

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

In the Matter of)

Review of the Commission's Rules)
Regarding the Pricing of Unbundled)
Network Elements and the Resale of)
Service by Incumbent Local Exchange)
Carriers)
_____)

WC Docket No. 03-173

COMMENTS OF SPRINT CORPORATION

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On behalf of its incumbent Local Exchange Carrier ("ILEC"), competitive LEC ("CLEC")/long distance, and wireless divisions, Sprint respectfully submits these comments in response to the Commission's Notice of Proposed Rulemaking (FCC 03-224) released in the above-captioned docket.¹

I. INTRODUCTION & SUMMARY

Sprint is unusual among American carriers. Its incumbent local exchange carrier operations provide unbundled network elements ("UNEs") and serve both urban and very rural areas. Its CLEC/long distance and wireless divisions are requesting carriers that are entitled under the Communications Act of 1934, as amended ("the Act"), to secure UNEs from ILECs. Sprint thus approaches the issues of this proceeding from the dual

¹ The Notice of Proposed Rulemaking ("NPRM") was released September 15, 2003, and a corresponding notice appeared in the Federal Register on October 17, 2003. 68 Fed. Reg. 59,757.

perspectives of a provider and a purchaser of UNEs. Sprint experiences the impact of the TELRIC² methodology and state pricing proceedings from both perspectives as well. Its positions necessarily reflect an internal calculus that recognizes the legitimate concerns of both ILECs and requesting carriers.

Sprint supports the TELRIC methodology, and believes no major changes to the methodology are appropriate or necessary. Criticisms of the TELRIC methodology are generally unjustified, and, in particular, the notion that TELRIC is “hypothetical” is mistaken. In Sprint’s experience, the state commissions, in implementing the TELRIC pricing methodology, are generally handling UNE pricing properly.

The NPRM observes that some parties -- principally the Bell Operating Companies (“BOCs”) -- have complained that state commissions’ TELRIC pricing procedures or results are out-of-line. If and where that can be demonstrated, affected parties have the ability to seek redress. BOCs especially are fully capable of defending their interests. Naturally, any pricing rules are bound to generate complaints from either or both sides of the UNE pricing issue. If they did not, that would be a sure signal that the rules were not being implemented properly.

II. BACKGROUND OF THE TELRIC METHODOLOGY

(A) Implementing the Act

Section 252(d)(1) of the Communications Act of 1934, as amended, directs that prices for UNEs must be “based on cost” and “may include a reasonable profit.” 47

² The Commission adopted the Total Element Long-Run Incremental Cost pricing methodology in Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, 11 FCC Rcd 15499 at ¶¶ 673-79 (1996) (subsequent history omitted) (“Local Competition Order”) (affirmed in relevant part by Verizon Comms., Inc. v. FCC, 535 U.S. 467 (2002) (“Verizon v. FCC”).

U.S.C. § 252(d)(1). To achieve this mandate, the FCC developed the TELRIC pricing methodology.

TELRIC takes all fixed and variable costs associated with providing a particular network element and spreads them over expected life of the element. It is designed to approximate the current reconstruction costs of a network in a competitive market. The methodology calculates cost of building and operating efficient facilities, as opposed to the cost of an existing facility at the time it was actually built. Local Competition Order ¶ 620; NPRM ¶ 2. The NPRM explains: “The Commission’s TELRIC pricing rules equate the incumbent LEC’s cost of providing network elements with the cost today of building a local network that can provide all the services its current network provides, using the least-cost, most-efficient technology currently available.” NPRM ¶ 17. The Commission added to this network design assumption an “additional constraint,” by requiring that “the new network must take as given the existing wire center locations.” Id., citing Local Competition Order ¶ 685. See 47 C.F.R. § 51.505(b)(1).

The Commission determined the methodology, but states regulators have responsibility for implementing TELRIC and ensuring UNEs are priced appropriately. In Sprint’s experience, state commissions have handled this responsibility competently and seriously. Hearings have been extensive, testimony and data generally have been appropriately thorough.

In fact, in light of maneuvering by BOCs to circumvent the Act and this Commission’s authority, in this proceeding, rather than issue and significant changes to or guidance on the TELRIC methodology, the Commission should instead reiterate where responsibility for pricing of UNEs falls. Consistent with the Act, the Commission

determines the pricing standard. The state commissions implement that standard. State legislatures have *no role*.

The Commission adopted the TELRIC model after developing and considering an extensive record. It evaluated, and rejected, all alternative cost standards. As recounted in the NPRM, the Commission found that basing UNE pricing on *embedded* or *historical costs* was inappropriate, because “it is forward looking costs, not historical costs, that are relevant in setting prices in competitive markets.”³ The Commission rejected use of reproduction costs for similar reasons. It rejected the efficient component pricing rule (or “ECPR”) methodology “because it relies on prevailing retail prices,” which are not cost based as required by the statute.⁴ It rejected the Ramsey pricing model, which allocates common costs among retail services in inverse proportion to the elasticity of demand, because UNE pricing would be highest for the elements that are most difficult to replicate, which would discourage entry by competitors, undermining the Act’s principal goal.⁵

TELRIC, in contrast, offered the best all-around model for establishing UNE pricing while maintaining efficient and realistic market entry and investment signals.

³ NPRM ¶ 33. The Supreme Court concluded, “the statutory language places a heavy presumption against any method resembling the traditional embedded-cost-of-service model.” Verizon v. FCC, 535 U.S. at 512.

⁴ NPRM ¶ 35. The Supreme Court also found this methodology unsuitable. Verizon v. FCC, 535 U.S. at 514.

⁵ NPRM ¶ 36. The Supreme Court upheld the Commission’s rejection of the Ramsey model, finding it “inconsistent with the Act” because it would deter entry by competitors and thus frustrate a key goal of the Act. Verizon v. FCC, 535 U.S. at 515-16.

(B) Upheld by the U.S. Supreme Court

The TELRIC methodology was ultimately reviewed by the United States Supreme Court in the Verizon case. The Court had already expressly upheld the Commission's authority under section 201(b) to establish a methodology to govern pricing for UNEs and interconnection, notwithstanding the Act's delegation of rate-setting authority to the states in section 252(c)(2).⁶ The Court examined the TELRIC methodology, considered the arguments of its legal and policy critics, and concluded – in a seven-to-one decision – that TELRIC is appropriate and consistent with the 1996 Act. It found the Commission's pricing rules “reasonable,” and observed that the BOCs' claim that TELRIC pricing of UNEs discourages investment “founders on fact,” given the considerable investment undertaken by incumbents and new entrants alike.⁷ The Court also denied the BOCs' constitutional challenge, noting that the BOCs had challenged the TELRIC methodology but not any specific TELRIC-based UNE rate.⁸

The Supreme Court's endorsement of the TELRIC model certainly sets a high hurdle for any argument that another standard would be more appropriate. Given the critical need for greater regulatory certainty for all carriers – ILECs and requesting carriers both – the Commission would do the industry and the public a disservice by entertaining any significant revisions to the UNE pricing methodology now. The NPRM

⁶ AT&T v. Iowa Utilities Bd., 525 U.S. 366, 378-85 (1999).

⁷ Verizon v. FCC, 535 U.S. at 516. The Court noted that the record showed CLEC investment of an extraordinary \$55 billion since 1996. It also observed that the BOCs' alternative pricing approach would compel competitors and consumers to pay for inefficiencies “caused by poor management ... or poor investment strategies.” Id. at 512.

⁸ Verizon v. FCC, 535 U.S. at 523.

volunteers that the Commission's interest in UNE pricing issues may be different now that "competition has taken root." NPRM ¶ 3. But in fact the competitive marketplace remains in its infancy, and the record does not establish a need for changes to the pricing methodology.

III. TELRIC IS A REASONABLE AND WELL-ESTABLISHED METHODOLOGY AND DOES NOT NEED SIGNIFICANT CHANGES.

(A) The TELRIC model is working fundamentally as it was intended.

The NPRM asks whether the TELRIC pricing methodology is working as intended and, in particular whether it is conducive to efficient investment in telecommunications facilities by ILECs and CLECs. NPRM 3. Sprint believes that, although no pricing model can be expected to be applied perfectly in every respect in all instances, overall it is serving reasonably well and is reasonably conducive to efficient facilities investment by ILECs and requesting carriers. States have been doing a generally fair and reasonable job in applying the model. Surely there is no reason to assume that another methodology could serve better, or that any significant adjustments are warranted.

The chief critics of the TELRIC model, of course, are the BOCs, and the NPRM suggests the Commission is unduly sensitive to their criticisms. Sprint believes the BOCs have failed to show that the TELRIC model is unreasonable. If the BOCs believe states are implementing the model improperly, the appropriate place for those concerns to be heard are in the state commissions and reviewing courts. If a BOC can show a state commission that its application of TELRIC is generating unrealistic rates, or can prove on appeal a that state commission has acted unreasonably, then the states are bound to make

adjustments or corrections to their application of TELRIC. But Sprint believes the BOCs have failed to show that state commissions are implementing it improperly, in any event.

(1) The BOCs have not demonstrated that ILECs are harmed by TELRIC.

The NPRM invites comment on whether ILECs are being harmed by TELRIC, as the BOCs have alleged. E.g., NPRM ¶ 5. Although the telecommunications industry remains in an unprecedented downturn, BellSouth, SBC, and Verizon nevertheless together have reported operating income of over \$19 billion for the first through third quarters of 2003, and net income of over \$15 billion.⁹ They remain highly profitable businesses; their financial health and ability to invest are surely not in question.

The BOCs have cited line losses and consequent erosion of retail revenues, and have suggested this is unnatural and the result of UNE-based competition enabled by TELRIC pricing. For its part, Sprint understands the pressures of competition. Its ILEC operations are seeing line loss despite considerable investment in plant and services, and it faces competition even in surprisingly rural markets. But ILEC line loss is to be expected, particularly in higher-density markets, as local exchange competition grows. It is the intended result – indeed the goal – of local competition.

The BOCs have less reason to complain than other ILECs. The BOCs have enjoyed rapid growth of market share in the in-region, interLATA long distance market, which has more than offset their loss of local lines. BellSouth, SBC, and Verizon have

⁹ Financial results are available at http://investor.verizon.com/news/VZ/2003-10-28_X332876.html; http://www.sbc.com/Investor/Financial/Earning_Info/docs/3Q_03_IB_FINAL.pdf; <http://www.bellsouth.com/investor/pdf/3q03p.pdf>.

gained nearly 31 million long distance lines, virtually overnight.¹⁰ Moreover, they have done so not by making any significant investment in long distance facilities but purely by leveraging their overwhelming dominance in the local exchange market and reselling services secured from other interexchange carriers. Their repeated complaints about “synthetic competition” enabled by TELRIC-priced UNEs are plainly hypocritical.

The 1996 Act conditioned BOC entry into the in-region, interLATA long distance market on their compliance with market-opening requirements. The BOCs relied heavily on competition from UNE-based CLECs to demonstrate the existence of meaningful facilities-based competition. Now that they have received the long distance prize, they are pressing harder than ever for “regulatory relief” from their market-opening obligations. Their opposition to TELRIC is part of this strategy, and their claims should be viewed with the utmost skepticism.

(2) The BOCs have not shown that TELRIC prices are below ILECs’ costs.

The NPRM invites comments on whether the TELRIC methodology results in UNE prices that are below actual ILEC costs. This is another claim repeatedly made, and never proven, by the BOCs. The BOCs have never produced any quantitative evidence that TELRIC prices are below costs. They provide the Commission with impressive comparisons of UNE rates to prior revenues. But revenues are not costs, which is why, for example, the Commission properly rejected the ECPR model. Similarly, the reductions in UNE switching rates that BOCs have cited in some states are not evidence

¹⁰ Verizon reports 15.9 million long distance lines in service (up 27% year-to-date); SBC 11.5 million (up nearly 50%); BellSouth 3.4 million (up more than 300%).
http://investor.verizon.com/news/VZ/2003-10-28_X332876.html at 1;
http://www.sbc.com/Investor/Financial/Earning_Info/docs/3Q_03_IB_FINAL.pdf at 7;
http://www.bellsouth.com/investor/pdf/3q03p_slides.pdf at 18.

that BOCs are not recovering their costs. Those states concluded that the evidence showed the BOCs previously had been over-compensated for those UNEs. If BOCs insist their costs are higher, they must prove their case. They have had many opportunities to do so, and as yet they have failed to do so.

It is also remarkable that no BOC has yet seen fit to enter another's territory on a widespread basis. If TELRIC pricing created such regulatory arbitrage for carriers, why are the BOCs not pursuing those opportunities? Clearly, their objective is protecting their overwhelming dominance of the local exchange and exchange access markets in their legacy Bell territories.

And again, even if one assumed that some states were setting UNE prices too low, that would not mean the TELRIC methodology is unsound. As Sprint explains in Section IV below, it means only that the inputs were incorrect. The BOCs can present their case before the state commissions and, if necessary, on appeal to the courts.

(3) The BOCs have not shown that TELRIC discourages investment.

The NPRM asks whether TELRIC as applied distorts economic signals and thus discourages ILEC or CLEC investment. NPRM ¶ 5. Sprint has seen no evidence that would support that conclusion. The BOCs have asserted that TELRIC pricing discourages investment, ostensibly by denying ILECs recovery of their costs and by providing CLECs artificially cheap access to ILEC facilities. But no BOC has proven that TELRIC has distorted economic incentives.

The BOCs have pointed to decline in telecommunications investment, but that decline is the result of other factors. They include, principally, an economic downturn that has had particular impact on the telecommunications industry, a particularly severe

downturn in the CLEC industry, and the burst of the Internet bubble. Sprint also disputes the notion that existing levels of investment are unhealthy. The BOCs, in particular, continue to invest heavily. Verizon, for example, announced last summer plans to undertake a massive \$20-40 billion investment in speculative local capacity in its own territory.¹¹ Verizon made this announcement even before the Triennial Review Order¹² was released, which the Commission intended to provide yet further incentives for ILEC investment. SBC and BellSouth have also been investing aggressively in network upgrades notwithstanding the current economic downturn.

BOC claims that CLEC investment has been discouraged by TELRIC are also entirely mistaken. Despite an extraordinary downturn in the CLEC industry that has driven dozens into bankruptcy, CLEC investment continues to grow, albeit not at the heady pace of the late 1990s. TELRIC did not discourage CLEC investment. In fact, the CLEC industry's past troubles may well have stemmed largely from *overinvestment* in facilities, when many CLECs simply lacked the customer base needed to support that investment. As intended by the Act, the pro-competitive policies of the Commission – of which the TELRIC pricing methodology is key – allow CLECs to use UNEs to build a customer base sufficient to justify and support further investment in their own facilities over time. The TELRIC methodology promotes efficient entry and investment for all competitors, and is more important to promote investment than ever before.

¹¹ “Verizon’s Gutsy Bet,” BusinessWeek (Aug. 4, 2003) at 52.

¹² Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 01-338, FCC 03-36 (rel. Aug. 21, 2003) (“Triennial Review Order”).

IV. TELRIC is not hypothetical or unrealistic.

(A) The notion that TELRIC is “hypothetical” is mistaken.

The NPRM opines that “part of the difficulty that states and interested parties have encountered” with TELRIC pricing issues “springs from the excessively hypothetical nature of the TELRIC inquiry.” NPRM ¶ 7. With all due respect, Sprint believes the suggestion that TELRIC is excessively hypothetical is mistaken. The Commission properly determined that only a forward-looking approach is suitable, as it best reflects efficient market entry and investment signals. Properly applied, the TELRIC model is a reasonable and realistic way to examine forward-looking costs – whether of network construction or of carrier business plans.

Naturally, any forward-looking cost model is to a degree hypothetical, and appropriately so. Business plans are forward looking and “hypothetical,” too. But the TELRIC methodology, as generally applied, is grounded in actual networks and actual network design. For example, Sprint’s cost studies reflect not merely the actual location of ILEC wire centers, but also real-world customer locations; real-world wire center boundaries; real-world cable routing along actual streets and over actual terrain, topography, and obstacles; real-world but state-of-the-art network design; real-world construction costs in the relevant market; and real-world vendor costs. Cost studies prepared by ILECs and other interested parties, and evaluated by the state commissions, moreover, are not works of fiction – or are not supposed to be. Indeed, the notion pressed by some parties that commissions should not look at *actual* data because TELRIC envisions a hypothetically efficient network is also untrue. The use of pertinent,

documented, current data is fully consistent with TELRIC and yields the fairest and most efficient possible results.

Thus, contrary to the NPRM's statement, a TELRIC proceeding is not a "black box." NPRM ¶ 7. In Sprint's view, state commissions do not exercise unduly "wide latitude," and any errors or abuse of their discretion are subject to review or appeal. Sprint does not believe there has been a "lack of predictability in UNE rates" that would not arise inevitably from any UNE pricing regime. Id. The BOCs' objections arise principally from their underlying opposition to the very concept of local competition.

Sprint also disputes the NPRM's stated assumption that, without "more specific guidance," TELRIC makes "network modeling opaque and make[s] it difficult to understand how actual UNE rates are derived." NPRM ¶ 7. Carriers have fashioned realistic TELRIC cost models which, though necessarily detailed and complex, provide transparency, and realism, to a remarkable depth. For its part, Sprint has devoted significant effort and resources to develop and prove realistic cost models. They may be complex, but they are transparent: you can trace the inputs through to the result. In contrast, relying on embedded costs, as the BOCs have long advocated, would necessarily give the BOCs (who alone know what embedded facilities they have) control over costing models and thus would make the pricing process opaque.

The NPRM notes that assuming simultaneously a market inhabited by multiple competitors and one with a ubiquitous carrier with a very large market share might work to reduce estimates of forward looking costs below the costs that would actually be found even in an extremely competitive market. NPRM ¶ 49. Sprint disagrees. The TELRIC model, with proper inputs, reflects the reality of ubiquitous plant installed by ILECs

capable of serving all customers and the substantial market share enjoyed by ILECs. The Commission's concern here may be applicable to true greenfield settings, as it concluded with fiber-to-the-home loops in the Triennial Review Order.¹³ Otherwise, this is not a problem (or not yet a problem), because competitors generally still have too small a market share.

(B) BOC proposals to simplify pricing methodology would lead to unrealistic results.

Sprint recognizes that state TELRIC pricing proceedings have indeed been “complicated and time-consuming.” NPRM ¶ 7. Such proceedings, however, are necessitated by the Act's requirement that UNEs be “based on cost” – as well as its instruction that pricing for UNEs “may include a reasonable profit.” 47 U.S.C. § 252(d)(1). Determining UNE pricing is not a simple task. It is inevitably complicated and detailed, and if it were not then the process would not be handled responsibly. Doubtless, if the process were simplified, many of the same critics would then be arguing that streamlining now was yielding unfair results.

Simplifying the process would not improve it. Use of samples, as proposed by BOCs and noted in the NPRM, is ill-advised and unreliable. Realistically, no one could validate the BOC samples. Though the NPRM suggests discovery might be a means of checking data (NPRM ¶ 60), it would plainly be insufficient. Samples would shift control of the pricing process from state commissions to the BOCs, by giving them an overwhelming advantage in cost proceedings as monopolists of the model. Other parties would be unable to check or validate their results.

¹³ Triennial Review Order ¶ 273.

In addition to compromising the integrity of the pricing process, “simplification” efforts would disrupt or even throw out years of work spent developing solid cost models. Sprint has invested substantial resources over six or seven years developing proven cost models for its ILEC operations in eighteen states, using detailed real-world data. Sprint does not appreciate the suggestion that all that work should be made obsolete, at the lobbying of the BOCs, for a new regime that inevitably would be much less accurate and that can and doubtless will be readily challenged as a result.

Simplification efforts would also be inconsistent with the Commission’s approach to Universal Service costing. As the NPRM notes, the TELRIC model was applied to nonrural companies for USF. NPRM ¶¶ 45-48. In the Universal Service proceeding, the Commission concluded that funding should be based on the forward-looking cost of providing universal service.¹⁴ The fact that universal service support was calculated using nationwide inputs (NPRM ¶ 46) does not make a more detailed application of the TELRIC methodology somehow less appropriate for UNE pricing. And if the TELRIC methodology were inherently unreasonable or prone to generating inaccurate results, it would do so when applied to universal service pricing, too. The fact that carriers – and all BOCs – have been content with the use of TELRIC as a universal service pricing methodology shows that their criticisms of the methodology for UNE pricing should be dismissed as self-serving.

¹⁴ Federal-State Joint Board on Universal Service, CC Docket No. 96-45, First Report and Order, 12 FCC Rcd 8776 at ¶¶ 199, 223-226, 232, 251 (1997) (subsequent history omitted).

(C) TELRIC requires looking at company-specific costs.

An important reason why the UNE pricing process must inevitably be complex – and cannot realistically be “simplified” – is the fact that TELRIC requires examination of company-specific costs. Clearly, one carrier’s costs will vary significantly from another’s. Smaller carriers, for example, have higher costs than larger ones. Smaller size generally means higher costs of capital, higher procurement costs from suppliers, and higher construction and operating costs per-line. Likewise, rural carriers have higher costs than urban ones. Rural carriers have fewer alternatives for contract work, which leads to higher costs. Lower customer density and noncontiguous service territories mean substantially higher costs per-line. Carriers with fewer lines also have higher administrative costs per-line.

Some parties have argued that the application of TELRIC for UNE pricing would be simplified by rejecting use of actual data. In effect, while the BOCs argue that TELRIC is too hypothetical, some others contend that TELRIC as applied is not hypothetical enough. Yet the notion that UNE pricing should not, or even need not, look at real data because it is a hypothetically efficient network is untrue. Again, the Act’s requirement that UNE pricing be based on “costs” necessitates an examination of actual cost data. It is in the consideration of network design that TELRIC takes on an appropriately limited “hypothetical” character. Under TELRIC, network design is determined not by how an ILEC actually constructed its network, but instead by considering how a single efficient carrier would build to serve all customer locations within a particular geographic area today, taking existing wire centers into account. In determining the costs of that network, real-world cost data is *essential* to determine

realistic forward-looking costs. That is why Sprint has gone to such efforts to reflect honest, real-world attributes in its cost studies, as shown in Section IV(A), above.

(D) If states make errors in applying the TELRIC methodology, aggrieved parties have avenues for redress.

As Sprint has noted previously in these comments, any problems with TELRIC pricing of UNEs arise not from the model, but from the inputs applied. Complaints should focus on those inputs and not on the model. Any party can challenge a state commission if it thinks unreasonable inputs have been applied or have generated an unreasonable result. If, for example, a BOC believes the state commission has applied unreasonable inputs to the TELRIC model, it can and should present its case before that commission. If it remains dissatisfied, it may appeal the matter to the courts. As this Commission can readily acknowledge, the BOCs are certainly capable of protecting their interests in court. But an aggrieved party must do more than complain; it must prove its case.

Thus, the Commission should resist the pressures from the BOCs – and any party – to modify the pricing methodology or introduce itself any more than absolutely necessary in the conduct of state pricing proceedings. The rules should not be rewritten, or adjusted, or clarified, just because the BOCs argue that they have been mistreated in some state proceedings. It should be enough for the Commission to remind all states to follow the rules that have already been adopted.

V. THE COMMISSION NEED NOT ISSUE A DETAILED ORDER IN THIS PROCEEDING.

(A) A detailed order is unnecessary and would be counterproductive.

A detailed order in this proceeding is both unnecessary and would be counterproductive. The Commission has already provided clarification to the states on cost of capital, and has given additional guidelines on depreciation.¹⁵ These are among the most important inputs relevant to investment incentives. Thus, the industry, the states, and the public do not need the Commission to write a detailed order on TELRIC pricing matters. The key to sound pricing is working within the rules and methodology already established. Where there are problems, those can be addressed at the states without further federal direction.

(B) Other Specific Issues

(1) Cost of capital (NPRM ¶¶ 82-91)

The NPRM invites comments on any guidance that may be provided on the issue of cost of capital. Clearly, cost of capital is an important issue, because TELRIC is based on forward-looking cost of capital applied to current costs for the model network. But no rewrite of the TELRIC model, or further clarification, is necessary.

The Commission has already addressed this issue. The Triennial Review Order “made clear that, in establishing a TELRIC-based cost of capital, the state commission must reflect the risk of participating in a market with facilities-based competition.”¹⁶

Whether the cost of capital applied by individual states is too low, as ILECs contend, is

¹⁵ Triennial Review Order ¶¶ 668-691.

¹⁶ Triennial Review Order ¶ 680.

not a question the Commission need address. With the issue returned to the states for re-examination, it is unnecessary for the Commission to comment further.

(2) Depreciation (NPRM ¶¶ 92-108)

The NPRM asks whether depreciation rates are unrealistic, and whether changes should be made. NPRM ¶¶ 92-108. The Commission similarly has already provided further guidance on the depreciation issue. The Triennial Review Order sensibly “declined to mandate a particular set of asset lives,” but “clarif[ied] that it is appropriate for state commissions to employ accelerated depreciation in order to reflect accurately the anticipated decline in the value of assets in a competitive market.”¹⁷ The Commission encouraged states to shorten asset lives for depreciation, because new generation equipment may be pushing older assets into obsolescence faster than traditional depreciation allowances reflect. States will be pursuing that issue now.

However, Sprint opposes the NPRM’s proposal to front-load depreciation in the early years of equipment life. This course would add needless complexity, could invite gamesmanship, and would depart sharply from the long-standing industry standard of straight-line depreciation in the utility ratemaking process.¹⁸ It would also be unfair to requesting carriers that purchase in the front years, because a double-declining balance would force them to overpay for use of the asset. The Commission should adhere to the Triennial Review Order’s guidance. It should stick with straight-line depreciation and reject other accelerated depreciation methods.

¹⁷ Triennial Review Order ¶ 690.

¹⁸ The straight-line method is almost universally used in the utility rate making process.” National Association of Regulatory Utility Commissions, Public Utility Depreciation Practices (1996) at 61 (noting also that non-straight-line “accelerated methods ... are not generally used for regulatory purposes”).

(3) Network routing, construction, and technology (NPRM ¶¶ 63-70)

The NPRM invites comments on its tentative conclusion that prices should reflect “real-world attributes of the routing and topography of an incumbent LEC’s network.” NPRM ¶ 63. Sprint disputes the notion that the “real world” is drastically different from the network routing assumptions adopted by the state commissions. Cable-routing, in particular, is a non-issue. Proxy models are not divorced from reality. Sprint’s model relies not merely on actual wire center locations, but also on careful considerations of actual wire center boundaries, actual rights of way, actual building locations, actual topography and geographic obstacles, actual vendor costs, actual state-of-the-art network design, and actual in-market construction costs. Thus it reasonably reflects actual topography, routing, and efficiency, even though existing network plant, as built over time, routinely takes more round-about and inefficient routes. This level of detail provides a higher measure of reliability, and is not unreasonable or burdensome. There is no need for the Commission to “adopt routing assumptions more closely tied to an incumbent LEC’s existing network.” NPRM ¶ 64.

Sprint’s model also uses efficient network design and technology. NPRM ¶¶ 67-70. Like all ILEC networks, Sprint’s existing plant naturally does not completely reflect the most efficient design or technology possibilities available today, because it was constructed over many years. But Sprint’s model yields reasonable results based on the assumptions adopted by the Commission, utilizing today’s standards of efficient design and technology. Other parties’ models do likewise. Proxy models are not hypothetical or unrealistic.

(4) Vendor cost, fill factors, and structure sharing (NPRM ¶¶ 71-81)

Properly applied, TELRIC will account for real-world costs. There have been problems in the treatment of vendor cost, fill factors, and structure sharing. The impact of these, however, are not so great as to warrant changes to the pricing methodology or detailed guidelines to the state commissions. The states can address these issues based on existing Commission direction.

In Sprint's experience, TELRIC can understate vendor cost (NPRM ¶¶ 76-81), because state commissions have sometimes overstated vendor discounts. The BOCs have exaggerated the seriousness of this problem, however. The impact is felt far less keenly by the massive BOCs than by smaller ILECs, including Sprint, that do not enjoy the much larger BOCs' purchasing power and discount opportunities.

Fill factor (NPRM ¶¶ 73-75) assumptions have commonly been much higher than actual. But the significance of the higher-than-actual fill factors adopted by many states has also been exaggerated. The marginal cost of capacity is small. Carriers typically install extra capacity to meet even fairly distant future needs, because it is much more efficient and cost-effective to incur the added material and carrying costs instead of building new cable at some future time. The cost of fiber capacity is not in fiber itself, but in the permitting, right of way, trenching, and construction of the facility.

The opportunities of structure sharing (NPRM ¶¶ 71-72) also have often been overstated. Sprint believes opportunities are not as frequent as state commissions often assume. ILECs can raise these issues with the states without Commission-imposed changes to the model.

(5) Geographic and class-of-service deaveraging (NPRM ¶¶ 133-137)

The NPRM seeks comment on the merits of geographic deaveraging and whether there are grounds for it to be discontinued. NPRM ¶ 136. Geographic deaveraging certainly makes sense. The Local Competition Order recognized “that geographically deaveraged rates more closely reflect the cost of providing UNEs,” as the NPRM also acknowledges. Local Competition Order ¶ 755; NPRM ¶ 133. Costs vary widely by geography and density, a fact especially important for smaller and rural ILECs and those that do not enjoy the BOCs’ vast, contiguous service territories and enormous purchasing power. Because geographic deaveraging reflects the reality of differences in costs by geography, it does not improperly affect entry incentives for different geographic areas. Indeed, eliminating geographic deaveraging would distort economic incentives by artificially lowering entry costs in high-cost areas. The Local Competition Order was certainly reasonable in directing states to establish at least three cost-based rate zones. Discontinuing mandatory geographic deaveraging would, for smaller carriers at least, violate section 252(d)’s requirement the UNE pricing based on costs.

The NPRM also asks whether “to retain the requirement to average rates across different classes of service.” NPRM ¶ 137. Sprint opposes any steps to deaverage by class of service. Class of service is properly irrelevant to UNE pricing. The TELRIC methodology provides the pricing standard for network elements, unrelated to what services or class of customers any particular element is used to support. The costs of providing UNEs do not differ based on type of retail service or type of customer, but rather by geography, as the Local Competition Order recognized. Local Competition Order ¶ 766; NPRM ¶ 134. New entrants naturally target high-margin business

customers, and that will remain the case regardless of whether a given state has or has not fully deaveraged retail rates.

(6) Rate changes over time (NPRM ¶¶ 138-140)

The NPRM volunteers that “one issue on which all parties likely agree is that UNE pricing proceedings can be tedious.” NPRM ¶ 138. Since the Act requires UNE pricing to be cost-based, the process will be necessarily, and unavoidably, tedious.

The process is also not a one-time event. Sprint agrees that states can and should periodically revisit TELRIC pricing. NPRM ¶ 138. By nature, rates are only a snapshot – a moment in time. After three years or so, another snapshot may be appropriate. In rare instances, a full pricing proceeding may be warranted, but generally a review limited to particular issues will be sufficient. Reopening TELRIC pricing issues should not be done cavalierly, and the states are in the best position to determine the timing and scope of review proceedings. Sprint believes it is neither necessary nor appropriate for the FCC to call on states at this time to commence a new round of UNE price setting, or that it set a nine-month or other deadline for such a process.

The state commissions also do not need formulas to do this. The NPRM asks whether there might be automatic mechanisms which would adjust rates based on productivity or inflation, similar to some price cap regimes. NPRM ¶ 139. Sprint also understands the Office of Strategic Planning and Policy Analysis recently released a staff working paper – not purporting to reflect the Commission’s views -- that proposes a “simple” automatic correction factor for UNE pricing.¹⁹ The authors theorize that if

¹⁹ D. Mandy & W. Sharkey, “Dynamic Pricing and Investment from Static Proxy Models,” released Sept. 15, 2003.

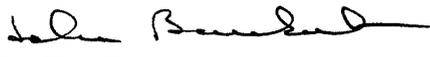
investment costs are falling over time, and the period between TELRIC price adjustments is shorter than the assumed asset life, then traditional TELRIC pricing would not permit ILECs to recover the cost of their investment. Any automatic correction factor, however, is inevitably crude and imprecise, and will tend only to compromise the relative accuracy of TELRIC pricing founded on proper cost studies. Over time, any automatic adjustment will likely lead to unreasonable results, either over- or understating costs. UNE pricing is not automatic, but requires periodic oversight by the state commissions. They can address adjustments on a going forward basis in their individual reviews, if and where that can be shown to be warranted based on actual economic conditions.

VI. CONCLUSION

The Commission has adopted a reasonable pricing methodology that was approved by the Supreme Court and that functions reasonably well. Its critics have never shown that the methodology actually harms ILECs or discourages investment. Where any state commission applies a questionable input, aggrieved parties can present their case in those proceedings or on appeal. The TELRIC methodology serves the public interest reasonably well. The Commission should not introduce additional uncertainty with needless adjustments or guidance to the state commissions, but should exercise restraint in this proceeding.

Respectfully submitted,

SPRINT CORPORATION

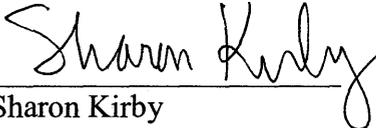
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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Comments of Sprint Corporation in WC Docket No. 03-173 was filed and served on this the 16th day of December, 2003 as follows:


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