexplicably state that the record "supports no changes beyond increasing the SLC by the CALLS/MAG levels and reducing the CCLs by a comparable amount."[32] This is simply untrue. The Commission received comment in response to the NPRM in Docket No. 98-77 in which commenters supported implementation of the "catch-up" access charge reforms now incorporated into the RCC proposal.[33] There has been full notice of these proposals, and there is a record to support the Commission's adoption of its tentative conclusions from the *1998 Access Reform NPRM*.

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30 *1997 Access Reform Order* at ¶ 234 ("Drawing down the per-minute-of-use residual TIC charge by targeting the price cap productivity (X-factor) adjustment to the trunking PCI and, specifically, the TIC SBI, thus effectively spreading those residual TIC revenues . . . among the universe of (both traffic-sensitive and [non-traffic sensitive]) access services and moving TIC recovery closer to flat-rated recovery."). The *1997 Access Reform Order* also directly shifted some TIC recovery to the PICC, where PICCs were not otherwise at applicable caps. *Id.*

31 *CALLS Order* at ¶¶ 141, 151. Under the *CALLS Order*, X-factor reductions for switched access services were targeted first to eliminate the residual TIC, then to reduce average traffic sensitive access charges to the applicable target rate. Special access services were placed in a separate basket and were unaffected by this targeting. Taken together, these changes meant that all X-factor reductions that eliminated the residual TIC were reductions that, under the pre-*CALLS Order* rules, would have gone to reduce the price cap in the common line basket. Just as under the *1997 Access Reform Order*, TIC costs were therefore spread to the common line basket, which was renamed the Common Line/Marketing/TIC (CMT) basket. In addition, by eliminating the residential and single line business PICC and recovering TIC costs in the CMT basket, TIC recovery contained in the IXC-paid PICC under the *1997 Access Reform Order* was shifted to the end user-paid SLC under the *CALLS Order*.

32 Wallman ex parte at 1.

33 For proposals and FCC tentative conclusions, *see 1998 Access Reform NPRM*. For supportive comments, *see* Comments of AT&T, CC Docket No. 98-77 at 12-16 (filed Aug. 17, 1998); Reply Comments of AT&T, CC Docket No. 98-77 at 8-9 & 12-13 (filed Sept. 17, 1998) ("AT&T ROR Reply"). Some other commenters did not object to the FCC's proposed reforms in principle, but suggested that they be deferred until they could result in actual rate structure changes, rather than simply shifting charges between different per minute rate elements. *See* MCI Comments, CC Docket No. 98-77 (filed Aug. 17, 1998). Because the RCC Plan results in shifting these charges to SLCs or to USF support and eliminating them from per minute IXC-paid access rates, the reasons for deferral are now eliminated.

Sixth, in its objection to reallocation of additional GSF costs to billing and collection, MAG repeats comments from 1998 asserting that this reform should not be undertaken because many rate-of-return LECs use outside billing vendors.[34] However, as AT&T pointed out in its 1998 Reply Comments, the record showed that many rate-of-return LECs did not rely on outside vendors.[35] Indeed, NRTA and NRTC estimated at the time that fewer than half their members used outside vendors.[36] The fact that some LECs may use outside vendors is not a reason for failing to treat rate-of-return LECs that do their own billing and collection in the same manner as other LECs that do their own billing and collection. Indeed, it would be arbitrary and capricious not to institute this "catch-up" reform for the rate-of-return LECs that do their own billing and collection.

Finally, MAG attacks the RCC Plan for not including requirements to re-regulate interstate long distance services through mandatory "pass-through" requirements, prohibitions on minimum charges for basic service customers, and requirements related to the offering of optional calling plans.[37] Such regulatory requirements are, however, wholly unnecessary in the highly competitive long distance market, and would restrict service offerings for consumers. As Chairman Powell has recognized, "The long distance industry is highly competitive and has created greater choice and value for all consumers."[38] Adoption of the RCC Plan will increase competition in long distance services in rural areas, by lowering the disincentives to entry created by today's high rural access charges. By both reducing costs of existing providers and increasing entry, the RCC Plan makes it substantially more likely that rural consumers will be able to benefit from competitive response offerings. As competition increases, it is also more likely that rural areas will be offered promotional discounts. MAG makes no demonstration that there is any market failure that needs to be addressed through regulation, either now or after implementation of the RCC Plan. MAG simply proposes "more burdensome, demand-stifling, innovation-sapping regulations."[39]

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[34] MAG CCB ex parte at 2.

[35] AT&T ROR Reply at 13.

[36] NRTA/NRTC Comments at 31 (estimating that 40% of NRTA/NRTC member LECs use outside billing and collection vendors rather than their own general purpose computers).

[37] MAG CCB ex parte at 1.

[38] *Low-Volume Long Distance Users*, 15 FCC Rcd. 6298, 6322 (1999) (Separate Statement of Commissioner Michael K. Powell, concurring).

[39] *Id.*

The Rural Consumer Choice Plan, as put forward by AT&T, GCI and Western Wireless is the only full plan for non-price cap universal service and access charge reform that is consistent with the express terms of the Communications Act as clarified by a series of decisions of the United States Court of Appeals for the Fifth Circuit, and with the Commission's prior access charge and universal service reform decisions. If adopted, the Rural Consumer Choice Plan will harness the power of the market to deliver rural consumers served by non-price cap LECs a wider range of choices for local and long distance services, and more innovative service offerings and packages.

Sincerely,

/s/ John T. Nakahata

John T. Nakahata
Counsel for AT&T, GCI and Western Wireless

c: Kyle Dixon, Legal Adviser to the Chairman
Deena Shetler, Legal Adviser to Commissioner Tristani
Matthew Brill, Legal Adviser to Commissioner Abernathy
Jordan Goldstein, Senior Legal Adviser to Commissioner Copps
Sam Feder, Legal Adviser to Commissioner Martin
Dorothy Attwood, Chief, Common Carrier Bureau
Carol Mattey, Deputy Chief, Common Carrier Bureau
Rich Lerner, Deputy Chief, Competitive Pricing Division, CCB
Bill Scher, Attorney, Accounting Policy Division, CCB