

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

In the Matter of)	
)	
Multi-Association Group (MAG) 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 VERIZON¹

The Commission should allow carriers that convert from rate of return to price cap regulation to retain the level of Long Term Support (“LTS”) to which they would otherwise be entitled, both before and after LTS is merged with Interstate Common Line Support. In this way, customers of high-cost carriers will not suffer sudden rate increases and the continued support to such carriers will not be at the expense of existing price cap carriers, whose universal service support from a capped fund would otherwise decline. In addition, the Commission should eliminate the “all or nothing” rule under which rate of return carriers acquired by price cap carriers are required to convert to price cap regulation. To the extent the Commission’s concerns

¹ The Verizon telephone companies (“Verizon”) are the local exchange carriers affiliated with Verizon Communications Inc. identified in the attached list.

that led it to establish the rule are still valid - ten years after it was adopted - there are other effective means to address any remaining issues about cost shifting or regulatory gaming.

ARGUMENT

In the *Further Notice of Proposed Rulemaking*, the Commission asked how rate of return carriers that are required to convert to price cap regulation should receive universal service support. 16 FCC Rcd 19613, ¶ 271 (2001) (“Notice”). As an example, the Commission cited the Puerto Rico Telephone Company (“PRTC”), a rate of return carrier which receives a significant amount of LTS as a rate of return carrier. Under existing rules, PRTC would need to convert to price cap regulation, because a controlling interest in PRTC was acquired by Verizon, whose existing local telephone carriers are under price caps.² See 47 C.F.R. § 61.41(c)(2). Such conversion could substantially reduce the level of high-cost support that PRTC receives today and could result in substantial rate increases for its customers. Such increases, in turn, could reduce subscribership in Puerto Rico, which is already substantially below the national average. Likewise, if the amount of universal service support to which PRTC and other rate of return carriers that convert to price caps would be entitled, albeit lower than their prior LTS, were taken from the capped Interstate Access Universal Service Support, the amount available to existing price cap carriers would decline. The result could be that some of those carriers would be unable to eliminate the support in Carrier Common Line and Presubscribed Interexchange Carrier

² The Commission granted PRTC a temporary waiver to allow it to continue operating as a rate of return carrier until July 1, 2002. *Puerto Rican Tel. Co. Petition for Waiver of Section 61.41 or Section 54.303(a) of the Commission’s Rules*, 16 FCC Rcd 12343, ¶ 7 (2001) (“PRTC Order”). PRTC recently filed to extend that waiver.

Charges, because there would be insufficient explicit Interstate Access Universal Service Support to cover those amounts.

When the Commission capped the explicit Interstate Access Universal Service Support at \$650 million, which it estimated covered a reasonable amount of the implicit support in the access charges of the price cap carriers, it “did not explicitly address how entry of new carriers into price caps affects distribution of interstate access universal service support.” PRTC Order at ¶ 7.³ As a result, any additional support distributed from the Interstate Access Universal Service Support to new price cap carriers would come at the expense of existing carriers. This could undermine the Commission’s goal of holding existing price cap carriers harmless during the conversion from implicit to explicit universal service support. *See* CALLS Order at ¶ 202. It would also be inconsistent with the Commission’s intent that the level of high-cost support be “specific, predictable, and sufficient.” *Id.* at ¶ 201. To avoid this result, rather than undermining the CALLS Order by attempting to increase the level of the Interstate Access Universal Service Support each time a rate of return carrier moves to price caps, the Commission should establish a mechanism to allow affected carriers to retain the amount of LTS to which they would otherwise be entitled, both before and after LTS is merged with Interstate Common Line Support.⁴

This could not occur without a rule change, however, because price cap carriers are today ineligible to participate in LTS, nor would they receive the new Interstate Common Line

³ The fund was capped at \$650 million in the CALLS Order, 15 FCC Rcd 12962, ¶¶ 201-205 (2000); 47 C.F.R. § 54.801(a). Although that order was remanded to better explain the calculation of the \$650 million cap, the reviewing court did not disagree that the Commission could establish a cap on the high-cost fund. Nor did it disagree that the Commission could retain the same cap. *See Texas Office of Public Util. Counsel v. FCC*, 265 F.3d 313 (5th Cir., 2001).

⁴ The Commission has tentatively concluded that the merger of those two support mechanisms will occur effective July 1, 2003. Notice at ¶ 274.

Support. Acquired carriers would have no alternative but to recover their universal service support from the Interstate Access Universal Service Support fund, and, as indicated, this would undermine the existing cap and/or other carriers' support.

The cleanest and most equitable way to avoid this result is to modify the "all or nothing" rule, section 61.41(c)(2). In this way, rate of return local exchange carriers that are acquired by price cap carriers could elect to remain under rate of return regulation.⁵ That rule was adopted more than a decade ago, based on the fear that price cap carriers would have the ability to shift costs to rate of return carriers they acquire or that they might attempt to "game the system" by switching back and forth between rate of return and price cap regulation. *See Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd 6786, ¶¶ 271-279 (1990); *modified on recon.*, 6 FCC Rcd 2637, ¶ 148 (1991).

By the same token, acquired rate of return carriers that choose price caps should be able to continue to receive Long Term Support, or its successor. This will protect the level of support that the carrier receives while not affecting the support levels received by other price cap carriers.

The first concern that led to the "all or nothing" rule was that carriers would attempt to shift costs to rate of return affiliates that should be attributed to the price cap carriers. However, since 1991, the Commission has readily granted waivers to both large and small price cap carriers that have acquired rate of return carriers.⁶ In each instance, the Commission found that the concerns about cost-shifting were unwarranted in the particular case before it. The fact is

⁵ The Commission asks whether the "all or nothing" rule should be retained in the Notice at ¶¶ 266-271.

⁶ *See, e.g., Gila River Telecommunications, Inc.*, 7 FCC Rcd 2161 (1992); *U.S. WEST Communications, Inc.*, 9 FCC Rcd 202 (1993); PRTC Order.

that those fears are unwarranted in any case. Accounting, cost allocation rules, jurisdictional separations procedures, and reporting requirements all protect against cost-shifting and make any attempt to shift costs easily detectable. In particular, the Commission's Part 32 Uniform System of Accounts rules, the Part 36 Separations rules, and the Part 64 cost allocation rules, all effectively safeguard investment and cost tracking and prevent carriers from shifting costs from one entity to another. Similarly, under Part 61 and Part 69 of the rules, carriers must provide sufficient detail and supporting information with tariff filings and tariff review plans that cost shifting is not possible.

The Commission's second concern in adopting the "all or nothing" rule was that carriers would attempt to "game the system" by switching an affiliate back and forth between regulatory schemes. The Commission can entirely eliminate this concern simply by making an acquired carrier's election to price cap or rate of return regulation irreversible, barring a waiver for good cause shown.⁷

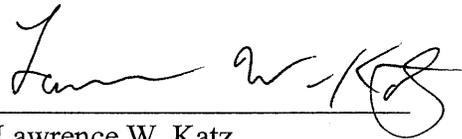
Also, in the past, a substantial portion of universal service support was embedded in access rates. Today, as required under the 1996 Act, much of this support has been removed from service rates and is recovered through separate charges. And this support is portable, so that competitors that serve high-cost areas are eligible to receive support. As a result, it would be nearly impossible for carriers to shift universal service costs among affiliates. In addition, as part of access reform, the FCC's pricing flexibility rules, and the CALLS plan, price cap carriers

⁷ Further, the FCC's concerns as they relate to PRTC are clearly not present. First, not only are the shifting of costs from the price cap affiliate (Verizon) to the non-price cap affiliate (PRTC) addressed by accounting and cost allocation rules, but they also would be clearly detectable. A switch investment or labor costs incurred by any other Verizon affiliate in any other jurisdiction simply could not be allocated to PRTC. Similarly, the second concern, that of switching back and forth between price cap and non-price cap regulation, is not relevant for PRTC, as eliminating the rule would simply provide continuity of regulation.

no longer have obligations and options related to over-earnings sharing and lower formula adjustments for under-earning. These changes also prevent carriers from “gaming the system” by shifting costs among affiliates. As a result, the concerns that led to the “all or nothing” rule no longer apply, and the rule should be repealed.

Accordingly, the Commission should allow rate of return carriers that are acquired by price cap carriers to retain the level of Long Term Support (or its successor) to which they would otherwise be entitled.

Respectfully submitted,



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THE VERIZON TELEPHONE COMPANIES

The Verizon telephone companies are the local exchange carriers affiliated with Verizon Communications Inc. These are:

Contel of the South, Inc. d/b/a Verizon Mid-States
GTE Midwest Incorporated d/b/a Verizon Midwest
GTE Southwest Incorporated d/b/a Verizon Southwest
The Micronesian Telecommunications Corporation
Verizon California Inc.
Verizon Delaware Inc.
Verizon Florida Inc.
Verizon Hawaii Inc.
Verizon Maryland Inc.
Verizon New England Inc.
Verizon New Jersey Inc.
Verizon New York Inc.
Verizon North Inc.
Verizon Northwest Inc.
Verizon Pennsylvania Inc.
Verizon South Inc.
Verizon Virginia Inc.
Verizon Washington, DC Inc.
Verizon West Coast Inc.
Verizon West Virginia Inc.