

Toni Acton
Associate Director
Federal Regulatory

SBC Telecommunications, Inc.
1401 I Street, N.W.
Suite 400
Washington D.C. 20005
Phone 202 326-8843
Fax 202 408-4807



ORIGINAL

November 1, 2002

EX PARTE OR LATE FILED
RECEIVED

NOV - 1 2002

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street SW
Room TW A-325
Washington, DC 20554

Re: **Ex Parte**
CC Dockets 00-199, 96-45, 01-337, 02-33, 01-338, CS Docket 02-52 and
WC Dockets 02-313.02-269

Dear Ms. Dortch:

The attached material was distribution to FCC staff on Friday, November 1, 2002
Please enter it into the record of the above referenced proceedings.

Sincerely,

A handwritten signature in black ink, appearing to read "Toni R. Acton", written in a cursive style.

Toni R. Acton
Associate Director

Attachment

UARUC
Annual Convention
November 2002
Chicago, Illinois

COMMUNICATIONS ISSUES
BRIEFING BINDER



NARUC Issue Briefing

National Association of Regulatory Utility Commission&

Table of Contents

UNBUNDLED NETWORK ELEMENTS	2
BROADBAND	4
TENTH CIRCUIT REMAND OF THE UNIVERSAL SERVICE HIGH COST SUPPORT MECHANISM	8
REFORM OF THE FEDERAL UNIVERSAL SERVICE FUND CONTRIBUTION MECHANISM	10
ACCOUNTING REFORM	11

NARUC Issue Briefing

National Association of Regulatory Utility Commission&

Unbundled Network Elements

Background

On December 20, 2001, the FCC released a notice of proposed rulemaking commencing the first Triennial Review of its unbundled network elements (UNEs) policies and rules. The Notice initiates a comprehensive evaluation of the FCC's unbundling rules to determine whether its regulatory framework for UNEs, as well as its specific unbundling requirements, are consistent with the objectives of the Act. The Notice focuses in particular on the impact of the FCC's rules on facilities-based competition and deployment of advanced services. It seeks to draw on the lessons learned since the 1996 Act was passed, and to establish a more targeted approach to unbundling that identifies more precisely the needs of requesting carriers.

On May 13, the U.S. Supreme Court issued its long-awaited decision regarding the lawfulness of the TELRIC pricing methodology and of sections 315(c)-(f) of the FCC's rules, which address ILECs' obligations to perform the functions necessary to combine unbundled network elements. The United States Court of Appeals for the 8th Circuit had previously ruled that, although the 1996 Act did not preclude a UNE pricing methodology based on forward-looking, rather than historical, costs, TELRIC is unlawful insofar as it relies on the forward-looking costs of a *hypothetical* competitor, as opposed to the ILECs' own forward-looking costs. The 8th Circuit also invalidated sections 315(c)-(f) of the FCC's rules as being inconsistent with the 1996 Act. The Supreme Court reversed the 8th Circuit on both issues. In upholding the TELRIC methodology for calculating UNE prices, the Court found that the FCC did not act unreasonably or outside its discretion when it established the TELRIC methodology. The Court did not rule, however, that TELRIC is legally mandated by the Act, or even that it is the best possible pricing policy. In addition, in upholding sections 315(c)-(f) of the FCC's rules, the Court held that they apply only when a requesting carrier is: (1) "unable to make the combination," or (2) "unaware that it needs to combine certain elements to provide a telecommunications service." The Court also emphasized that although an ILEC must "perform the functions necessary to combine" elements, it is not necessarily required "to complete the actual combination."

On May 24, 2002, the United States Court of Appeals for the D.C. Circuit remanded the FCC's order establishing a national UNE list and vacated and remanded the FCC's line-sharing order. Among other things, the Court required the FCC to undertake an impairment analysis that was "more nuanced in light of the **social costs** of unbundling – specifically its negative effects on incentives to invest and innovate." The Court goes on to direct the FCC to consider the inter-modal competition provided to wireline broadband by cable modem providers.

Since the FCC is considering these issues in its Triennial UNE review docket, it solicited comments on the impact of this decision as part of that proceeding. On September 4, 2002, the Court stayed the mandate of its remand order until January 2, 2003, to provide the FCC time to conclude its Triennial Review proceeding.

Key Positions

3 The FCC should not unbundle new investment.

3 The FCC should not require ILECs to unbundle facilities for use in convergent competitive markets (e.g., advanced services, wireless and inter-exchange).

➤ The FCC should not unbundle elements that are being competitively deployed today. Switching in particular, should not be unbundled.

Rationale

➤ Facilities-based local exchange competition has become a reality since the 1996 Act.

➤ ILECs face competition from both CLECs and convergent technology platforms.

➤ Excessive unbundling inhibits facilities investment by ILECs as well as CLECs.

➤ The FCC must focus on what unbundling requirements are "necessary" and without which a CLEC would be "impaired."

➤ The current regulatory regime regarding UNE-P and pricing is unsustainable,

➤ UNE-P undermines telecom investment, impacting not only the carriers, but manufacturers as well.

NARUC Issue Briefing

National Association of Regulatory Utility Commissioners

Broadband

Background

The Federal Communications Commission (Commission) has initiated four different proceedings that will determine the regulatory framework for the nascent and intensely competitive broadband market. It is imperative that the Commission take decisive action to implement a uniform national broadband policy for all broadband providers, regardless of their technology or historical classification.

Regulatory Requirements for ILECs (Title II Proceeding)

On December 20, 2001, the Commission released a *Notice of Proposed Rulemaking* to examine how ILEC interstate broadband services should be regulated under Title II common carrier regulation. The Notice also seeks comment on SBC's petition to be declared non-dominant in its provision of broadband services. This proceeding is focused on whether the Commission should remove dominant carrier regulations (e.g. pricing and tariffing rules) that apply only to ILEC-provided broadband services.

Triennial UNE Review

On December 20, 2001, the Commission released a *Notice of Proposed Rulemaking* commencing its first Triennial Review of the Commission's unbundled network elements (UNEs) policies and rules. The Notice initiates a comprehensive evaluation of the Commission's unbundling rules to determine whether its regulatory framework for UNEs, as well as its specific unbundling requirements, are consistent with the objectives of the Act. An important issue in this proceeding is whether to extend unbundling requirements to new ILEC investment in broadband networks.

Framework for Broadband Access over Wireline Facilities (Title I Proceeding)

On February 15, 2002, the Commission released a *Notice of Proposed Rulemaking* to examine whether wireline telephone companies should continue to be required to offer the transmission component of their broadband Internet access services as a stand-alone telecommunications service. A key issue is whether wireline providers should have an obligation to open their networks to non-affiliated Internet Service Providers (ISPs).

Framework for Broadband Access over Cable (Cable Proceeding)

On March 15, 2002, the Commission released a *Declaratory Ruling and Notice of Proposed Rulemaking* in a proceeding that classified **cable modem service as an** interstate information service, with no separate telecommunications service offering. As in the Title I proceeding, a key issue in the Notice is whether cable providers should have an obligation to open their networks to non-affiliated ISPs.

Key Positions

D Title 11 Proceeding - ILECs should not be subject to dominant carrier regulation — including burdensome pricing and tariff requirements — in their provision of packetized broadband services. The broadband market is intensely competitive and the ILECs are not the dominant providers of broadband services in either the mass-market or the business segment of the market. Cable providers are the undisputed dominant providers of broadband Internet access services to the mass market. IXCs are the undisputed dominant providers of broadband packetized services, such as ATM, Frame Relay, and Ethernet, in the business market.

➤ Triennial *UNE* Review - Extending unbundling requirements to new ILEC investment in broadband networks would distort competition and inhibit investment in broadband deployment. The result would be less competition and consumer choice in the broadband market. As the DC Circuit recently confirmed and the Commission has repeatedly recognized, the broadband market is intensely competitive and ILECs are not the dominant providers. Therefore, a requesting carrier cannot demonstrate that it is impaired without access to the ILECs' unbundled broadband facilities. Moreover, billions of dollars of risky investment is needed to deploy high-speed packet capabilities in both the interoffice and local loop parts of the ILEC network. Unbundling requirements would greatly increase ILEC infrastructure and operational costs and limit return on investment, thereby impeding their ability to compete with dominant cable providers.

➤ Title 11 Proceeding - Wireline providers must have the same flexibility as the cable providers do in designing and packaging broadband services for consumers and structuring arrangements with ISPs. Currently, ILECs are required to perform "radical surgery" on their broadband Internet access services and create stand-alone telecommunications services. This outdated requirement, which was adopted twenty years ago in a "one wire world," constrains the ILECs' ability to compete in offering new and innovative broadband services. Similar to cable, ILECs should have the flexibility to structure and package their broadband services and enter into market-based commercial arrangements with ISPs. Under no circumstances should the secondary market participants (ILECs) be subject to more stringent regulation than the market leaders (cable).

➤ Cable Proceeding - As a legal and policy matter, the Commission must apply the same ISP access requirement to competing and functionally equivalent cable and ILEC broadband Internet access services. There are no technical barriers to providing multiple ISP access to cable networks and there are no relevant technical differences in providing multiple ISP access to cable and ILEC broadband networks. The only issue is one of policy and cost. If the Commission determines that the costs of mandating multiple ISP access to cable broadband networks outweigh the benefits, then it must reach the same conclusion with respect to ILEC broadband networks.

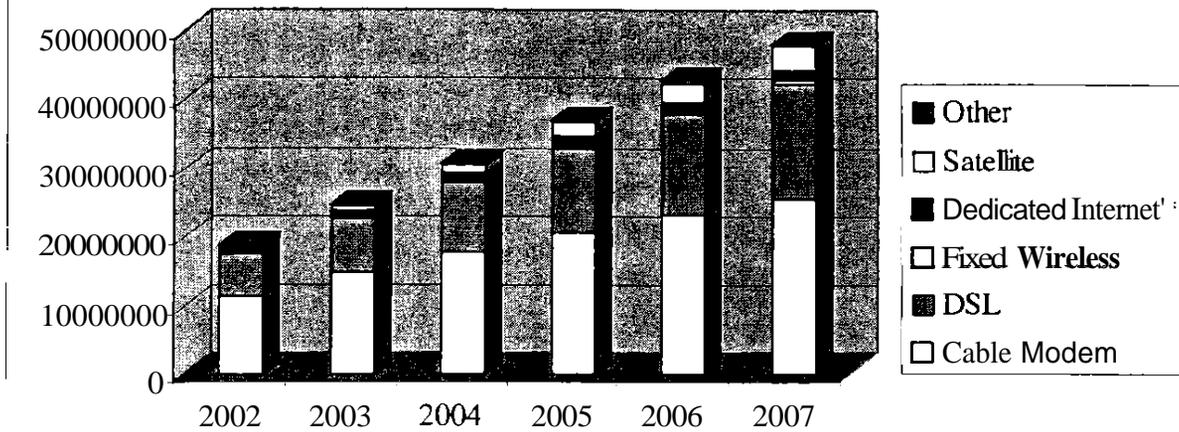
Rationale

➤ The broadband market is a highly competitive market with multiple broadband platforms and providers. DSL is being deployed to the mass market to provide a competitive alternative to cable modem services, which is wholly unregulated. The Commission has recognized that cable dominates this market and enjoys a 2:1 advantage over ILEC providers. Regulatory uncertainties are hampering ILECs' ability to compete with cable providers. The Commission should act quickly to establish a national broadband policy that removes the regulatory disparity between cable modem and DSL service and that removes the regulatory uncertainty that currently chills investment in and deployment of new broadband technologies.

Supporting Positions

"Throughout the brief history of the residential broadband business, cable modem service has been the most widely subscribed to technology, with industry analysts estimating that approximately 68% of residential broadband subscribers today use cable modem service. Analysts estimate that about 29% of residential broadband subscribers use DSL service. In the past year ... cable's lead over DSL has grown." (FCC's Cable Declaratory Ruling *and NPRM*, March 15, 2002, paragraph 9)

Overall Broadband Subscriber Segmentation



	2002	2003	2004	2005	2006	2007
Cable Modem	11,282,000	14,730,000	17,827,000	20,709,000	23,200,000	25,529,000
DSL	6,120,000	7,933,000	10,035,000	12,187,000	14,487,000	16,639,000
Fixed Wireless	69,230	110,475	212,129	345,020	480,181	623,390
Dedicated Internet*	990,000	1,090,000	1,160,000	1,210,000	1,260,000	1,310,000
Satellite	346,000	640,000	1,384,000	2,162,000	2,845,000	3,510,000
Other	181,000	220,000	270,000	338,000	415,000	480,000

Includes HDSL and HDSL2

With over 7 million consumer and 500,000 business subscribers at the end of 2001, cable modem will easily maintain its leadership as the most important broadband connectivity technology in the United States."

(2002 *Broadband Subscriber Forecast*, Yankee Group (August 2002))

NARUC Issue Briefing

National Association of Regulatory Utility Commissioners

Tenth Circuit Remand of the Universal Service High Cost Support Mechanism

Background

SBC provides service in many rural, high-cost areas but does not receive any high cost support from the federal fund. SBC must therefore support these high-cost areas with implicit subsidies derived from its profitable business customers. However, because competitors actively target SBC's profitable customers, these sources of implicit support are rapidly eroding.

Significant reform of the high-cost support mechanism is needed, and an opportunity for such reform was created by the Tenth Circuit's remand of the FCC's order establishing the high-cost support mechanism:

- In particular, the Court held that it was impossible to determine whether the FCC's model satisfied the requirements of the **1996** Act until the FCC divulged its comprehensive plan for implementing universal service.
- **As** part of this plan, the Court held that the FCC must induce state cooperation in implementing Section 254 of the **1996** Act.

Though the NPRM suggests - and some commenters agree - that the scope of the Court's remand is narrow, such a view ignores significant problems with the current high-cost support mechanism:

- The current system relies heavily on implicit subsidies as a primary source of support.
- The FCC has never addressed the statutory requirement that rates be "just, reasonable, and affordable".

On remand, the FCC ordered the Federal-State Joint Board on Universal Service (Joint Board) to issue a recommendation by August **15, 2002**. The Joint Board issued a Recommended Decision on October **22, 2002**. Pursuant to the **1996** Act, the FCC has one year to take action on the Recommended Decision.

Key Positions

- The scope of the Court's remand is extremely broad. It is not limited to merely providing clearer statutory definitions or providing better post-hoc justifications for an arbitrary benchmark. It requires the FCC to establish inducements for state cooperation to implement Section 254 of the 1996 Act.
- The FCC should initiate a comprehensive proceeding to reform the high-cost support mechanism.
- The FCC must end its reliance on eroding implicit subsidies as the primary source of universal service support. Though the FCC anticipated the erosion of *implicit* support as a necessary consequence of increased competition, no action has been taken to replace that support.
- SBC proposed a three-step approach to a *national* plan for reforming universal service. The FCC should:
 - Establish an affordability benchmark based on median household income.
 - Establish a universal service mechanism that provides funding for all areas where the forward-looking costs exceed the affordability benchmark.
 - Establish a transition plan that allows residential local rates to rise to levels that are self-supporting and affordable.
- Not only is the "affordability" of rates mandated by the 1996 Act, *it is also a required first step for determining the degree to which prices must be supported. Only when the FCC determines the degree to which prices must be supported can it determine the appropriate size of the fund.*

NARUC Issue Briefing

National Association of Regulatory Utility Commissioners

Reform of the Federal Universal Service Fund Contribution Mechanism

Background

In February 2002, the Commission released an NPRM seeking comment on the method by which USF obligations are assessed to carriers and subsequently recovered from end-users. The FCC was primarily concerned with two issues: 1) maintaining **the** stability of the funding mechanism in light of changing market conditions; and **2)** the degree to which the universal service line item surcharge varies from carrier-to-carrier. The FCC is scheduled to release an Order in the November 2002 timeframe.

Key Positions

SBC supports the assignment of universal service obligations on a per-connection basis. In a cooperative effort with BellSouth, SBC has proposed a method by which connections can be used as an equitable basis for assigning universal service contributions.

Should the FCC choose to adopt another per-connection proposal, the resultant methodology must satisfy the 1996 Act's requirement that every carrier that provides interstate telecommunications services shall contribute "on an equitable and non-discriminatory basis." SBC believes that:

3 Any reform proposal adopted by the FCC must treat **competing** services in a similar fashion, whether provided by wireline or wireless platform or whether the Commission regulates the carrier as a "dominant" or "non-dominant" carrier.

3 All policymakers must address the current asymmetrical application of universal service regulations to competing providers of broadband services.

NARUC Issue Briefing

National Association of Regulatory Utility Commissioners

Accounting Reform

Background

In the past year, the FCC has questioned whether there is an ongoing federal need to maintain its own existing detailed accounting rules. Several states, however, have opposed the reduction or elimination of the FCC rules. Subsequently, the difficulties at Enron, WorldCom and other companies have prompted the FCC to institute a moratorium on FCC accounting reforms. The Federal-State Joint Conference on Accounting Issues will provide an additional forum to examine what regulatory accounting data and related information is truly essential and reasonable, and which existing requirements are obsolete and unnecessarily burdensome or discriminatory. The FCC expects the Joint Conference to seek the cooperation of private sector representatives to assist in identifying appropriate improvements to the accounting rules. SBC welcomes the opportunity to work cooperatively with the Conferees.

Formerly distinct sectors of the communications industry are converging at an accelerated pace. Both federal and state regulators must reexamine the detailed accounting and reporting requirements that have been imposed on only one class of carriers -- the incumbent local phone companies.

In this new era, Generally Accepted Accounting Principles, (GAAP), is equally sufficient for all companies, assuming that it is not abused. The FCC's existing accounting rules could not have prevented the accounting irregularities that were identified recently. Neither the FCC's rules nor the changes being contemplated could detect or prevent such fraudulent behavior. These rules *serve* a different purpose, one that *is* obsolete under price caps -- cost-based rate setting.

Key Positions

3 In the still pending 2000 Biennial Review Phase 3 rulemaking (and now the 2002 Biennial Review), the FCC should eliminate its rules that restrict property records, depreciation, capitalization, working capital and materiality. The Part 32 listing of accounts could continue for a transition period of three years, as proposed in the Further Notice (FNPRM), in order to assist states that depend on the FCC structure. **After** the transition period, ILECs should only be required to follow the same accounting rules that IXC's, CLECs, wireless carriers and cable companies must *follow*.

➤ Certain technical problems included in the Phase 2 Order should be corrected. The new reporting of loop cable statistics, wholesale and retail sub-accounts and ARMIS broadband information should not be imposed.

Rationale

➤ The FCC should withdraw from the regulation of accounting practices. Rates are no longer set according to costs for carriers under price caps. Elimination of the accounting rules will have little, if any, direct impact on reported results. The FCC recognizes that "any unnecessary regulation places a corresponding unnecessary burden on carriers that are subject to it."

➤ In terms of the Phase 2 Order, loop cable statistics are not maintained by carriers and would be costly and difficult to obtain. The new sub-accounts for wholesale and retail costs require monthly procedures for data that is only required every few years, and which include costs that are not even considered in UNE pricing. The new broadband reporting requirements will inject additional asymmetrical regulation into a highly competitive market, which is dominated by companies that are not subject to these requirements.