

**Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554**

In the matter of)
)
Multi-Association Group (MAG) Plan for) CC Docket No. 00-256
Regulation of Interstate Services of Non-Price)
Cap Incumbent Local Exchange Carriers and)
Interexchange Carriers)
)

**COMMENTS OF
THE NATIONAL EXCHANGE CARRIER ASSOCIATION, INC.**

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Summary

NECA's pooling process can accommodate a broad variety of incentive regulation plans in a manner that fully satisfies the Commission's goals in this proceeding. Pool settlement and rates setting processes can be adapted to accommodate any of the various incentive regulation plans currently under consideration by the Commission. Having large numbers of carriers continue to participate in the pool helps to stabilize monthly cash flows and pool earnings and avoids administrative burdens for the Commission and access customers. Adapting existing pooling approaches to incentive regulation mechanisms avoids the need for carriers to leave the NECA pools in order to gain the benefits of moving to an incentive-based regulatory system. The existing pooling mechanism can also easily be modified to encompass pricing flexibility proposals without imposing undue administrative burdens.

The Commission should leave existing Long Term Support rules in place pending review of the effects of access reform on rural carriers. Leaving existing rules in place will avoid risking harm to the NECA pooling process and will not disadvantage other carriers. The Commission should leave section 54.901(a)(5) in its current form, at least on an interim basis, pending longer-term review of the impacts of the MAG Order and other rule changes on rate of return carriers.

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The National Exchange Carrier Association, Inc. (NECA) submits these comments in response to the Commission's *Further Notice of Proposed Rulemaking* (FNPRM) in the above-captioned proceeding.¹ NECA's comments are focused on questions raised in the FNPRM related to pooling, in particular, whether incentive regulation plans for rate-of-return (ROR) carriers can be designed to work within the NECA pool, whether the pooling process can be adjusted to handle pricing flexibility options for ROR carriers without undue burden, and whether existing rules governing availability of Long Term Support (LTS) should be revised so as to consolidate LTS with the new Interstate Common Line Support (ICLS) mechanism.

¹ See 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, *Second Order and Further Notice of Proposed Rulemaking*, 66 Fed. Reg. 59761 (2001)(FNPRM).

I. THE NECA POOLING PROCESS CAN ACCOMMODATE INCENTIVE REGULATION IN A MANNER THAT FULLY ACCOMPLISHES THE COMMISSION’S GOALS IN THIS PROCEEDING.

In the FNPRM, the Commission states its objective to build on the alternative regulation proposal contained in the MAG plan and its experiences with incentive regulation for price cap carriers to develop an alternative regulatory structure for rate-of-return (ROR) carriers.² The Commission identifies perceived shortcomings in the MAG Incentive Regulation Proposal³ and suggests several principles for alternative regulation to ensure that rates remain just and reasonable, in accordance with section 201(b).⁴ The Commission then addresses a series of specific issues in developing an alternative regulatory plan.⁵

In its consideration of alternative regulation, the Commission asks for specific comment on the compatibility of these options with the NECA pooling process.⁶ The Commission notes that the pooling process affords administrative benefits to carriers and to the Commission but expresses concern that it may also “blunt some of the benefits” of an alternative regulation plan and give carriers little incentive to pursue cost efficiencies.⁷

² *Id.* at ¶ 212.

³ *Id.* at ¶¶ 217-220.

⁴ *Id.* at ¶¶ 221-226; 47 U.S.C. § 201(b).

⁵ *Id.* at ¶¶ 227-240. Issues for comment include optionality, alternative regulation in a pooling context, use of revenue per line, productivity and sharing, and monitoring considerations.

⁶ *Id.* at ¶ 228.

⁷ *Id.*

The Commission asks for comment on whether an alternative regulation plan can and should be designed to work with the NECA pooling structure and for suggestions on ways to revise pooling procedures to facilitate meaningful incentive regulation.⁸ In the alternative, the Commission asks whether ROR carriers should be required to leave the pool to participate in alternative regulation.⁹

The pooling process can accommodate a broad variety of incentive regulation plans in a manner that fully satisfies the Commission's goals in this proceeding. As the Commission is aware, NECA itself has previously proposed including optional incentive plans within its pooling system.¹⁰ NECA also reviewed details of the MAG alternative regulation plan prior to its filing and confirmed that the plan would work within the context of existing pooling and settlement mechanisms.¹¹

Accommodating incentive regulation within existing pooling mechanisms essentially involves establishment of a settlement mechanism that distributes access charge revenues to participating companies on a formula basis. Under a revenue-per-line plan, for example, companies would be eligible to include in rates a certain amount of expected revenue for each line served. That amount would then remain fixed, or would perhaps be subject to future adjustments based on a pre-defined formula, without regard to changes in

⁸ *Id.*

⁹ *Id.*

¹⁰ See Proposed Revision of Part 69 of the Commission's Rules to Allow for Incentive Settlement Options for NECA Pool Companies, *Petition for Rulemaking*, Nov. 5, 1993, and *Supplemental Comments*, May 15, 1995.

¹¹ See Letter to NRTA, NTCA, OPASTCO, and USTA (the Multi-Association Group) from James W. Frame, Vice President, Operations, NECA (Feb. 16, 2001)(Attachment 1 to Comments of LEC Multi-Association Group, Feb. 26, 2001).

the actual costs of providing service. Because company earnings would be dependent on the extent to which actual costs can be kept below the set revenue per line amount, companies would have incentives to keep costs low.

The same dynamics can apply in a pooling environment. Just as revenue per line amounts can be established for companies filing individual tariffs, NECA has the ability to set settlement per line amounts for individual companies within the pool.¹²

Banded rates for companies would then be established by projecting settlement levels for individual access elements and then setting rates to recover those settlements. That is, NECA would develop test period revenue requirements (projected costs including the authorized rate of return on investment) for the entire pool by adding together test period projected cost company revenue requirements, average schedule settlements, and settlements to incentive plan participants to produce the pool's total revenue requirement. As noted above, this is the essentially the same mechanism that NECA has used to develop rates since its inception, except that a portion of pool revenue requirements would be based on projected incentive settlements in addition to projected average schedule and cost settlements.

Dividing pool-wide projected revenue requirement by pool-wide demand would yield uniform rates for the pool. Since 1998, however, NECA has introduced "banded" access rates. The rate banding process groups companies with similar costs per unit of demand into separate rate categories. Companies within a band charge the same rates.

¹² An obvious example of this (although not an "incentive regulation plan" *per se*) is the mechanism used for average schedule companies, which receive pool settlements based on approved formulas that rely on units of demand (e.g., lines, minutes of use, route miles, etc.). The Commission itself has recognized the similarities between the average schedule mechanism and incentive regulation plans. See Policy and Rules Concerning Rates for

Rate banding allows low cost companies to remain in the pool and to continue to enjoy the benefits of risk sharing and centralized tariff administration, yet charge lower than average rates to their customers. Having large numbers of carriers continue to participate in the pool helps to stabilize monthly cash flows and pool earnings and avoids administrative burdens for the Commission and access customers associated with review of potentially hundreds of individual access tariffs.

Should the Commission adopt an incentive plan for rate of return companies that involves targeted access rates for pool members, NECA would simply apply existing rate banding methodologies to incentive plan companies based on incentive formula characteristics of each company. This approach would enable incentive companies to enjoy the administrative benefits of pooling while also seeing the benefit of their cost efficiencies in lower access rates. Because settlements and rates would be based on incentive settlement formulas, companies would have substantial incentives to keep costs low.

By adapting existing rate banding processes to an incentive regulation mechanism, the NECA pooling process can accommodate any of the various incentive regulation plans currently under consideration by the Commission. Most importantly, adapting existing pooling approaches to incentive regulation mechanisms avoids the need for carriers to leave the NECA pools in order to gain the benefits of moving to an incentive-based regulatory system. Since the Commission's goals for incentive regulation in this proceeding can be fully accomplished within the context of existing NECA pooling mechanisms, there is no reason why the Commission should force companies to give up

Dominant Carriers, CC Docket No. 87-313, *Second Report and Order*, 5 FCC Rcd 6786 at ¶ 277 (1990).

the benefits of pooling in order to introduce incentive regulation options to rate of return companies.

II. THE NECA POOLING PROCESS CAN ALSO ACCOMMODATE PRICING FLEXIBILITY.

In connection with pricing flexibility, the Commission asks for comment on the impact of pricing flexibility on the NECA pooling process and whether NECA would need to establish exception rates for qualifying ROR LECs.¹³ The Commission asks for comment on the resulting burden on NECA and whether there are any other ways of handling pricing flexibility within the pooling process that would be less burdensome.¹⁴ Finally, the Commission asks for comment on whether pricing flexibility in a pooling environment would offer any competitive opportunities to ROR carriers or be so burdensome on NECA that it would warrant requiring ROR carriers to leave the NECA pool as a condition of obtaining pricing flexibility.¹⁵

Existing pooling mechanism can easily be modified to encompass pricing flexibility proposals. As discussed above, rate banding in its current form permits NECA to establish differing rates for groups of companies with lower costs within the existing pooling process. As the Commission recognizes, however, rural companies often face special circumstances in responding to competitive pressures. These can occur, for example, when a rural company is heavily dependent on a single large customer in its area, or a few such customers, for substantial portions of its revenues. Thus, to the extent that existing rate banding methods fail to provide sufficient flexibility to meet individual

¹³ See FNPRM at ¶ 252.

¹⁴ *Id.*

¹⁵ *Id.*

competitive circumstances, NECA could modify its settlement and rate setting mechanisms on a more targeted basis to narrower groups of companies without encountering undue administrative burdens.

Such targeted rates could be applied regardless of whether the Commission adopts rules permitting geographic deaveraging of rates within a study area, term and volume discounts,¹⁶ or contract-based pricing. While filing and review of such rates for individual companies or groups of companies can be expected to impose some additional work for NECA and the Commission, the burdens associated with such filings using NECA's centralized tariff administration process can be expected to be far less than the burdens of filing and reviewing individual tariffs proposing flexible pricing arrangements.

Since existing NECA processes can accomplish needed pricing flexibility without imposing undue administrative burdens, there is again no reason for the Commission to require carriers to leave the NECA pools in order to gain the benefits associated with pricing flexibility.

III. THE COMMISSION SHOULD LEAVE EXISTING LONG TERM SUPPORT RULES IN PLACE PENDING FUTURE REVIEW.

The FNPRM tentatively concludes that LTS will be merged with the new ICLS mechanism as of July 1, 2003 and that after that time, participation in the NECA common line pool will no longer be required for receipt of LTS.¹⁷ In the Commission's view, LTS will no longer serve an independent purpose after the CCL charge is phased out. The

¹⁶ For example, NECA's Tariff F.C.C. No. 5, Sections 7.2.8 and 8.3, currently provide for term discounts based on the length of the service commitment period selected by the customer for High Capacity/ Synchronous Optical Channel Services and DSL Access Services, respectively.

¹⁷ See FNPRM at ¶ 272.

Commission also expresses concern that the current restriction of LTS to pooling carriers “hampers the competitiveness of incumbent LECs.”¹⁸

Rather than move immediately to merge LTS and ICLS support in 2003, the Commission should consider leaving existing rules in place pending review of the effects of access reform on rural carriers. As discussed below, there is a significant risk that merger of these two support funds in 2003 will weaken the NECA pooling process and impose unnecessary administrative burdens on both carriers and the Commission. Because lower-cost LECs have ample opportunity to file end user rates that more closely reflect costs, existing rules do not hamper the competitiveness of any NECA pool LECs. Leaving existing rules in place will therefore avoid risking harm to the NECA pooling process without creating adverse impacts on incumbent LECs or other parties.

As the FNPRM recognizes, the LTS mechanism was established in 1989 as a means of permitting smaller telephone companies participating in the NECA common line pool to continue charging reasonable carrier common line rates following the advent of voluntary common line pooling.¹⁹ By requiring exiting carriers to fund the difference between pool participants’ CCL revenue requirements and revenues received from the pool’s CCL charge, LTS assured reasonable comparability of interstate CCL rates between NECA pooling and non-NECA pool participants.²⁰

¹⁸ *Id.*

¹⁹ *See* MTS and WATS Market Structure and Amendment of Part 67 of the Commission’s Rules and Establishment of a Joint Board, CC Docket Nos. 78-72 and 80-286, *Report and Order*, 2 FCC Rcd 2953 (1987)(*NTS Recovery Order*).

²⁰ *Id.* at 2957-58.

In 1997, the Commission moved LTS support into the new universal service mechanism. The Commission's 1997 *Universal Service Order*²¹ included LTS with other forms of universal service support and modified the calculation methodology for LTS.²² The *Universal Service Order* further provided that LTS amounts be made "portable" on a per-line basis to eligible competitive local exchange carriers (CLECs).²³

In that proceeding, the Commission considered, but rejected proposals to make LTS available to non-pool participants.²⁴ Among other things, the Commission correctly recognized at the time that low-cost LECs that elect to leave the NECA pool do so because their costs are low enough to permit them to forego LTS support, and that providing such LECs with LTS would not further the goals of universal service.²⁵

Under the Commission's MAG Order, CCL charges are expected to be reduced substantially effective July 1, 2002 as higher End User Common Line charges are phased in. Beginning July 1, 2003, the CCL charge is to be eliminated entirely. Revenue

²¹ Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Report and Order*, 12 FCC Rcd 8776 (1997)(*Universal Service Order*).

²² See *Universal Service Order* at ¶ 751.

²³ *Id.*

²⁴ Federal-State Joint Board on Universal Service, Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge, CC Docket Nos. 96-45, 96-262, 94-1, 91-213, and 95-72, *Fourth Order on Reconsideration in CC Docket No. 96-45, Report and Order in CC Docket Nos. 96-45, 96-262, 94-1, 91-213, 95-72*, 13 FCC Rcd 5318 (1998)(*Fourth Recon. Order*).

²⁵ *Id.* The Commission also agreed with AT&T that competitive neutrality could also be achieved by withdrawing LTS from any CLECs operating in an exiting pool member's territory. *Id.* at 5363.

shortfalls resulting from reduction (and eventual elimination) of the CCL charge will be recovered instead through the new Interstate Common Line Support mechanism.

ICLS amounts will be computed by calculating the common line revenue requirement for each study area and then subtracting study area revenues obtained from end user common line charges, CCL charges (until eliminated), special access surcharges, certain non-analog line port costs, and any LTS amounts for which the carrier is eligible.²⁶ For carriers that elect to leave the NECA CL pool after October 11, 2001 (the date the MAG Order was adopted), ICLS will be calculated by subtracting any LTS amounts for which the carrier would have been eligible had it not ceased its participation in the pool.²⁷ Thus, higher-cost carriers continue to have a strong incentive to remain in the NECA CL pool under the rules as currently structured.

As the FNPRM points out, however, the principal rationale for providing LTS funding to NECA pool participants (*i.e.*, assuring nationwide comparability of NECA pool CCL rates) will no longer apply following elimination of the CCL charge. Nevertheless, carriers may continue to participate in the NECA CL pool for purposes of computing and filing end user common line charges, special access surcharges and non-analog line port costs. NECA CL pooling and settlement mechanisms will also continue to help maintain stable monthly common line revenue flows for small companies, pending revenue true-ups associated with the new ICLS mechanism.

Retaining the current LTS rules will help assure that pool participation remains at high levels, which, in turn, will avoid unnecessary administrative burdens and costs for

²⁶ 47 C.F.R. § 54.901(a).

²⁷ *Id.*

carriers and the Commission. By maintaining a broader base of companies within the pool, monthly revenue fluctuations from changing cost and revenue projections and intermediate true ups will be reduced for participating carriers. This will be particularly important in the first few years of the MAG Order implementation process, as rate of return carriers adjust to the extraordinary changes in universal service support and access charge mechanisms scheduled to take place in the next few years.

Maintaining current rules for LTS will not disadvantage carriers, as the FNPRM appears to conclude. As discussed above, for carriers that have relatively low common line costs, availability or non-availability of LTS is not likely to be a significant factor in reaching a decision as to whether to exit the pool. Moreover, NECA has recently introduced subscriber line charge rate banding,²⁸ and anticipates accommodating de-averaged SLC rates, as permitted under the Commission's revised rules.²⁹ These options would permit individual low-cost carriers to charge rates closer to their own costs while still remaining in the pool. Furthermore, the Commission's access charge rules have always permitted carriers to file individual EUCL tariffs yet remain in NECA's CL pool. Thus, low-cost companies continue to have multiple options to file competitive rates without revising rules on LTS eligibility.

For all the above reasons the Commission should not rush to conclude that existing LTS payments should automatically be merged with the new ICLS mechanism effective July 1, 2003. The Commission should instead leave section 54.901(a)(5) in its current

²⁸ See also National Exchange Carrier Association, Inc. Tariff F.C.C, No. 5, Transmittal No. 919, December 17, 2001, introducing rate banding for Multiline Business EUCL charges.

²⁹ See 47 C.F.R. § 69.104(r).

form, at least on an interim basis, pending longer-term review of the impacts of the MAG Order and other rule changes on rate of return carriers.

IV. CONCLUSION

The NECA pooling process can accommodate both incentive regulation and pricing flexibility for rate of return carriers in ways that fully satisfy the Commission's goals in this proceeding. Carriers that participate in incentive regulation plans within the context of the pool can retain the administrative benefits associated with pooling and retain incentives to reduce costs and improve productivity. NECA's existing rate setting and settlement processes can also handle pricing flexibility plans without undue cost. Consequently, there is no reason for the Commission to force rate of return companies to leave the pool in order to take advantage of these new regulatory options.

The Commission should leave existing rules governing LTS in place pending further study of the effects of regulatory change on carriers and the NECA pool. As discussed above, merging the LTS and ICLS support mechanisms has the potential to erode the benefits of pooling for many carriers. Leaving existing rules in place, in contrast, will not prevent individual companies from establishing cost-based end user common line

rates, or disadvantage carriers in any other way. Because the potential for harm outweighs any likely benefit, the Commission should maintain the *status quo* for the time being.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the Comments was served this 14th day of February 2002, by electronic delivery to the persons listed below.

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