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January 7, 2003

VIA ELECTRONIC FILING

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 Twelfth Street, SW
Washington, DC 20554

Re: UNE Triennial Review, CC Docket Nos. 01-338, 96-98, 98-147;
Notice of *Ex Parte* Contacts

Dear Ms. Dortch:

Today and yesterday I had *ex parte* meetings with Leonard Steinberg, General Counsel of Alaska Communications Systems Group, Inc., on behalf of its operating subsidiaries, ACS of Alaska, Inc., ACS of Anchorage, Inc., ACS of Fairbanks, Inc., and ACS of the Northland, Inc. (collectively "ACS"), concerning the above-captioned proceeding. Mr. Steinberg and I met with Christopher Libertelli of the Chairman's Office, Commissioner Abernathy and Matthew Brill, Commissioner Adelstein and Lisa Zaina, Commissioner Copps and Jordan Goldstein, and Commissioner Martin and Daniel Gonzalez.

The purpose of these meetings was to persuade the Commission to amend its rules in the above-mentioned dockets so that incumbent local exchange carriers ("ILECs") other than Bell operating companies are offered appropriate relief from unbundling requirements in markets where there are high levels of competition, such as Alaska. Amending the Commission's rules in this manner would allow the Commission to come into compliance with the D.C. Circuit's mandate in *USTA v. FCC* to refine the "impairment" standard, and would provide meaningful clarity concerning the point at which an ILEC's unbundling obligation under Section 251(c) ceases.[1] The enclosed materials, which further describe the competitive situation in Alaska, were distributed at these meetings. In addition, ACS distributed copies of its January 6, 2003 *ex*

[1] *See USTA v. FCC*, 290 F.3d 415 (D.C. Cir. 2002).

parte letter to the Commission, which was filed in the above-captioned dockets and is publicly available.

Please call me if you have any questions regarding this submission.

Respectfully submitted,

Karen Brinkmann

Enclosure

cc: Commissioner Abernathy
Commissioner Adelstein
Commissioner Copps
Commissioner Martin
Christopher Libertelli
Matthew Brill
Lisa Zaina
Jordan Goldstein
Daniel Gonzalez
William Maher

Interconnection Competition In Alaska
– *Local Telephone Services* –

Unintended Consequences of the
Telecommunications Act of 1996

January 2003

Summary

- No state is more dependent upon telecom than Alaska
  - Alaskan communities are distant and disconnected from each other and the rest of the nation
  - Telecommunications is essential for health, public safety, strategic defense, petroleum production, etc.
- Implementation of Telecom Act's competitive provisions threatens to bankrupt Alaska's largest LEC, ACS
  - 70% of State's population relies on ACS telecom network
  - ACS Serves key military installations and oil industry facilities
- State regulators have aggressively promoted competition --
  - *setting hypothetical UNE rates below embedded and actual FLEC costs*

  without regard to implications for high cost service areas
  - *terminating rural exemptions for almost 50% of the rural lines in the State, with all terminations occurring in ACS service areas*

Promotion of Competition

- Competitors lease ACS facilities at rates well below ACS' cost
  - In Fairbanks, GCI pays only $19.19 for a local loop that, on average, costs ACS in excess of $30
  - In Fairbanks and Juneau, GCI pays about $10 for conversion services that cost ACS about $35
- As "carrier of last resort," ACS is required to build facilities for use by GCI in Anchorage, Fairbanks, and Juneau -- yet between low UNE rates and GCI's likely deployment of cable telephony, ACS will likely never recover its investment
- Rural exemptions terminated in communities with fewer than 1,000 lines, average cost/line in excess of $50/month

Undue Economic Burden

- ACS has already cut costs dramatically but it cannot continue to provide service and cut costs sufficiently to make up for the loss of revenue
- ACS rate of return in Anchorage (excluding unregulated directory revenue) is less than 2 percent and declining
- Returns are insufficient to attract capital or even maintain historical levels of service
- High cost areas Fairbanks and Juneau, where rural exemptions were terminated, are even more at risk
- Regulators have required ACS to take twice as long to depreciate basic telephone cable as GCI takes

Undermining Telecom Act Goals

- Current trend will destroy viability of ACS -- result will not be competition, rather substitution of GCI as new monopoly provider
- Rather than recognize our competitive environment, our increased risk, our need to enhance innovation, regulators are extending, rather than shortening depreciation lives, exacerbating already poor business conditions
- Telecom Act, as currently implemented in Alaska, is not bringing consumers the promised benefits of innovative technologies and better services at lower prices
- Instead, implementation of the Act is wreaking havoc with Alaska's basic telecom infrastructure and universal service

Comparison

Lower 48 LECs and Alaskan LECs

Lower 48 LECs:

Company	Lines
Verizon	61,561,783
SBC Comm.	59,532,000
BellSouth	25,422,000
Qwest Comm.	17,787,000
Sprint	8,200,000
ALLTEL	2,612,325
Citizens	2,481,400
CenturyTel	1,797,643

Lines as of 12/31/01

Alaskan LECs:

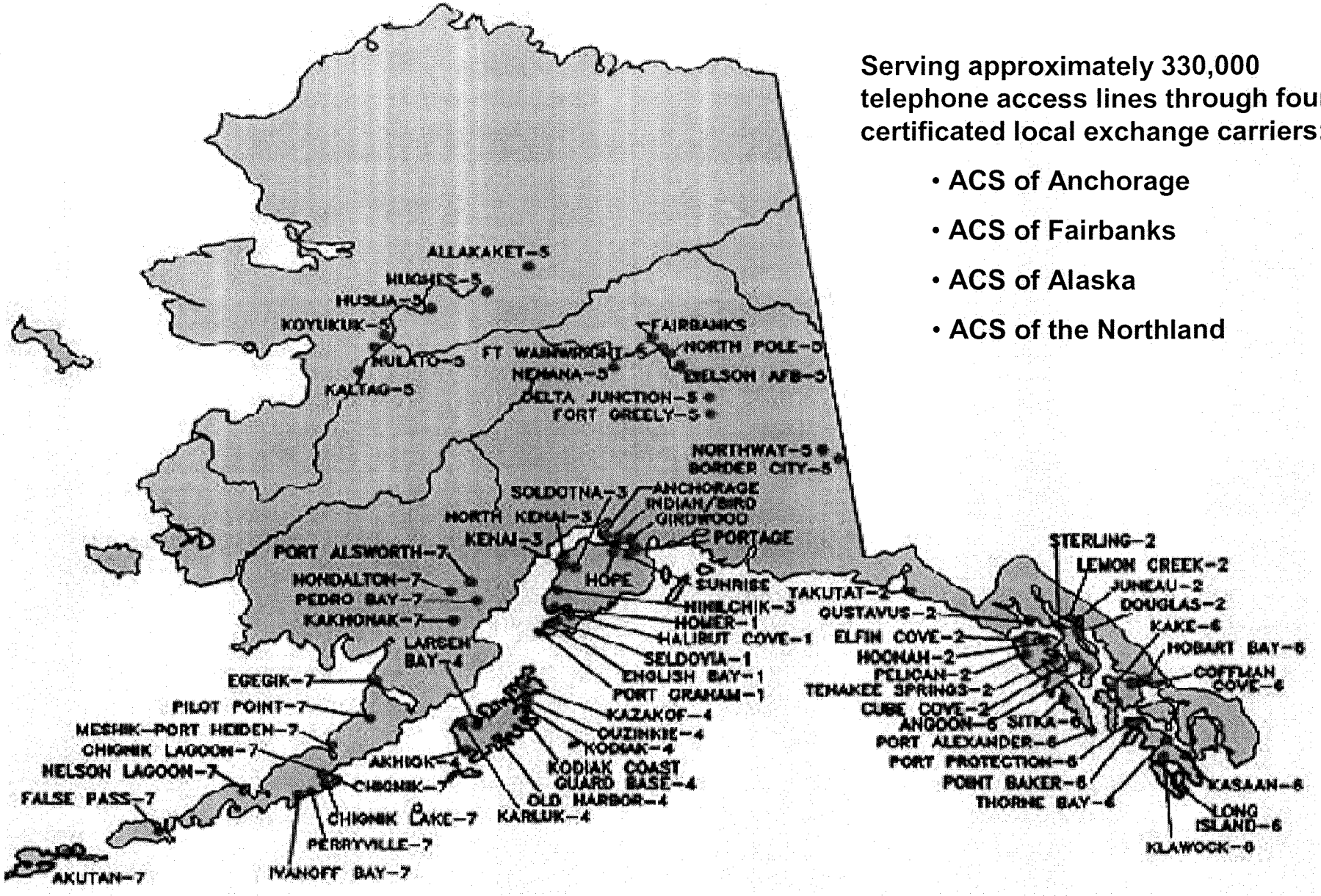
Company	Lines
ACS	332,923
MTA	65,335
TelAlaska	19,147
AP&T	13,137
Ketchikan	11,678
Copper Valley	6,819
United Company	6,580
Arctic Slope	5,657

Lines as of 12/31/01

Unique Alaskan Characteristics

- No Regional Bell Operating Company (RBOC) has ever provided local service in Alaska
- Verizon and SBC each serve approximately 1/3 of total lines in the U.S. – together, all of the ***RBOCs serve about 90% of U.S. lines***
- Alaska's largest LEC, ***ACS, serves fewer than 2/1000 of total U.S. lines***
  - Alaskan LECs lack economies of scale, operate in high-cost areas, and face unique service challenges in the state related to distances, geography, climate, etc.

ACS Serves 74 Alaskan Communities



Serving approximately 330,000 telephone access lines through four certificated local exchange carriers:

- ACS of Anchorage
- ACS of Fairbanks
- ACS of Alaska
- ACS of the Northland

ACS Local Telephone Markets

Anchorage
185,000 Lines

- Opened to competition in 1997
- ***Nation's most competitive market (50% market loss)***
- Competitive LECs are GCI and ATT Alascom

Fairbanks
45,000 Lines

- Designated "rural" under Telecom Act, receives USF
- Rural exemption terminated; competition commenced 2001
- ***Rapid market share loss (approximately 20% EOY 2002)***
- Competitive LEC is GCI (monopoly cable TV provider)

Juneau
30,000 Lines

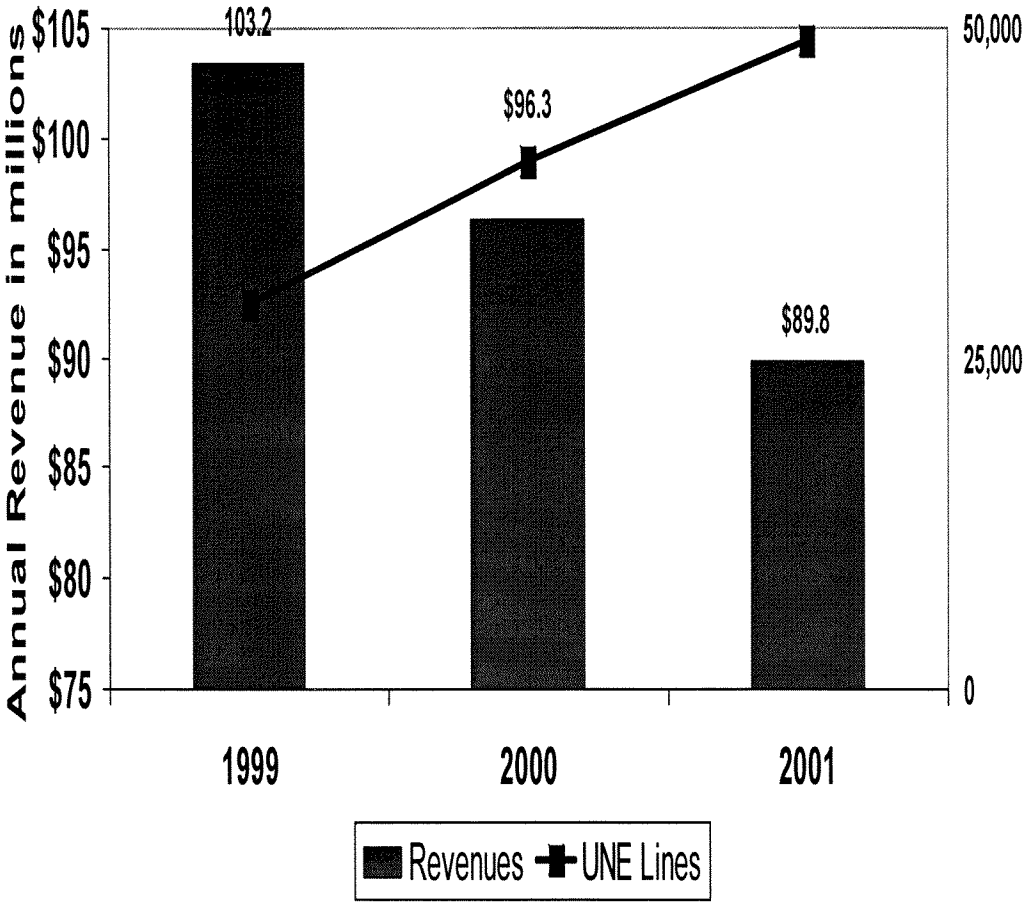
- Designated "rural" under Telecom Act, receives USF
- Rural exemption terminated; competition commenced 2002
- ***Rapid market share loss (approximately 10% EOY 2002)***
- Competitive LEC is GCI (monopoly cable TV provider)

"Northland"
70,000 Lines

- 70 high cost communities, requires significant USF support
- Rural exemption terminated for one of its two study areas
- ***Competition ordered in 2001, expected to roll out in 2003***

ACS of Anchorage

Revenues Have Declined as Competition Increased



Recent Competitive Line Losses:

Lines	6/30/02	Share
ACS Retail	101,901	50.0%
GCI UNE	57,361	28.2
GCI Wholesale	7,395	3.6
GCI Bypass(Est.)	24,171	11.9
ATT Wholesale	12,974	6.3
Total	**203,802**	**100%**

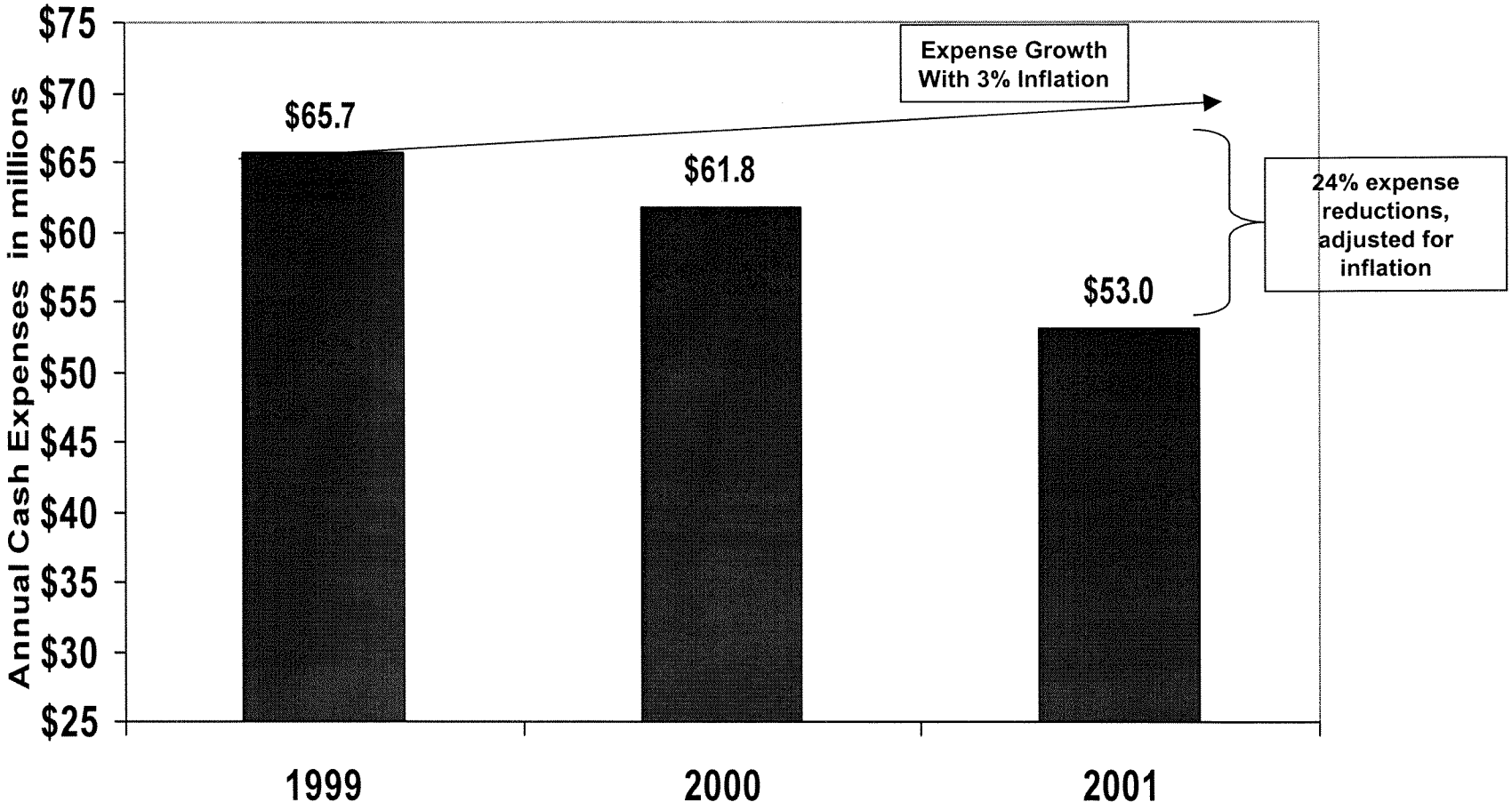
GCI Total 43.7%

Source: Annual Report to RCA – Regulated Revenues. GCI Bypass Lines estimated based on public filings.

UNE Line = Line that ACS leases to a competitor for a fixed monthly fee.

Wholesale Line = line that ACS resells to a competitor at a negotiated discount.

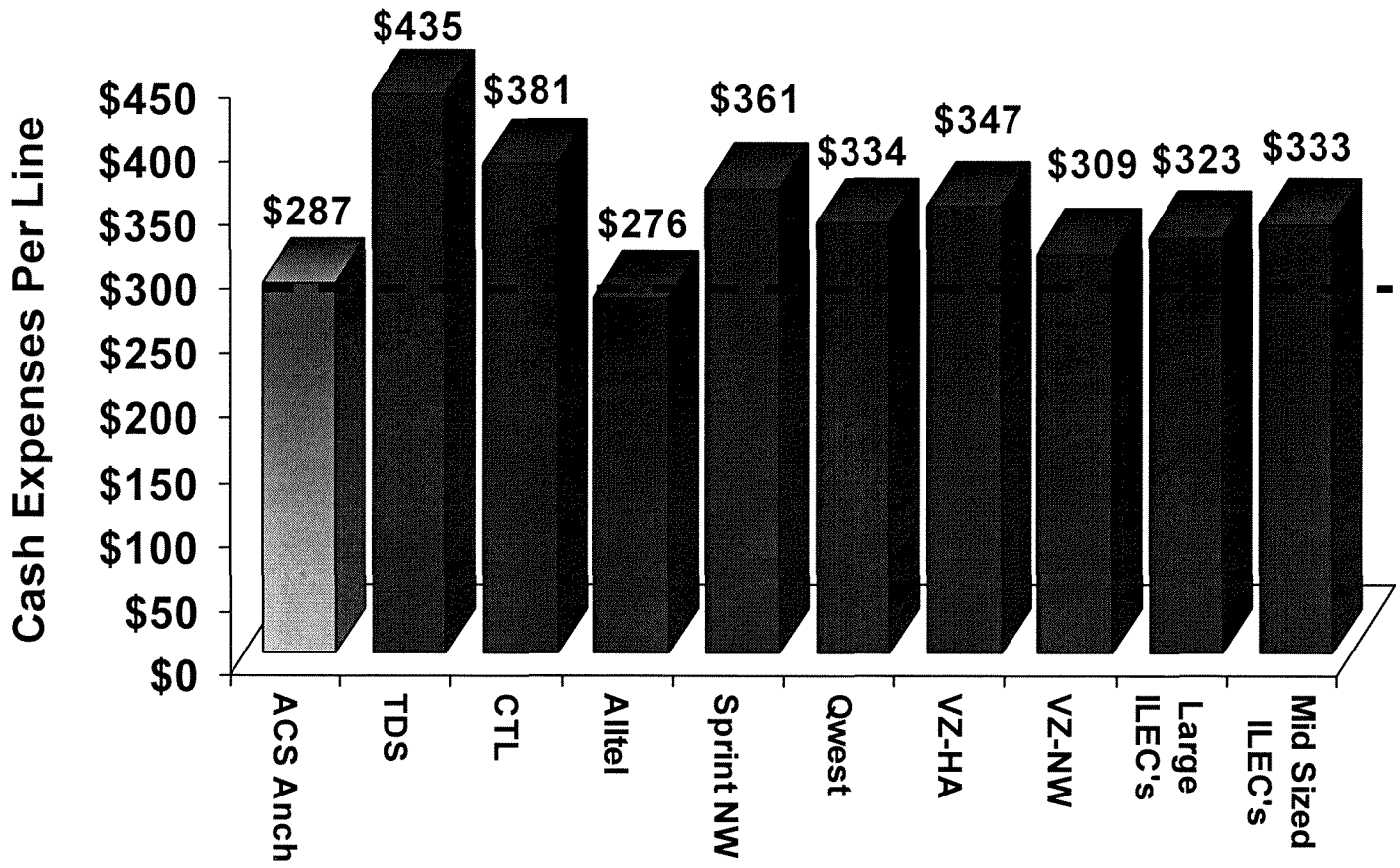
ACS Anchorage – Impact of Competition:
Reduced Costs and Increased Efficiency



ACS Anchorage is Very Efficient

Cash Expenses Per Line vs. Industry

2001

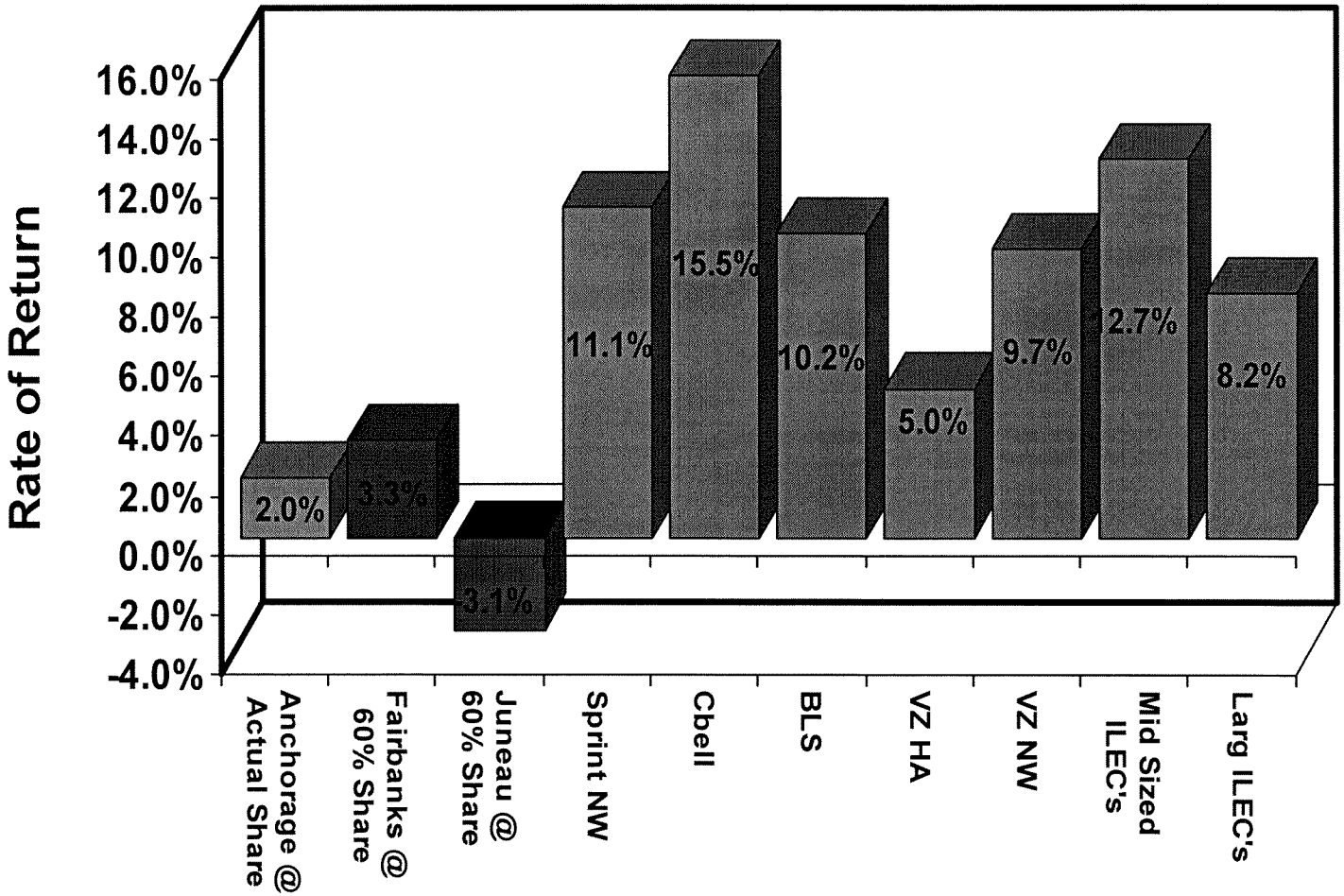


ACS Anchorage = 2001 Results. Industry = All reporting LEC's to FCC.
Source: Form M's, Company annual reports, "Statistics of Communications Common Carriers, 2000/2001 Edition", FCC

Comparison of Returns

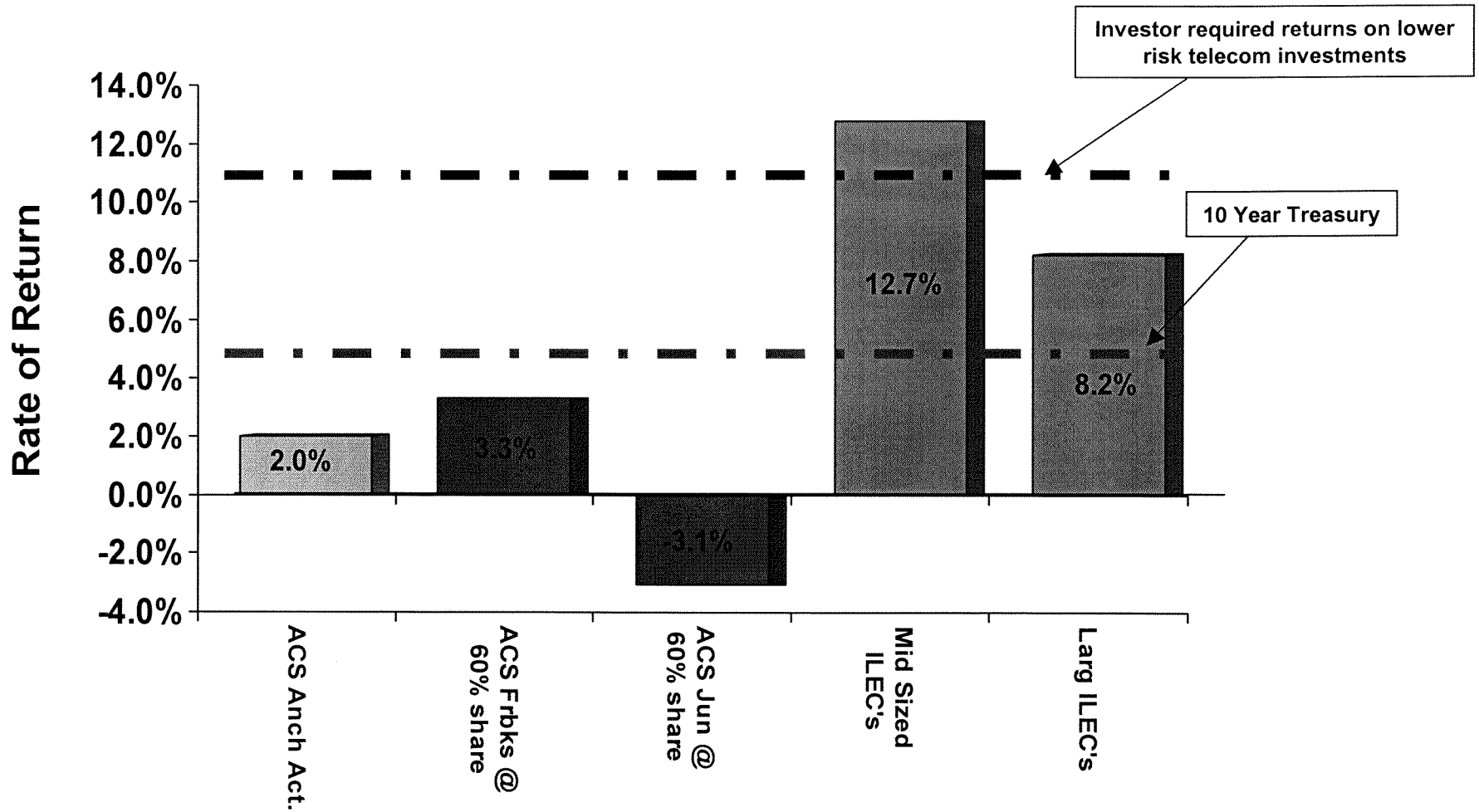
ACS Competitive Markets are Well Below The Industry

[Anchorage = actual market share; Fairbanks & Juneau = pro-forma @ 60% share]



Source: "Statistics of Communications Common Carriers, 2000/2001 Edition", FCC. Large ILEC's include Qwest, Ameritech, Pacbell. Mid Sized ILEC's include Sprint, Alltel, Citizens and Cincinnati Bell. Rate of return = net income/net plant.

ACS Returns Cannot Attract Capital to Fund Losses

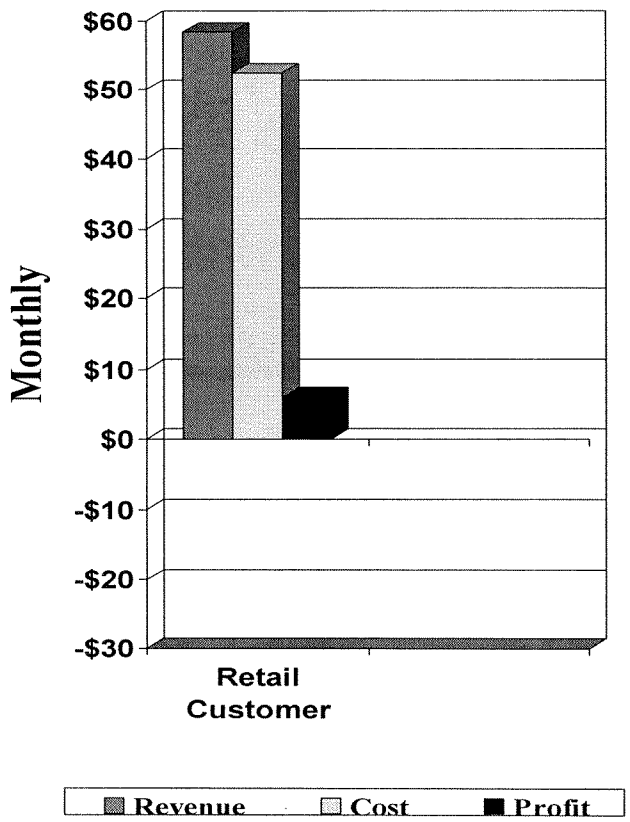


Source: "Statistics of Communications Common Carriers, 2000/2001 Edition", FCC. Large ILEC's include Qwest, Ameritech, Pacbell. Mid Sized ILEC's include Sprint, Alltel, Citizens and Cincinnati Bell. Rate of return = net income/net plant.

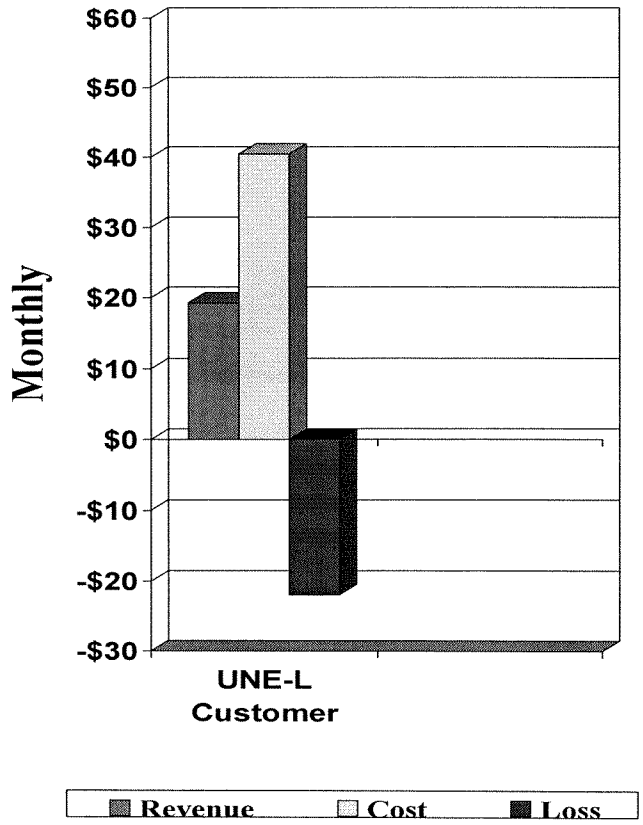
Economics of Interconnection Competition

UNE loop rate set by the regulators to facilitate interconnection competition is insufficient to permit the Company to recover its costs – as it must still build and maintain the network even for lines leased to competitor. Company loses money on every line it leases.

Economics of Serving One Retail Customer



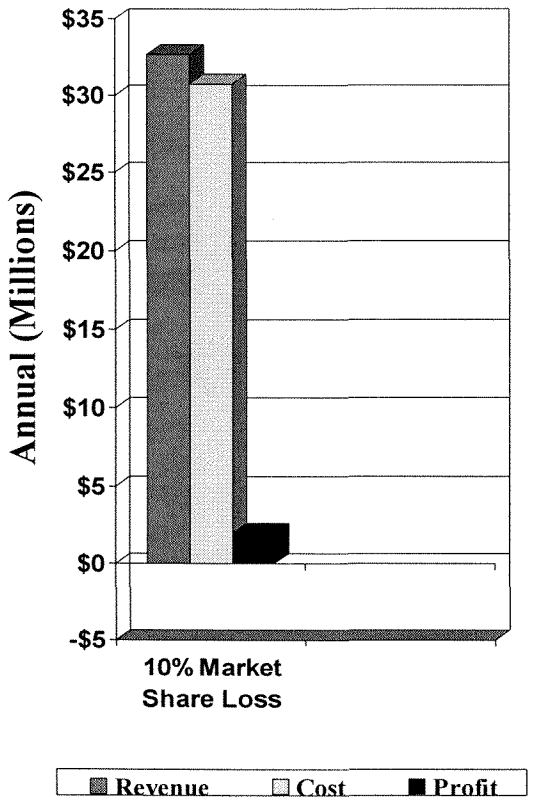
Economics of Leasing One UNE-Loop



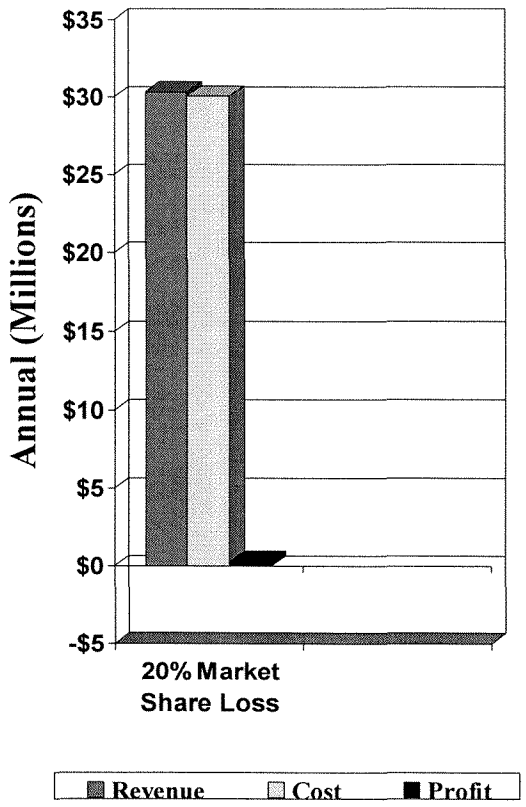
Situation Cannot Be Sustained

Revenues and expenses are out of balance as competitor gains market share by leasing UNE loops. At 20% market share loss, ACS earns negligible return on investment and generates no cash for building new facilities. At 40% market share loss, ACS is not viable.

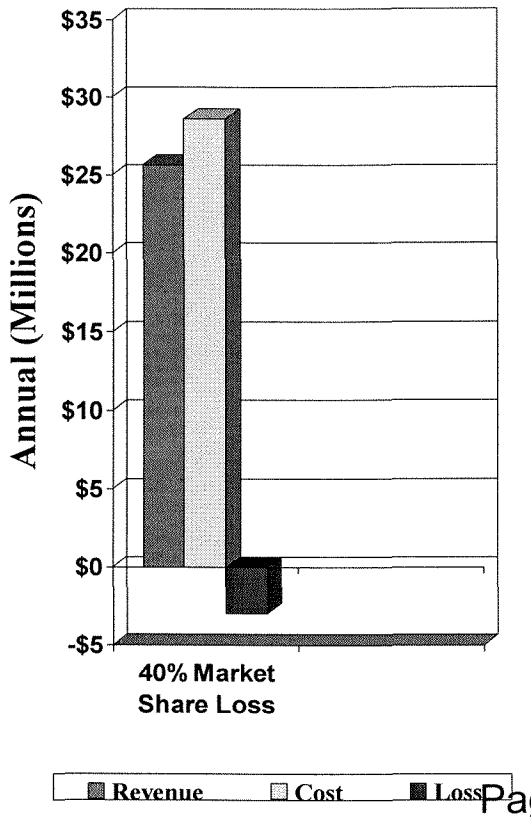
Assumes 10% Market Share Loss to UNE Loops



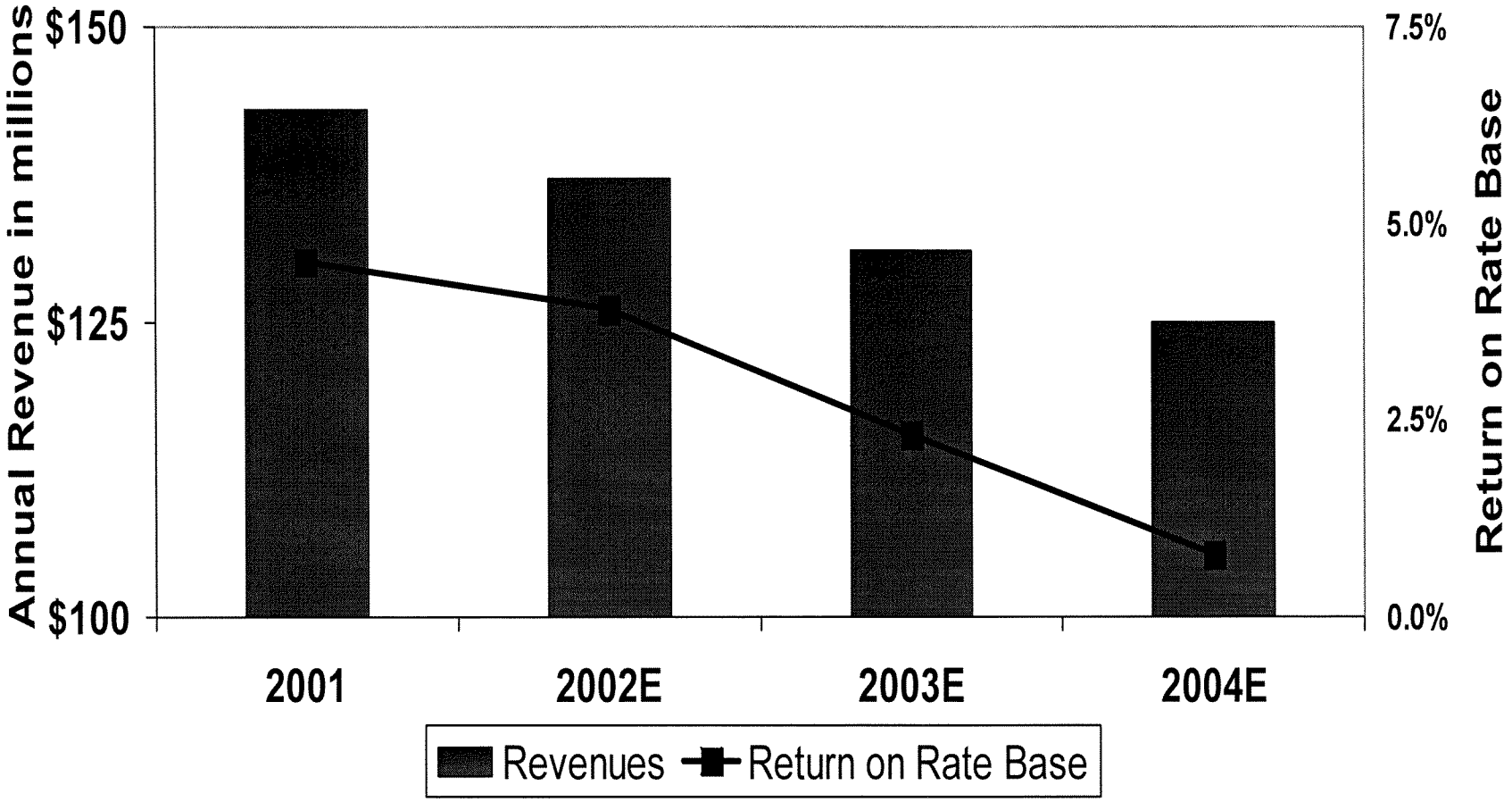
Assumes 20% Market Share Loss to UNE Loops



Assumes 40% Market Share Loss to UNE Loops

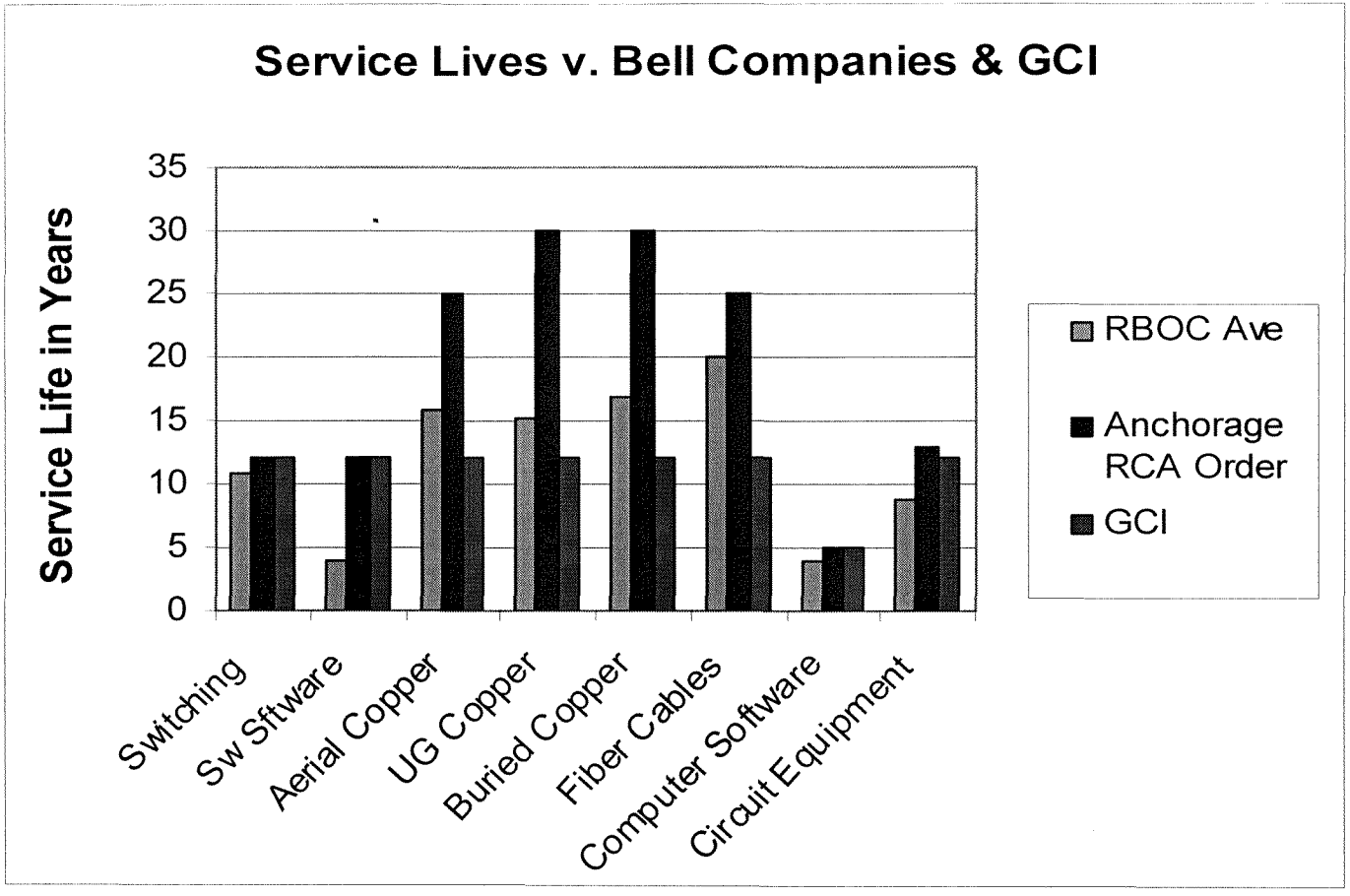


Total Competitive Markets are Experiencing Rapid Declines in Financial Returns



Above results are for ACS Anchorage, Fairbanks and Juneau markets.

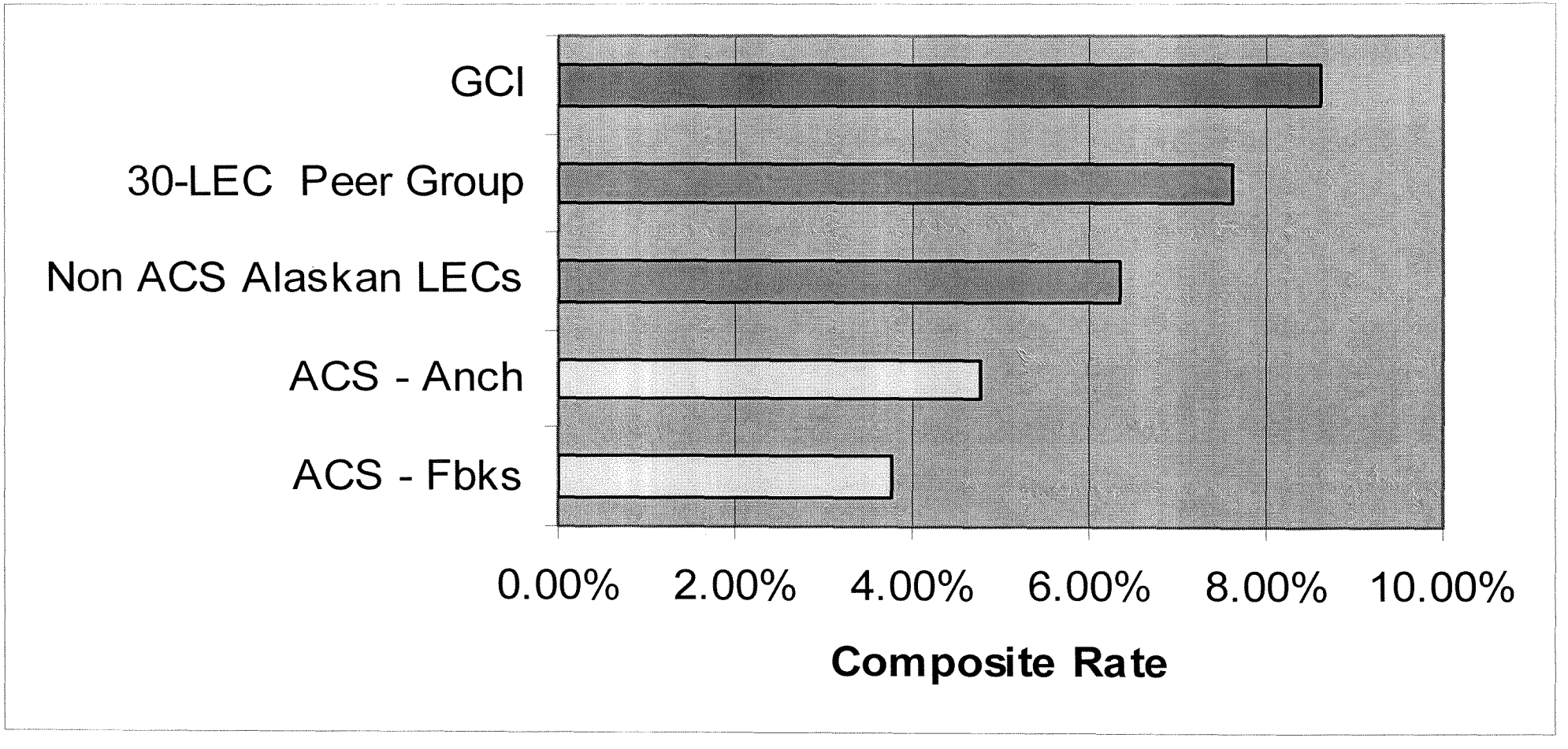
Depreciation - Service Lives



State Regulators Have Ordered ACS To Build Facilities For And Provide Services To CLECs, While Simultaneously Denying ACS The Revenue Necessary To Pay For These Facilities And Services

Industry Comparison

Composite Depreciation Rates



Revenue Impact

All Jurisdictions

Prior LEC Depreciation	$51,673,000
RCA Ordered Depreciation	$38,958,000
RCA-Ordered Reduction	<$12,715,000>

Reduction ordered by state commission will reduce rate base for purposes of establishing local service and access rate – and may also result in a retroactive requirement to refund

Proposed Solutions

- In light of the specific facts and circumstances of competition in Alaska, the FCC should find that UNEs are no longer necessary for, nor will their absence impair, significant competition in Alaska's competitive markets.
- ACS suggests the FCC adopt a mechanism that triggers relief from the UNE obligations. Triggers worth considering include: (1) consumer choice; (2) collocation in wire centers; (3) CLEC switching capacity; or (4) market share.
- Competitors that trigger relief can compete via their own facilities, resale, or facilities leased on a commercial basis.