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

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In the Matter of

Multi-Association Group Plan for
Regulation of Interstate Services of
Non-Price Cap Incumbent Local Exchange
Carriers and Interexchange Carriers

CC Docket No. 00-256

Federal-State Joint Board on
Universal Service

CC Docket No. 96-45

Access Charge Reform for Incumbent
Local Exchange Carriers Subject to
Rate-of-Return Regulation

CC Docket No. 98-77

Prescribing the Authorized Rate of Return for
Interstate Services of Local Exchange Carriers

CC Docket No. 98-166

**COMMENTS
of the
GENERAL SERVICES ADMINISTRATION**

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Summary

In recent orders, the Commission ruled on several aspects of a comprehensive proposal by carrier associations to reform the regulatory regime for rate-of-return LECs. GSA responds to requests by the Commission for comments on additional facets of the proposed plan.

At the outset, GSA urges the Commission to employ a productivity offset as an essential element of regulation for all carriers that transition to price caps. Competitive LECs, interexchange carriers, state regulators, and end users have explained that an offset is necessary because there are significant differences between productivity changes for the telecommunications industry and those for the economy as a whole.

GSA notes that when the Commission initiated price cap regulation for the larger LECs, it implemented multiple safeguards for consumers. For those carriers, the Commission: (1) established a procedure for earnings sharing; (2) re-initialized carriers' rates; and (3) introduced a productivity offset in the price cap formula. Thus, if the Commission does not wish to have earnings sharing or re-visit rate levels, a productivity offset is needed as the minimum step to protect the interests of consumers as the smaller LECs transition to price caps.

GSA also urges the Commission to conclude that the "all-or-nothing" rule should not be discarded, as the carrier associations proposed. This Commission rule helps prevent carriers from benefiting by shifting "revenue requirements" between affiliates (or study areas) subject to different types of regulation.

Finally, GSA recommends that the Commission monitor service quality levels for carriers transitioning to price caps. Competition among LECs has not reached the point where it can replace regulatory surveillance. Moreover, as competition increases, it is even more important for consumers to have the information needed to make informed choices among alternative suppliers. Finally, service quality reporting in a uniform format will help motivate rate-of-return carriers to maintain high performance levels.

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**COMMENTS
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GENERAL SERVICES ADMINISTRATION**

The General Services Administration ("GSA") submits these Comments on behalf of the customer interests of all Federal Executive Agencies ("FEAs") in response to the Further Notice of Proposed Rulemaking ("Further Notice") in CC Docket No. 00-256 released on November 8, 2001. The Further Notice was adopted concurrently with the Second Report and Order in CC Docket No. 00-256, the Fifteenth Report and Order in CC Docket No. 96-45, and the Report and Order in CC Docket Nos. 98-77 and 98-166 ("MAG Orders").

In the MAG Orders, the Commission addressed a Petition for Rulemaking ("Petition") submitted on October 20, 2000 by the Multi-Association Group ("MAG"). The Commission performed a comprehensive analysis of MAG's proposed regulatory plan. However, the Commission did not address several facets of the plan because it

found that inputs from carriers and other parties would be beneficial before additional rulings. The Further Notice seeks comments and replies on several of these open issues.

I. INTRODUCTION

Pursuant to Section 201(a)(4) of the Federal Property and Administrative Services Act of 1949, as amended, 40 U.S.C. 481(a)(4), GSA is vested with the responsibility to represent the customer interests of the FEAs before Federal and state regulatory agencies. From their perspective as end users, the FEAs have consistently supported the Commission's efforts to bring the benefits of competitive markets to consumers of all telecommunications services.

As contemplated by the Telecommunications Act of 1996, the Commission has taken significant steps to extend the benefits of competition and choice by reforming rate structures and bringing per-minute rates to more cost-based levels, while furthering universal service goals.¹ For carriers under price cap regulation, this process began in 1997 and continued through the *CALLS Order*.² In the MAG Orders, the Commission implements several parallel reforms for local exchange carriers ("LECs") under rate-of-return regulation.³ The Commission takes these steps as a selective response to the comprehensive set of regulatory reforms proposed by MAG.⁴

¹ MAG Orders, para. 1, citing Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56, codified at 47 U.S.C. § 151 *et seq.* ("Telecommunications Act").

² *In the Matter of Access Charge Reform and Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262 and 94-1, Sixth Report and Order, *Low-Volume Long-Distance Users*, CC Docket No. 99-249, Report and Order, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Eleventh Report and Order, 15 FCC Rcd 12962 (*"CALLS Order"*), *aff'd in part, rev'd in part, and remanded in part, Texas Office of Public Util. Counsel et al. v. FCC*, 5th Cir. Nos. 00-60434 (5th Cir. September 10, 2001).

³ MAG Orders, para. 1.

⁴ *Id.*, para. 10.

MAG includes the National Rural Telephone Association (“NRTA”), the National Telephone Cooperative Association (“NTCA”), the Organization for the Promotion and Advancement of Small Telephone Companies (“OPASTCO”) and the United States Telecom Association (“USTA”).⁵ Together, these organizations represent a diverse group of incumbent local exchange carriers. Their Petition describes a comprehensive approach to regulatory issues facing non-price cap carriers — the smaller and mid-size LECs serving many rural and insular areas. MAG asks the Commission to adopt its proposed plan as a total package.⁶

GSA submitted Comments and Reply Comments on the petition in response to the Notice of Proposed Rulemaking released on January 5, 2001.⁷ In those submissions, GSA urged the Commission not to adopt the proposed regulatory regime without modifications.⁸ For example, GSA acknowledged that several of the proposed revisions in the structure of interstate access charges would be beneficial, but explained that other conditions would place undue burdens on business multi-line users.⁹ Also, GSA acknowledged that MAG’s plan will motivate smaller LECs to expand their services and invest in new technologies, but cautioned that modifications in the price cap formula are necessary to account for the differences in productivity between the telecommunications industry and the national economy.¹⁰

⁵ Petition, p. 1.

⁶ MAG Orders, para. 3.

⁷ Comments of GSA, February 26, 2001; and Reply Comments of GSA, March 12, 2001.

⁸ Comments of GSA, pp. 7-9; and Reply Comments of GSA, pp. 4-7.

⁹ Comments of GSA, pp. 7-9; and Reply Comments of GSA, pp. 7-9.

¹⁰ Comments of GSA, pp. 10-15; and Reply Comments of GSA, pp. 10-13.

In the MAG Orders, the Commission changes the access charge rules and modifies the universal service support system for rate-of-return carriers in several important ways. For example, the Commission:

- adopts MAG's proposal to increase the caps on subscriber line charges ("SLCs");
- establishes a plan to phase-out the common carrier line ("CCL") charge by July 1, 2003;
- implements measures to align the local switching and transport rate structures with costs;
- creates a new universal service support mechanism to convert implicit support to explicit support that will be available to all eligible telecommunications carriers; and
- modifies the existing rules to allow limited geographic deaveraging of access charges.¹¹

The Commission takes several additional steps regarding pricing rules and universal service, but stops short of specifying the parameters of an incentive plan for rate-of-return LECs.

In the Further Notice, the Commission seeks recommendations on measures to give additional pricing flexibility to the smaller LECs.¹² Also, the Commission requests comments on the MAG's proposed changes to the "all-or-nothing" rule concerning price regulation.¹³ Finally, the Commission seeks comments on quality assurance and expansion of new and advanced services in areas served by rate-of-return carriers under any alternative regulatory plan that it may adopt.¹⁴

¹¹ MAG Orders, para. 15.

¹² *Id.*

¹³ *Id.*

¹⁴ *Id.*, para. 224.

II. A PRODUCTIVITY OFFSET IS AN ESSENTIAL ELEMENT OF PRICE CAPS FOR RATE-OF-RETURN CARRIERS.

The MAG plan specifies procedures for rate-of-return LECs to transition to incentive regulation over a period that may be as long as five years.¹⁵ The carrier's rates and charges would initially be based on the current settlements from the National Exchange Carrier Association ("NECA") pools, and subsequently increased by the amount of inflation each year.¹⁶ MAG's plan does not include any initial rate reductions, nor any offset (sometimes called the "X-factor") to account for differences between productivity improvements for the telecommunications industry and those for the economy as a whole.

The Commission observes that several parties explain that any sound regulatory plan should include a productivity offset to ensure that rates remain "just and reasonable."¹⁷ Several of these parties observe that the telephone industry has traditionally achieved greater productivity improvements than are reflected in the national Gross Domestic Product Price Index ("GDP-PI").¹⁸ To address this issue, the Further Notice invites parties to comment on the extent to which a productivity offset should be part of any regulatory plan prescribed for rate-of-return carriers.¹⁹

GSA was one of the parties urging the Commission to include a productivity offset in any plan for carriers that transition to price caps.²⁰ Other end users urged the Commission to employ a 6.5 percent X-factor for these carriers.²¹

¹⁵ Notice of Proposed Rulemaking, January 5, 2001, para. 15.

¹⁶ Further Notice, para. 234.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*, para. 235.

²⁰ Reply Comments of GSA, March 12, 2001, pp. 10-11.

²¹ Comments of Ad Hoc Telecommunications Users Committee, February 16, 2001, pp. 15-17.

State regulators have also described the need for a productivity offset. For example, the People of the State of California and the California Public Utility Commission (“California”) explain that there is no basis to conclude that the costs incurred by rural LECs will increase in proportion to the GDP-PI.²² These regulators urge the Commission to include a productivity adjustment for carriers transitioning from rate-of-return regulation, and recommend that the Commission initiate a proceeding to determine the appropriate magnitude of this factor.²³

A carrier providing interexchange and local exchange services, General Communications, Inc. (“GCI”), provides quantitative evidence demonstrating the need for a productivity offset in the price cap formula. GCI shows that between 1994 to 1998, the average unseparated cost for a local loop declined one percent per year for all carriers nationwide, although inflation measured by the GDP-PI averaged 1.9 percent per year.²⁴ Thus, loop costs declined about three percent per year relative to inflation.

When price cap regulation was initiated for the larger LECs, the Commission: (1) implemented a procedure to share earnings above established thresholds between carriers and their customers; (2) initialized rates following a review of the current cost of capital; and (3) included a productivity offset in the price cap formula.²⁵

There is no indication in the Further Notice that “earnings sharing” is even being considered for rate-of-return LECs. Moreover, the Commission has terminated the proceeding for prescription of rate-of-return levels that were most recently reviewed

22 Comments of California, February 16, 2001, p. 22.

23 *Id.*

24 Comments of GCI, February 16, 2001, p. 5.

25 Further Notice, para. 221.

more than 10 years ago.²⁶ Therefore, as a minimum step to safeguard the interests of consumers, the Commission should require a productivity offset as an element of the price cap plan.

III. THE “ALL-OR-NOTHING” RULE PROVIDES SIGNIFICANT BENEFITS FOR CONSUMERS.

Section 61.41 of the Commission’s rules contains requirements concerning mergers and acquisitions, and rules concerning transitions to and from price caps. The section states that if a carrier (or study area) converts to price cap regulation, all of its affiliates (or study areas) must make this same transition.”²⁷ Also, if a carrier under price caps is involved in a merger, acquisition, or similar transaction, it must continue to operate under the price cap regime after the re-organization.²⁸ In addition, when rate-of-return and price cap carriers merge or acquire one another, the rate-of-return carrier must convert to price caps within one year.²⁹ Finally, LECs coming under price caps are not permitted to withdraw from such regulation, or participate in NECA tariffs without a waiver.³⁰ The Commission invites comments on whether these provisions, generally referred to collectively as the “all-or-nothing” rule, should be continued at this time.³¹

GSA urges the Commission to find that the “all-or-nothing” rule provides important protections for consumers. Without such restraints, a LEC might shift costs from its price cap affiliate to an affiliate under rate-of-return regulation. This step

²⁶ MAG Orders, para. 15.

²⁷ Further Notice, para. 260.

²⁸ *Id.*

²⁹ *Id.*

³⁰ *Id.*

³¹ *Id.*, para. 15.

would permit a non-price cap affiliate to increase its charges to meet the greater "revenue requirement" with no counterbalancing benefits for users of services under price caps.

Moreover, constraints on transitions between rate-of-return and price cap regulation help prevent a carrier from attempting to "game the system."³² Without such constraints, a carrier could increase earnings by opting out of price cap regulation, then build a larger rate base under rate-of-return regulation in order to increase its income, and finally return to price cap regulation, cutting costs back to an "efficient" level. The Commission has noted that this procedure does not serve the public interest, and has granted waivers only where petitioners have shown good cause.³³

In its comments in this proceeding early this year, AT&T explained that MAG is not correct in contending that the Commission's current accounting and reporting requirements are sufficient to guard against cost-shifting.³⁴ WorldCom expressed similar cautions, explaining that detection of cost-shifting would be especially difficult for the smaller LECs because there is relaxed oversight of their accounting practices.³⁵

GSA concurs with AT&T and WorldCom on this issue. Therefore, GSA urges the Commission to continue the requirements in Section 61.41 of the rules without change.

³² *Id.*, para. 261.

³³ *Id.*

³⁴ Reply Comments of AT&T Corp. ("AT&T"), March 12, 2001, p. 17.

³⁵ Comments of WorldCom, February 26, 2001, p. 5.

IV. THE COMMISSION SHOULD MONITOR SERVICE QUALITY LEVELS FOR CARRIERS TRANSITIONING TO PRICE CAPS.

The Commission seeks comments on maintaining service quality for rate-of-return LECs as they transition to price caps.³⁶ The Further Notice poses the possibility that the Commission might choose to rely on state programs to ensure that adequate investment and service quality levels are maintained.³⁷

GSA urges the Commission to play a significant role in maintaining high service quality and not rely, even principally, on other regulatory authorities. As one step, GSA recommends that the Commission carefully monitor service quality levels for incumbent LECs under any regulatory regime.

In its Comments earlier this year in CC Docket No. 00–229, GSA urged the Commission to maintain service quality reporting requirements for LECs under price caps.³⁸ Addressing proposals by several carriers to reduce the scope of reporting, GSA explained that service quality data continues to be vital, even for experienced consumers.³⁹

Competition among carriers providing local services has not reached the point where it replaces the need for regulatory surveillance. Indeed, the most recent report by the Common Carrier Bureau's Industry Analysis Division shows that competitive LECs served only 8.5 percent of end user lines as of December 31, 2000.⁴⁰ Moreover, only 35 percent of this small fraction — that is, three percent of the total lines — were served using the competitive LECs' own facilities.⁴¹ To provide services to two-thirds

³⁶ Further Notice, para. 224.

³⁷ *Id.*

³⁸ CC Docket No. 00–229, Comments of GSA, January 12, 2001.

³⁹ *Id.*, p. 4.

⁴⁰ Industry Analysis Division, *Trends in Telephone Service*, May 21, 2001, Table 1.

⁴¹ *Id.*, Table 3.

of their lines, competitors either “resold” facilities owned by incumbent LECs or employed the incumbents’ unbundled network elements (“UNEs”).⁴²

Moreover, any ensuing increases in competition will not eliminate the need for service quality data. Indeed, an independent means to help consumers predict service levels and evaluate carriers’ service claims is particularly important with more competition.

In the first place, service quality data is necessary to make informed choices among alternative suppliers. Secondly, the presence of competitors provides a potential incentive for carriers to “cut corners” in order to offer their services at lower prices, with the hope that once committed, subscribers will not quickly change their local exchange service provider.

Many government and commercial users are experienced in procuring telecommunications services in a competitive environment, but they still need service quality information. Although service quality levels are often specified in contracts, business users depend on public information concerning the service levels met by carriers. In fact, service quality for the carriers operating in a region may be a primary factor in establishing the technical specifications in a request for proposals for firms to provide telecommunications services. Also, service quality achievements provide an independent means of assessing the likelihood that a carrier will meet the commitments in its proposal to provide telecommunications services under a contract. Finally, service quality reporting in a uniform format will provide an important motivation to rate-of-return carriers to maintain high service quality levels.

GSA recommends that the Commission require reporting by rate-of-return carriers for only six basic service quality measures in the Automated Reporting

⁴² *Id.*

Management Information System ("ARMIS"). These measures are: (1) the percentage of installation appointments that are met; (2) the time required to initiate service; (3) the percentage of lines that have problems, including out-of-service lines; (4) the time required to have out-of-service lines repaired; (5) the percentage of repair appointments that are missed; and (6) the time required to repair service.⁴³ These minimal reporting requirements should not place an unreasonable burden, even on the smaller LECs.

⁴³ CC Docket No. 00-229, Notice of Proposed Rulemaking, November 9, 2000, para. 16.

V. CONCLUSION

As a major user of telecommunications services, GSA urges the Commission to implement the recommendations set forth in these Comments.

Respectfully submitted,

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CERTIFICATE OF SERVICE

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