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ACCESS REFORM FOR RATE OF RETURN LECS

Last month, in JSI's *News & Commentary* No. 9808, we advised you that the Federal Communications Commission (FCC) had released a Notice of Proposed Rulemaking (NPRM) that may significantly affect how small local exchange carriers (LECs) bill interexchange carriers (IXCs) and recover their costs for access. We also indicated that, if adopted, these changes will not only affect how you charge for the access services you provide, but will also affect the level of recovery. On July 15, the FCC extended the date for filing comments in this proceeding. Comments are now due August 17, 1998.

This proceeding and its potential impact will affect the manner in which you conduct all aspects of your businesses, both regulated and non-regulated. We consider the filing extension as an opportune time to share with you our initial thoughts and tentative conclusions on several matters that are the subject of the FCC's NPRM. Our objective is to foster industry discussion on these issues in hopes of persuading the FCC that specific consideration should be given to rate-of-return LECs in its access reform proceeding.

We reported previously that the NPRM raises the general question of why the FCC should not impose on rate-of-return LECs the same access reform changes it has already imposed on price-cap LECs (the regional Bell operating companies [RBOCs] and other large telcos). These changes include increased rates for multi-line business and non-primary residential subscriber line charges (SLCs), and a new charge to be assessed to IXCs – the controversial Presubscribed Interexchange Carrier Charge (PICC).

JSI agrees that many of the changes proposed by the FCC are consistent with the fundamental principle of cost-causation. (For instance, non-traffic sensitive [NTS] revenues should normally cover NTS costs.) However, based upon recently available industry information, we have determined that the adoption of these changes will create significant industry imbalances. These imbalances will place your LEC operations in future jeopardy.

JSI has obtained from National Exchange Carrier Association (NECA) industry information related to its latest filing for the common-line and traffic-sensitive pools. Using this data, JSI analyzed the proposed access reform changes to determine their potential impact on the access rate structures and levels of rate-of-return LECs that participate in the NECA pools. We find these results both startling and disturbing. With equal rates of growth in both costs and demand, the SLC and PICC rates that would be applicable to rate-of-return LECs are listed in Table 1.

Table 1
Estimated SLC and PICC Rates for Rate-of-Return LECs*
1999-2008

	Current Year	July, 1999	July, 2000	July, 2002	July 2004	July, 2006	July, 2008
SLC Charges							
Primary Line Residence, Single Line Business	3.50	3.50	3.50	3.50	3.50	3.50	3.50
Non-Primary Line Residence	3.50	5.00	6.50	9.00	9.00	9.00	9.00
Multi-line Business	6.00	9.00	9.00	9.00	9.00	9.00	9.00
PICC Charges							
Primary Line Residence, Single Line Business	-	.53	1.03	2.03	3.03	4.03	5.05
Non-Primary Line Residence	-	1.50	2.50	4.50	6.50	8.50	10.50
Multi-line Business	-	2.75	4.25	7.25	10.25	13.25	16.25

*Rates are not adjusted for inflation. For display purposes, we have reported rate impacts for every other year.

We are alarmed that, under the proposed rules, the SLCs for a non-primary residential line and a multi-line business line reach the FCC-imposed cap of $9.00 per line in three years. Based on the desire to drive the carrier-common-line (CCL) rate to zero, the PICC is able to increase, subject to annual caps. The estimated PICC in 2008 reaches $5.05 for primary residential and single business lines, $10.50 for non-primary residential lines, and $16.25 per month for multi-line business lines. (Year 2008 is the last year of SLC and PICC increases necessary to eliminate the CCL for rate-of-return LECs.)

Some argue that the PICC is only a per-line charge to the IXC, based on the presubscribed access lines of the IXC. However, recent evidence suggests that a number of IXCs are passing along this charge to their end-user customers. The fact that the IXCs must geographically average rates across their customer base is little comfort to regional IXCs and independent local exchange carriers (ILEC) long-distance affiliates that do not have a large geographic scope. We consider the PICC, as it is currently applied, to be a *de facto* second SLC.

JSI contends that the costs and operating area characteristics of rate-of-return LECs, as compared with price-cap LECs, makes the proposed price-cap-type access reform for rate-of-return LECs both infeasible and undesirable. In fact, we believe that it would be contrary to the universal service and consumer protection provisions of the Telecommunications Act of 1996. Furthermore, these actions will discourage IXCs from providing toll service in high-PICC areas, and will thereby deprive rural users of the benefits of the new telecommunications age. Moreover, the high levels of PICC and SLC in ILEC territories will all but eliminate regional and small long-distance operations – including rate-of-return, LEC-affiliated operations.

We believe that there are several viable alternatives that the FCC should consider. First, the FCC should cap both the SLC and PICC rates at nationwide RBOC averages. Alternatively, we believe that the suggestion that SLC rates be frozen at current levels, and PICC rates capped at nationwide RBOC averages, has merit and should be discussed.

Due to an absolute necessity to create, at minimum, comparable SLC and PICC rates for both rate-of-return and price-cap LECs, we feel that proposed FCC actions need to be modified. Without modification, the RBOC and rate-of-return LEC rate differential is dramatic, as shown in Table 2.

Table 2
Comparison of Price-Cap and Rate-of-Return LEC SLC and PICC in Year 2008

	Year 2008		Percentage
	Price-Cap LECs	Rate-of-Return LECs	Difference
SLC Charges			
Primary Line Residence, Single Line Business	$3.50	$3.50	0%
Non-Primary Line Residence	$7.14	$9.00	26%
Multi-line Business	$7.14	$9.00	26%
PICC Charges			
Primary Line Residence, Single Line Business	$2.15	$5.05	135%
Non-Primary Line Residence	$ -	$10.50	n/a
Multi-line Business	$ -	$16.25	n/a

When comparable SLC and PICC rates are established, the desirability of transferring the central office line port costs, the residual Transport Interconnection Charge (TIC) and the marketing costs to the common-line access element is in doubt. Based upon our analysis, these transfers result in the substitution of a usage-sensitive CCL rate for the usage-sensitive traffic-sensitive rates of the TIC and Local Switching rate elements. In the end, the composite switched access rate does not change significantly.

We have provided you with this information now so that you will have a better understanding of the potential consequences of access reform on your future business endeavors.

If you have any questions or comments, please do not hesitate to contact any of our offices.