Federal Communications Commission
Washington, D.C. 20554

In the Matter of
Developing a Unified InterCarrier Compensation Regime

CC Docket No. 01-92

**INITIAL COMMENTS
OF THE
PUBLIC SERVICE COMMISSION OF WISCONSIN
ON THE
MISSOULA INTERCARRIER COMPENSATION REFORM PLAN**

The Public Service Commission of Wisconsin (PSCW) respectfully submits these comments in response to the Federal Communications Commission's (FCC's) notice requesting comments regarding the Missoula Intercarrier Compensation (ICC) Reform Plan.[1] These comments will evaluate the Missoula Plan based on the principles the PSCW previously filed in comments in this docket, on May 19, 2005, and July 19, 2005. These comments also suggest modifications to the Missoula Plan to address certain issues that affect Wisconsin customers and the providers that serve them. Procedurally, we encourage proponents of the Missoula Plan to propose solutions and suggest the FCC provide opportunity for comments, on any and all, suggested solutions to these issues, including those identified here.

The PSCW continues to recognize the need for ICC reform and the importance of a coordinated federal-state reform process. Without ICC reform, the public switched telephone network (PSTN) will become further underutilized through bypass or used without compensation

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[1] Notice in CC Docket No. 01-92, released July 25, 2006, published in the Federal Register on August 9, 2006, (71 Fed. Reg. 45510).

from unidentified carriers (commonly called “phantom traffic”), leading to ever-increasing average costs, and potential local rate increases, and thus, pose a threat to universal service. Consequently, it is important that the FCC continue its investigation and move forward with ICC reforms. While the Missoula Plan does represent a large step forward in terms of building consensus within a polarized industry, issues still remain that divide large segments of the industry. Work needs to be done to address those issues, especially customer affecting issues.

A broad-based consensus plan increases the probability of successful implementation and has a better chance of avoiding or withstanding a court challenge. It is in this spirit that the PSCW identifies outstanding issues in these comments that beg for resolution. A modified Missoula Plan has the potential for gaining a wider base of support. To do so, however, would require the proponents of the Missoula Plan to offer amendments, and the FCC to seek additional comments on such amendments, much like was done before the FCC ultimately approved CALLS.

The consensus that is building around the Missoula Plan is, to a large extent, a provider consensus, and as noted elsewhere herein, that is important for getting any ICC reform plan formed and implemented. The PSCW urges the FCC--and all parties--to view this effort through the window of consumer concerns. ICC reform and the many elements of the Missoula Plan are complex. The need for efficient and rational carrier-to-carrier arrangements and pricing are vital to a competitive, effective telecommunications network. But when crafting the details of a plan and considering the future of how compensation will work, the FCC and all regulators need to recognize the urgency and necessity of keeping service affordable and options available for the ultimate users of the network. The issues raised, herein, are intended to cover some of the technicalities of the Missoula Plan, but are underpinned, in most part, by the need to recognize and respect the needs of consumers.

Missoula Plan Review

In its previous comments, the PSCW recommended the following seven core principles by which to review and evaluate ICC reform proposals:

1. Rely on rate uniformity to avoid arbitrage.[2]
2. Maintain technological and competitive neutrality by requiring compensation for exchange of telecommunications traffic regardless of type of provider (wireline, wireless, cable, VoIP, etc.).
3. Encourage maintenance and use of the Public Switched Telephone Network (PSTN) infrastructure without discouraging the development and use of alternative network infrastructures.
4. Avoid sudden and dramatic changes in wholesale and retail rates (i.e., rate shock).
5. Promote universal service, especially in rural and high cost areas.
6. Provide for timely cost recovery through a balance of wholesale and retail rates. Avoid cost over- or under-recovery and windfalls.
7. Promote jurisdictional cooperation between the FCC and state commissions to implement a national policy.

The Missoula Plan has many positive features. For example, it addresses arbitrage through rate uniformity where practical for reciprocal compensation and access (intra and interstate) (Principle #1). It has competitive features such as competitive alternatives for transport (Principles #2 and #3). It improves identification of traffic, identifies points of financial responsibility, and establishes appropriate billing information, thus encouraging maintenance and use of the PSTN (Principle #3). It

[2] Lack of rate uniformity among reciprocal compensation, inter- and intrastate-access within a company creates a greater risk of arbitrage than lack of rate uniformity among companies. Uniform ICC rates among companies where substantial cost differences exist could require ongoing support mechanisms for cost recovery.

provides a transition mechanism over several years that attempts to avoid sudden and dramatic rate changes, and offers practical solutions that recognize the unique regulatory histories and operational difficulties of various carriers (Principle #4). Restructure Mechanism funding also attempts to avoid sudden and dramatic rate changes, and promotes universal service, especially in rural and high cost areas (Principles #4 and #5).

When compared to the PSCW's principles, the Missoula Plan has the following notable shortcomings:

- The treatment of some Track 2 companies may lead to sudden and dramatic changes in retail customer rates if a degree of restructure/USF support is not maintained in perpetuity. This is contrary to Principle #4.
- So-called "pegged" rates may under-recover costs for some Track 2 companies, contrary to Principle #6.
- To the extent the Missoula Plan relies on "pegged" rates and pre-empts states from setting reciprocal compensation rates based on Total Element Long Run Incremental Cost (TELRIC) pricing standards, jurisdictional cooperation between the FCC and state commissions to implement a national policy is compromised (Principle #7).[3]
- The Missoula Plan has yet to address the availability of Restructure Mechanism funds for CLECs. Without this issue being addressed, the Missoula Plan cannot be considered competitively neutral as envisioned by Principle #2.
- Market forces alone may be inadequate to ensure that cost savings are passed through to customers. Some Track 1 companies therefore may realize windfalls, contrary to Principle #6.

State of Wisconsin Profile

To appreciate the impact of the Missoula Plan on Wisconsin customers and their providers, a profile of Wisconsin is provided below. In some respects, the state of Wisconsin

[3] At the same time, this is somewhat consistent with Principle #1 that strives for rate uniformity among reciprocal compensation and intra- and interstate access rates to avoid arbitrage.

represents a microcosm of the national ICC profile. The number and variety of carriers and traffic among them generate the kinds of problems and issues the Missoula Plan attempts to address. To the extent problems and issues can be addressed to meet the needs of all Wisconsin consumers, problems and issues will likely be addressed nationally. Consider the following facts:

- Track 1 carriers compromise 88 percent of the lines nationally; Track 2 companies–8 percent; and Track 3 companies–4 percent. Wisconsin's line comparison is 68 percent, 23 percent, and 9 percent, respectively.
- Wisconsin has 85 incumbent local exchanges carriers (ILECs) in 602 telephone exchanges. Ownership includes small cooperatives and closely held independent carriers, as well as large holding companies (e.g., AT&T, Verizon, CenturyTel, TDS, and Citizens/Frontier).
- ILECs are regulated under various forms of regulations including rate-of-return, price cap, and alternative regulation.
- Rate rebalancing (lowering intrastate access rates, raising local rates) has occurred by statute or by PSCW order for several price cap and alternatively regulated ILECs.
- As of December 31, 2005, competitive local exchange carriers' (CLECs) share of end-user switched access lines was 18 percent in Wisconsin and 18 percent nationwide. (<u>Local Telephone Competition: Status as of December 31, 2005</u>, Industry Analysis and Technology Division, Wireline Competition Bureau, FCC, July 2006, Table 8.)
- As of December 31, 2005, the percentage of lines provided to residential customers by Wisconsin ILECs was 64 percent, compared to 66 percent nationwide. The percentage of lines provided to residential customers by Wisconsin CLECs was 53 percent compared to 44 percent nationwide. (*Ibid.* Table 8.)
- As of December 31, 2005, the percentage of Wisconsin zip codes with no CLECs was 29 percent, as compared to 18 percent nationally. Wisconsin had 33 percent of its zip codes with 1-3 CLECs as compared to 25 percent nationally. At the other end of the spectrum, Wisconsin had 22 percent of its zip codes with 10 or more CLECs as compared to 35 percent nationally. (*Ibid.,* Table 17.)

- As of December 31, 2005, the number of Wisconsin mobile wireless telephone subscribers was 3,355,951, which exceeds the 3,327,444 Wisconsin landlines (2,739,056 ILEC/588,388 CLEC). Nationwide, the number of mobile wireless customers also exceeds the number of landlines, i.e., 203,699,128 wireless subscribers versus 175,350,377 landlines (143,766,498 ILEC/31,583,879 CLEC). (*Ibid.*, Tables 10, 11, and 14.)
- Geographically, Wisconsin has major cities (Milwaukee and Madison) and other metropolitan areas (e.g., Green Bay, Wausau, Eau Claire, and Superior), as well as small towns and villages surrounded by sparsely populated and remote rural areas. Wisconsin's economy has a mixture of agricultural, manufacturing and service industries.

These statistics underscore the importance to all Wisconsin consumers of developing a balanced, broad-based consensus plan that serves the interest of consumers in all segments of the industry.

Suggested Missoula Plan Modifications

The PSCW's initial comments will focus on three areas, namely Track 2 companies, the availability of Restructure Mechanism funds for CLECs, and the flow through of cost savings, to increase industry awareness of these specific concerns. The PSCW has participated in meetings on Early Adopter Funds involving Missoula Plan supporters and interested state commissions.[4] That group is also considering issues concerning the support for the rural areas of nonrural providers, the potential for area code exhaust, and the need for state flexibility. The PSCW is concerned about all the issues that may be addressed in this forum. However, the PSCW believes such concerns will be thoroughly vetted in the comments of others and does not elaborate on them here. The PSCW reserves its opportunity to address these concerns in reply comments.

[4] Missoula Plan, July 18, 2006, p. 63, footnote 24, p. 76, footnote 27.

Track 2 Issues: Wisconsin consumers served by Track 2 carriers already have the highest rates in Wisconsin[5] and will face the risk of even higher rates under the Missoula Plan. CenturyTel and Frontier/Citizens are Wisconsin's Track 2 carriers. Using data reported to the PSCW and, along with some simplifying assumptions, average local flat monthly rates and Subscriber Line Charges (SLC) by carrier Track were estimated before ICC Reform (2004), after Missoula Plan implementation, and if Restructure Mechanism support is not maintained in perpetuity following Missoula Plan implementation. The resulting monthly flat rates and SLC for local service are as follows:[6]

Period in ICC Reform Transition	**Track 1**	**Track 2**	**Track 3**
2004 Before ICC Reform	$19.09	$24.93	$20.20
After Missoula Plan	21.51	27.18	22.45
After Missoula Plan if Restructure Support is Not Maintained	21.51	34.54	24.67

In terms of geographic density, as measured by average lines per square mile, Wisconsin's Track 2 carriers are more similar to Track 3 carriers than to Track 1 carriers. That is to say, on average, Track 1 carriers have 188 lines per square mile, whereas Track 2 and Track 3 carriers have 21 and 24 lines per square mile, respectively. Geographic density is generally recognized to be inversely related to costs, i.e., higher costs are associated with lower densities. Yet, Track 2 carriers' ICC rates are treated more like Track 1 carriers than Track 3 carriers under the Missoula Plan.

[5] Mid-size companies that fall into Track 2 do not receive any USF local switching support due to the number of lines they serve and some of the lines in Track 2 receive only safety valve high cost support in light of their former ownership by nonrural companies.
[6] This presentation assumes all factors other than rate changes and restructure support are constant. It does not consider possible changes in traffic volume or potential additional costs to some providers under the Plan.

Wisconsin Track 2 carriers will need about $40 million in additional annual funding from the Restructure Mechanism, or $7.36 per line per month, at the end of the 2-year transition period. This raises concern over the long-term sustainability of the fund. Further, if future Track 2 "pegged" rate levels should be adjusted even lower after 4 years when the Missoula Plan rates are reviewed, then even greater amounts of restructure/USF support would be needed to avoid increasing the disparity between rates for various consumers.[7]

"Pegged" rates for Track 2 carriers may under-recover traffic sensitive[8] (TS) costs from wholesale customers for some Track 2 carriers. If TS costs are under-recovered, TS cost recovery would be shifted to end-users in the form of higher local and SLC rates, or onto the Restructure Mechanism. "Pegged" rates for Track 2 carriers set below TS costs create a greater need for Restructure Mechanism funding compared to the cost-based rates for Track 3 carriers.[9] Further, charging rates below TS cost does not send appropriate price signals to encourage efficient use of and investment in infrastructure.[10]

[7] 47 U.S.C. 254(b)(3) requires that all consumers "in all regions of the Nation" have access to telecommunications and information services that are "reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas."

[8] Traffic sensitive is used in the context of jurisdictional separations of costs (47 C.F.R. Part 69). However it can also be used to describe any telecommunications costs where an increase in the volume of traffic leads to increases in costs, such as the need to augment capacity to meet peak demand.

[9] ICC rates for Track 3 are generally referred to as cost-based rates. However, while interstate rates may be considered cost-based when applying National Exchange Carrier Association (NECA) national pooling mechanisms, if intrastate rates mirror the interstate pooled rates, those intrastate rates that are not pooled rates will not be cost-based for all individual companies. Some rates for Track 3 providers that own tandem switches are not cost based. Tandem rates are "pegged rates" regardless of Track designation of the provider.

[10] Large ILECs may argue in a broadband environment there are no traffic sensitive costs. However, in other forums considering broadband services, many large ILECs present the argument that they should be allowed to charge more for premium transmission priority in light of capacity limitations.

There are several possible solutions to Track 2 issues. Some of these solutions may not be mutually exclusive.

- Eliminate Track 2 by merging Tracks 2 and 3.
- Lengthen the transition period for Track 2 companies.
- Place all rate-of-return carriers into Track 3.
- Use a density (average lines per square mile) criterion for Track 2.
- Prescribe a method for updating "pegged" rates.
- Set standard default rates, subject to full negotiations and/or arbitration.
- Start with higher "pegged" rates, and adjust them according to actual market experience.
- Provide assurance that all traffic sensitive costs will be recovered in wholesale rates or from long-term USF.

There may be other solutions that address the Track 2 issues raised in these comments. Procedurally, the PSCW encourages proponents of the Missoula Plan to offer modifications to address Track 2 issues and suggests the FCC seek further comment on any and all modifications to the Missoula Plan that address Track 2 issues.

Restructure Mechanism Availability to CLECs: The Missoula Plan states that "Restructure Mechanism dollars will be available to other carriers in circumstances to be determined in the future." (p. 74) An incomplete plan creates uncertainty for CLECs and threatens their financial stability. In other words, CLECs are at a competitive disadvantage if they are uncertain about future costs and revenues that flow from intercarrier compensation. Without certainty, the Missoula Plan cannot be deemed competitively neutral.

The PSCW's examination of Wisconsin's CLECs as compared to Wisconsin's ILECs shows them to be more similar to Tracks 2 and 3 carriers than to Track 1 carriers in the proportion of revenues currently recovered from intercarrier compensation. Therefore, CLEC rate increases equivalent to ILEC SLC increases may not be sufficient alone to offset their access revenue losses. It is as important to provide CLECs with financial stability during this transition period as it is important to provide financial stability to other carriers that currently obtain a significant portion of their revenues from access services.

Some possible solutions to make the Restructure Mechanism available to CLECs may include the following:

- Use the methods applicable to price-cap carriers (with imputed SLC increases) to replace lost access revenues through the Restructure Mechanism.
- Mitigate the financially vulnerable position of CLECs at the beginning of ICC reform by making CLECs Track 2 carriers, rather than Track 1 carriers. Also consider allowing CLECs to participate in the Rural Transport Rule.[11]
- Provide support to CLECs now, subject however to further evaluation in a universal service proceeding as to how to determine the actual costs associated with access services and how to convert implicit support to explicit support.

The PSCW encourages Missoula Plan proponents to offer amendments to the Missoula Plan and suggests the FCC seek further comments on any and all modifications to the Missoula Plan that address Restructure Mechanism availability to CLECs.

Flow Through of Cost Savings: One carrier's lost ICC revenue is another carrier's cost savings. As a result, some customers will see higher rates, and some should see lower rates. In a perfect world, the results of ICC reform should be "zero sum" for customers as a whole. Over a

[11] Under the Rural Transport Rule, Track 1 ILECs will continue to absorb some of the costs of transporting traffic originated by rural carriers. This possible modification for CLECs would need further adjustment to address the situation where a Track 1 ILEC is not involved in a call.

5-year period, the estimated cost savings will accumulate to about $32.5 billion dollars.[12] Will the competitive marketplace flow through these cost savings to consumers? If not, some carriers will realize an undeserved windfall.

Term contracts on business accounts, often 2 years or more, and 1- to 2-year terms on residential wireline packages and wireless accounts, reduce the chances of immediate flow-through to customers. Without a regulatory obligation, those customers may forego an estimated $2.9 billion in the first year and $5.9 billion in the second year of ICC reform. Moreover, the degree of competition varies geographically. Without a requirement to flow-through cost savings, customers with few competitive choices are less likely to see the benefits of ICC reform flow through to them in the form of lower rates.

Some possible solutions to accomplish flow-through of cost savings may include the following:

- Require regulatory credits or forego other regulatory charges such as number portability, 911, USF, etc. (If regulatory charges are imposed during the term of an existing customer contract, presumably credits could also be implemented. Customer objections to lower bills are unlikely.)
- Require opportunity for contract amendments to reflect the flow-through of cost savings. (Again, customer objections to lower bills are unlikely.)

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[12] Based on the following estimates of access reductions using Wisconsin data for relative average access reduction per line for each Track, and Track 1 and Track 2 reductions in the first two years of the Plan:

Year of Missoula Plan	Annual Amount (Billions)	Cumulative Amount (Billions)
Year 1	$2.9	$2.9
Year 2	$5.9	$8.8
Year 3	$7.8	$16.6
Year 4	$7.9	$24.5
Year 5	$8.0	$32.5

While access rates are changed in steps, step one is at the start of the plan so step three is the end of year 2.

- Offset SLC increases with decrease in overall package price.
- Do not allow SLC increases on packages but impute the SLC for computation of Restructure Mechanism support.
- Require carriers who realize overall cost savings to make an additional contribution to the Restructure Mechanism at least in the first 2 years of the Missoula Plan.

The PSCW encourages proponents of the Missoula Plan to offer amendments and suggests the FCC seek further comments on any and all modifications to the Missoula Plan that address flow-through of cost savings.

This issue of flow-through is one example of a Missoula Plan facet that raises questions about how the plan will impact consumers. As noted at page 2 above, the PSCW urges that the consumer perspective not be overlooked as this proceeding moves forward. In that regard, the PSCW highlights observations of the National Regulatory Research Institute (NRRI), which has identified concerns regarding the consumer impacts of the Missoula Plan.[13] NRRI points out that the Missoula Plan shifts recovery for greater than 50 percent of LEC network costs onto end users and away from other carriers. NRRI also discusses, and points out various shortcomings of the analysis of the consumer impacts of the Missoula Plan done by AT&T economists Richard Clarke and Thomas Makarewicz.[14] NRRI notes: "With respect to wireline consumers, their (AT&T's) basic argument is that increases in consumer surplus resulting from lowered access charges will benefit consumers by saving them money on existing long-distance usage and induce additional long-distance usage via lower long-distance prices."[15] However, NRRI cites

[13] Edwin Rosenberg, Lilia Pérez-Chavolla, and Jing Liu, *Commissioner Briefing Paper Intercarrier Compensation and the Missoula Plan*, The National Regulatory Research Institute (NRRI), NRRI 06-14, October 2006.
[14] Richard N. Clarke and Thomas J. Makarewicz, *Economic Benefits from Missoula Plan Reform of Intercarrier Compensation*, Missoula Plan, Exhibit 2, 18 July 2006.
[15] Ibid., NRRI, p. 61.

these issues with AT&T's analysis: 1) the erroneous assumption of 100 percent flow through to consumers of the benefits of carrier access cost reductions, 2) the use of a conventional estimate of AT&T's existing price demand elasticity for long distance services that is not clearly reasonable in today's market, and 3) the lack of analysis of the very large amount of long distance usage necessary (over four hours) for customers to be net beneficiaries under the plan. In summary of AT&T's analysis of the consumer impacts of this shift, NRRI concludes:

> Overall, the analysis provided with the Plan indicates that many categories of users will have lower bills after the Plan is implemented. However, low-usage customers (rural wireline, urban wireline, and wireless) end up paying more in total. Customers who use multiple services, including broadband, will see reduced total bills. Heavy long-distance users, including many business customers, will likely benefit relatively more than low and moderate users.[16]

That AT&T and NRRI diverge on these matters underscores the complexity of this issue. Reforms that make more effective and efficient interactions among providers are worthwhile, but the equation is broader and must include full consideration of consumer impacts as well.

Conclusion

ICC reform is necessary. Current mechanisms for ICC and USF support need to be reformed for purposes of equity, competitive neutrality, universal service protections, and economic rationale. The Missoula Plan represents a good starting point based on the principles the PSCW has previously enunciated. The Missoula Plan is not, however, without its shortcomings. With certain modifications to address issues identified in these comments, the Missoula Plan could lead to a balanced, broad-based consensus plan that meets the needs of the

[16] Ibid. p. 64.

entire industry and provides customers protection from high rates and inadequate service. The PSCW strongly encourages proponents of the Missoula Plan to offer amendments to address these issues and encourages the FCC to provide further opportunity to comment on any proposed modifications to the Missoula Plan.

Dated at Madison, Wisconsin, ___October 25, 2006__

By the Commission:

/s/ *Sandra J. Paske*

Sandra J. Paske
Secretary to the Commission

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