requirements.[268] First, providers of interexchange telecommunications services are required to charge rates in rural and high-cost areas that are no higher than the rates they charge in urban areas.[269] This is known as the geographic rate averaging rule. Second, providers of interexchange telecommunications services are required to charge rates in each state that are no higher than those in any other state.[270] This is known as the rate integration rule.

84. In the *Geographic Rate Averaging Order*, the Commission explained that geographic rate averaging benefits rural areas by providing access to a nationwide telecommunications network at rates that do not reflect the disproportionate burdens that may be associated with recovery of common line costs in rural areas.[271] The Commission also noted that geographic rate averaging ensures that rural customers will share in lower prices resulting from nationwide interexchange competition.[272] Similarly, the Commission enunciated that its policy of integrating "offshore points" such as Hawaii and Alaska into the mainland's interstate interexchange rate structure brings the benefits of growing competition to the entire nation.[273]

85. Under the Commission's rate averaging and rate integration requirements, IXCs bear the burden of averaging on a nationwide basis the different per-minute switched access rates charged by LECs. This results in an implicit subsidy flowing from customers in low-cost areas served by IXCs to customers in high-cost service areas. The Commission historically has taken steps to facilitate IXC compliance with these requirements. For example, the averaging of the CCL charge in the NECA pool and the subsequent adoption of the LTS mechanism each reduced the access rate differentials that IXCs had to accommodate in their interstate long-distance rates.[274]

86. Absent some further reform of the access charge regime, we are concerned that the rate averaging and rate integration requirements eventually will have the effect of discouraging IXCs from serving rural areas. These requirements may place IXCs that serve rural areas at a competitive disadvantage to those that focus on serving urban areas. For instance, the BOCs offer long-distance services only within their regions and not to customers served by high-cost rural LECs. Nationwide IXCs such as AT&T, on the other hand, offer long-distance services in both urban and rural areas, including areas served by rural LECs. We are thus concerned that the competitive realities of the marketplace may drive increasing specialization of companies serving rural as opposed to non-rural areas, ultimately leading to higher costs and fewer competitive choices for rural consumers. We ask parties to comment on the relationship between the rate averaging and rate integration requirements and the access charge reform

[268] *Id.* at 9565-66, para. 2.

[269] 47 C.F.R. § 64.1801; *see Geographic Rate Averaging Order,* 11 FCC Rcd at 9568-69, para. 9, 9574, para. 20.

[270] 47 C.F.R. § 64.1801; *see Geographic Rate Averaging Order,* 11 FCC Rcd at 9588, para. 52.

[271] *Geographic Rate Averaging Order,* 11 FCC Rcd at 9567, para. 6.

[272] *Id*.

[273] *Id*. at 9588, para. 52.

[274] *See Access Charge Order,* 93 FCC 2d at 328, paras. 314-15*; MTS and WATS Market Structure Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 78-72, CC Docket No. 80-286, Report and Order, 2 FCC Rcd 2953, 2956 para. 24 (1987).

proposals described above. Do any of the proposals ease concerns about the disparate impact of rate averaging and rate integration requirements on nationwide IXCs? If not, are there additional steps the Commission should take to address these concerns? For example, are there circumstances where the Commission should forbear from the rate averaging and rate integration requirements? Or is section 254 amenable to an interpretation that would permit the Commission to treat a portion of the high costs of interstate local switching and transport as universal service? Parties are asked to comment on the legality of such an interpretation and the desirability of taking such an approach.

E. Network Interconnection Issues

1. Background

87. Under section 251(c)(2)(B), an incumbent LEC must allow a requesting telecommunications carrier to interconnect at any technically feasible point.[275] The Commission has interpreted this provision to mean that competitive LECs have the option to interconnect at a single point of interconnection (POI) per LATA.[276] In addition, our rules preclude a LEC from charging carriers for traffic that originates on the LEC's network.[277] For traffic subject to section 251(b)(5) of the Act, our rules permit a terminating carrier to recover from the originating carrier the cost of certain facilities from an "interconnection point" to the called party.[278] In the *Intercarrier Compensation NPRM*, the Commission solicited comment on whether an incumbent LEC should be obligated to bear its own costs of delivering traffic to a single POI when that POI is located outside the calling party's local calling area.[279] Alternatively, the Commission asked whether a carrier should be required to interconnect in every local calling area or pay the incumbent transport and/or access charges if the location of the single POI requires transport beyond the local calling area.[280] The Commission also sought comment on

[275] 47 U.S.C. § 251(c)(2)(B).

[276] *Application by SBC Communications Inc., Southwestern Bell Tel. Co. and Southwestern Bell Communications Services, Inc., d/b/a Southwestern Bell Long Distance pursuant to Section 271 of the Telecommunications Act of 1996 to Provide In-Region, InterLATA Services in Texas*, CC Docket No. 00-65, Memorandum Opinion and Order, 15 FCC Rcd 18354, 18390, para. 78 n.174 (2000).

[277] 47 C.F.R. § 51.703(b). At least two courts have held that this rule applies even in cases where an incumbent LEC delivers calls to a POI located outside its customer's local calling area. *See Southwestern Bell Tel. Co. v. Public Utils. Comm'n of Texas*, 348 F.3d 482, 486-87 (5th Cir. 2003); *MCImetro Access Transmission Services, Inc. v. BellSouth Telecommunications, Inc*., 352 F.3d 872, 881 (4th Cir. 2003). Local calling areas are established or approved by state commissions. *Local Competition First Report and Order*, 11 FCC Rcd at 16013-14, para. 1035.

[278] Specifically, our rules permit recovery of the costs of transport and termination of telecommunications traffic between LECs and other telecommunications carriers. 47 C.F.R. § 51.701. The rules define "transport" as the "transmission and any necessary tandem switching of telecommunications traffic subject to section 251(b)(5) of the Act from the interconnection point between the two carriers to the terminating carrier's end office switch that directly serves the called party, or equivalent facility provided by a carrier other than an incumbent LEC." *Id.* § 51.701(c). The rules define "termination" as the "switching of telecommunications traffic at the terminating carrier's end office switch, or equivalent facility, and delivery of such traffic to the called party's premises." *Id.* § 51.701(d).

[279] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9651, para. 113.

[280] *Id.* The Commission also asked whether its regulations permit the imposition of access charges for calls that originate and terminate within one local calling area but cross local area boundaries due to the placement of the POI. *Id*.

whether current rules result in inefficient network design by forcing the originating LEC to bear the cost of transport outside the local calling area, or whether requiring competitors to establish multiple POIs or pay for transport beyond the local calling area forces competitive carriers to replicate the incumbent LEC network.[281]

88. In addition to these specific questions, the Commission sought comment on two working papers describing bill-and-keep approaches to intercarrier compensation and default interconnection rules that would apply when carriers cannot agree on the terms for interconnection.[282] Under the Central Office Bill and Keep (COBAK) approach, no carrier may recover any costs of its customers' local access facilities from interconnecting carriers, and the calling party's network is responsible for the cost of transporting the call to the end office serving the called party.[283] This approach would require the calling party's network to construct transport facilities to the called party's end office or purchase transport facilities or services from another carrier (including possibly the called party's network). Under the Bill Access to Subscribers – Interconnection Cost Split (BASICS) approach, networks would recover all intra-network costs from their end-user customers and divide equally the costs that result from interconnection.[284] The BASICS approach would require networks to distinguish between intra-network costs and the incremental costs of interconnection.[285]

89. In response to the *Intercarrier Compensation NPRM*, most competitive LECs and CMRS providers urge the Commission to maintain the single POI per LATA rule.[286] They argue that the current rule prevents incumbent LECs from imposing costly and burdensome interconnection requirements, thereby creating barriers to entry.[287] According to these commenters, a rule requiring competitors to interconnect in every local calling area or pay for transport to the POI outside the local calling area would essentially require new entrants to replicate the existing incumbent LEC network, regardless of whether it is efficient to do so.[288] Competitive LECs emphasize that they are willing to establish additional POIs

[281] *Id.* at 9652, para. 114.

[282] *See id.* at 9620-22, paras. 22-30.

[283] *Id.* at 9620-21, para. 23.

[284] *Id.* at 9621, para. 25.

[285] *Id*. at 9622, para. 28.

[286] *See, e.g*., Cbeyond Comments at 9; Focal *et al*. Comments at 56; Global NAPs Comments at 7 n.11; Level 3 Comments at 28; PCIA Comments at 30; Sprint Comments at 29; Time Warner Comments at 15; WorldCom Comments at 8l; AT&T Wireless Reply at 29; e.spire and KMC Reply at 14-15; Focal *et al*. Reply at 43; Level 3 Reply at 3; PCIA Reply at 11; Taylor Communications Reply at 34; VoiceStream Reply at 31-32; WebLink Wireless Reply at 17. Some CMRS providers maintain that they should not be required to maintain more than one POI per MTA. *See* CTIA Comments at 34; PCIA Comments at 30; Arch Wireless Reply at 7.

[287] *See* AT&T Comments at 57; Cablevision Lightpath Comments at 5; Time Warner Comments at 14; AT&T Reply at 36-37; AT&T Wireless Reply at 30.

[288] *See* Cablevision Lightpath Comments at 3; PCIA Comments at 31; AT&T Reply at 36; Focal *et al*. Reply at 43; Taylor Communications Reply at 36. *See also* Letter from Patrick H. Merrick, Director, Regulatory Affairs, AT&T, to William Caton, Acting Secretary, Federal Communications Commission, CC Docket No. 01-92, at 11 (filed May 1, 2002) (claiming that mirroring the incumbent LEC network is not economic for new entrants and will stifle competition) (AT&T May 1 *Ex Parte* Letter).

when traffic levels warrant them,[289] and they contend that any additional transport costs are minimal in any event.[290]

90. As discussed in the *Intercarrier Compensation NPRM*, the incumbent LECs support a requirement that competitive carriers establish a POI in each local calling area or pay the transport costs to reach a POI outside the local calling area.[291] Incumbent LECs argue that, under the current rules, they bear a disproportionate amount of transport costs when a competitive LEC primarily terminates traffic and the recipient of the traffic is located near the competitive LEC's switch.[292] The competitive LECs and many CMRS providers oppose the idea of paying for transport and contend that the incumbent LEC should be required to deliver all traffic originating on its network to the selected POI at no charge.[293] Other commenters suggest that the interconnecting carrier selecting the POI be responsible for some portion of the transport costs to a POI located outside the local calling area, or that the interconnecting carrier establish additional POIs once certain criteria are met.[294] These commenters propose different criteria for establishing additional POIs, including specific traffic volume or distance thresholds.[295]

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[289] *See* Allegiance Comments at 27; AT&T Comments at 59; Time Warner Comments at 14; WorldCom Comments at 22; AT&T Reply at 37; WorldCom Reply at 8; AT&T May 1 *Ex Parte* Letter at 12. They reason that additional POIs increase network reliability, and that network planners and engineers are in the best position to determine when additional POIs are warranted. *See* Allegiance Comments at 27-28.

[290] *See* PCIA Comments at 32.

[291] *See Intercarrier Compensation NPRM*, 16 FCC Rcd at 9651, para.112. *See also* MECA Comments at 44; SBC Comments at 18-19. *But see* Focal *et al*. Reply at 44-45 (pointing out that the incumbent LECs appear to support a single POI per LATA rule in the context of bill-and-keep). In addition, SBC argues that the single POI per LATA rule diminishes competitive LEC incentives to build their own networks. SBC Comments at 18. *But see* AT&T Reply at 37 (arguing that the existence of numerous POIs belies SBC's assertions).

[292] *See* Letter from Karen Brinkmann, Counsel to CenturyTel, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket Nos. 96-98, 99-68, and 01-92, Attach. at 1-2 (filed Sept. 30, 2004); Letter from Donna Epps, Vice President, Federal Regulatory Advocacy, Verizon, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket Nos. 99-68 and 01-92, at 2-3 (filed Dec. 16, 2004). *See also* Time Warner Reply at 28 (explaining that "free riding" can occur when a competitive LEC terminates more traffic than it originates and the recipient of the traffic is located near the competitive LEC's switch, thereby forcing the originating carrier to bear a disproportionate amount of transport costs).

[293] *See* Advanced Paging, *et al*. Reply at 5-6; AT&T Reply at 34; Cablevision Lightpath Reply at 8. *See also* AT&T May 1 *Ex Parte* Letter at 6. Indeed, some commenters maintain that the interconnection "at any technically feasible point" language in section 251(c)(2)(B) of the Act precludes the Commission from modifying this rule. *See, e.g*., Allegiance Comments at 26-27; AT&T Comments at 56; AT&T Reply at 34; Taylor Communications Reply at 34-35. Thus, they maintain that each carrier should bear all transport costs on its side of the POI.

[294] *See* CenturyTel Comments at 31-32; Sprint Comments at 29-30; Texas Commission Comments at 11. AT&T Wireless, for instance, suggests that the carriers share (split) the transport costs because such an approach will encourage both parties to negotiate efficient POIs. *See* AT&T Wireless Reply at 29-30. *See also* Time Warner Reply at 29 (suggesting that the Commission establish a presumption that the current rules apply if the traffic originates and terminates in the same local calling area, and permit the states to address "outlier" situations).

[295] *See* Level 3 Comments at 29; Sprint Comments at 31 (suggesting a combined traffic volume and distance threshold); Texas Commission Comments at 12 (supporting a traffic volume threshold); Level 3 Reply at 24-25 (supporting a default traffic volume threshold). *See also* Time Warner Comments at 14 (stating that it agreed to establish additional POIs once traffic volumes reach a DS1 threshold).

2. Discussion

91. The comments confirm that issues related to the location of the POI and the allocation of transport costs are some of the most contentious issues in interconnection proceedings.[296] In particular, the record suggests that there are a substantial number of disputes related to how carriers should allocate interconnection costs, particularly when the physical POI is located outside the local calling area where the call originates or when carriers are indirectly interconnected. These disputes arise in part because of a lack of clarity among the various rules governing the costs of interconnection facilities and the relationship of those rules to the single POI rule.[297] In addition, our current rules may encourage traffic imbalances because terminating networks not only collect reciprocal compensation, they also avoid financial responsibility for transport facilities. When traffic is out of balance, the cost of interconnection is borne primarily by the originating carrier, and the terminating carrier may lack the incentive to minimize the transport costs associated with connecting the two networks.[298] For instance, competitive LECs appear to have targeted customers that primarily or solely receive traffic, such as ISPs, in order to become net recipients of traffic.[299]

92. In this Further Notice, we solicit additional comment on changes to our network interconnection rules to accompany proposed changes to the intercarrier compensation regimes. The record contains a number of different proposals concerning the responsibility for network interconnection costs. For example, BellSouth asks that we establish a default POI at the incumbent LEC's tandem office and hold each carrier responsible for transport costs on its side of the POI.[300] Qwest proposes a POI at the "edge" of the network, with each carrier responsible for costs on its side of the POI.[301] Qwest identifies

[296] *See, e.g.*, Sprint Comments at 29 (urging the Commission to provide more definitive default rules concerning the obligations of carriers to establish POIs and the responsibility for transport costs); Level 3 Reply at 22-23 (asking the Commission to clarify its POI rules); PCIA Reply at 11 (stating that clarification of the interconnection rules is "long overdue"); Time Warner Reply at 28 (requesting that the Commission ensure that competitors are able to take advantage of the efficiencies of a single POI in a LATA without "free riding" on the incumbent LEC network).

[297] We note that there are petitions for declaratory ruling pending before the Commission that raise issues related to the responsibility for interconnection costs under our existing rules. *See Comment Sought on Sprint Petition for Declaratory Ruling Regarding the Routing and Rating of Traffic by ILECs*, CC Docket No. 01-92, Public Notice, 17 FCC Rcd 13859 (2002); *Pleading Cycle Established for Comments on @ Communications Petition for Declaratory Ruling*, CC Docket No. 02-4, Public Notice, 17 FCC Rcd 1010 (2002). We will clarify the application of our current rules when we address these petitions.

[298] *See* Sprint Comments at 29.

[299] *Intercarrier Compensation NPRM*, 16 FCC Rcd at 9616, para. 11. In such situations, the originating carrier bears the cost of interconnection to the single POI selected by the competitive LEC in addition to paying reciprocal compensation for the termination of traffic. Because ISP customers rarely, if ever, originate traffic, there is little traffic flow in the opposite direction, and the originating carrier bears the majority of the interconnection costs between the two carriers.

[300] *See* Letter from W.W. Jordan, Vice President – Federal Regulatory, BellSouth, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at Attach. (filed June 14, 2002). Similarly, Verizon proposes default interconnection points at incumbent LEC tandem wire centers. *See* Verizon Reply at 13-18.

[301] *See* Letter from John W. Kure, Executive Director – Federal Policy and Law, Qwest Communications International, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at Attach. (filed Aug. 2, 2002).

specific locations for the "edge" of the network depending on the network and/or the type of interconnecting carrier.[302] Similarly, the ICF proposes a new approach to network interconnection based on carrier "Edges."[303] As discussed above, the ICF plan establishes default technical and financial rules that generally require an originating carrier to deliver traffic to the "Edge" of a terminating carrier's network.[304]

93. We ask parties to comment on the network interconnection proposals in the record and on the ICF's proposed default network interconnection rules.[305] Is the level of detail proposed by the ICF appropriate for inclusion in federal rules, or would it be better for the Commission to establish more general requirements that leave the details to be negotiated between the carriers? What are the costs and benefits of establishing different interconnection rules for hierarchical, non-hierarchical, and CRTC networks, as the ICF proposes? Is this approach philosophically consistent with the goal of a unified regime? Is this a sensible way to approach interconnection between different types of networks, or are there other factors we should consider?

94. We also seek comment on whether the Commission should consider different network interconnection rules for small incumbent LECs or rural LECs.[306] Would different network interconnection rules for small incumbent LECs or rural LECs serve the Commission's goals of promoting economic efficiency and facilities-based competition? Would a rule requiring competitors to pay for transport outside the local calling area to the POI essentially require new entrants to replicate the existing incumbent LEC network, regardless of whether it is efficient to do so? Further, is such an approach competitively and technologically neutral given the different network architectures of competitive networks, including wireless networks?

95. Other proposals, such as the ARIC, CBICC, and NASUCA proposals, do not address changes to the existing network interconnection rules. If we do not adopt the ICF proposal, we seek comment on whether to retain our existing network interconnection rules as part of our reform efforts or whether we should consider alternative methods of determining financial responsibility for network interconnection costs. Parties that support retention of the existing network interconnection rules should address the issues arising under the current rules (as described above) and also the impact of any particular compensation reform proposal on the existing network interconnection rules. Parties that do not support retention of our existing network interconnection rules should comment on alternative methods of determining financial responsibility for network interconnection costs.

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[302] *Id.*

[303] *See* ICF Proposal at 3-31. *See also supra* para. 40.

[304] *See* ICF Proposal at 4-9.

[305] In addition, we note that the default network interconnection rules proposed by Western Wireless appear to be based, in part, on the ICF's "Edge" approach. *See* Western Wireless Proposal at 12. For interconnection between hierarchal incumbent LECs and other carriers, the Western Wireless proposal permits interconnection at the carrier "edge" or under a shared transport arrangement at the option of the competitive carrier. *Id.*

[306] For example, under the EPG proposal, the incumbent LEC would not be responsible for delivering traffic or paying any costs to a POI located outside the incumbent LEC's contiguous service area or beyond the serving area boundary. EPG Proposal at 33.

96. We also solicit comment on whether changing our pricing methodology for reciprocal compensation, as proposed above, will have any effect on the incentives of competitive carriers, including CMRS providers, to establish multiple POIs. For example, if the Commission adopts a bill-and-keep approach and competitors pay the same rate (zero) to terminate calls wherever they connect to the incumbent LEC network, will there be incentives to interconnect at more than one POI per LATA? If reducing reciprocal compensation rates also reduces the incentive to establish multiple POIs, is there a need for the Commission to establish ground rules to facilitate more efficient interconnection? Parties proposing to require competitive carriers to establish multiple POIs per LATA should explain clearly what standards they would apply and provide objective evidence demonstrating the reasonableness of their proposal.

97. Finally, we ask parties to address whether any additional rule changes are needed to harmonize the network interconnection rules that apply to section 251(b)(5) traffic with the rules that apply to access traffic. For example, if we adopt a unified rate that applies to all types of traffic but retain interconnection rules that vary by type of traffic, carriers still may have an incentive to classify traffic as one type or the other in order to reduce their share of the interconnection costs. Should different rules apply to interconnection facilities connecting an IXC POP and a LEC switch?

F. Cost Recovery Issues

1. Interstate Access Charges

a. Price Cap LECs

98. By any measure, interstate access charges imposed on IXCs by price cap carriers have declined significantly over the years. At the time the original access charge regime was adopted, the average interstate traffic-sensitive switching rate was 3.1 cents per minute and the average total access charge was 17.26 cents per minute.[307] Most recent figures show the average interstate traffic-sensitive rate to be 0.48 cents per minute and the average total access charge to be 1.44 cents per minute.[308] Notwithstanding these reductions, access charges continue to represent a significant revenue source for these carriers and a significant cost component for IXCs.[309]

99. Many of the reform proposals include mechanisms by which some carriers will be permitted to offset revenues previously recovered through interstate access charges.[310] Other proposals question the need to offset revenues and oppose proposals that include revenue guarantees or assumptions

[307] *Telephone Trends Report*, Table 1.2. These figures represent the average rates (weighted by minutes of use) for all LECs that file access tariffs subject to price-cap regulation and all LECs in the National Exchange Carrier Association (NECA) pool.

[308] *Id.*

[309] In 2003, BOC interstate access revenues for switching amounted to approximately $1.8 billion. Source: Automated Reporting Management Information System (ARMIS) Annual Summary Report (FCC Report 43-01), Table 1, Cost and Revenue (1996-2003).

[310] For instance, the ICF Proposal calls for increased SLCs and two new universal service recovery mechanisms. *See* ICF Proposal at 69-74.

concerning revenue neutrality.[311] We solicit comment on whether these mechanisms, or something comparable, must be adopted if we reduce or eliminate the ability of LECs to impose interstate switched access charges on IXCs. What is the Commission's legal obligation to provide alternative cost recovery mechanisms? Would the elimination of interstate switched access charges be confiscatory in the absence of such mechanisms? Should carriers be required to demonstrate that they will be unable to recover their switching and transport costs from other sources before we establish such mechanisms? For instance, NASUCA states that the Commission "should not assume that preservation of the current levels of access revenues is justified without any explanation of the financial need of the carriers."[312]

100. If we conclude that alternative cost recovery mechanisms are needed, we solicit comment on the various proposals that have been submitted. The ICF proposal, for example, includes elaborate rules designed to ensure that any revenue reductions are offset by new revenue opportunities.[313] In considering the ICF and other proposals, we ask parties to address whether the Commission is legally obligated to make any transition to a new compensation regime revenue neutral for the affected carriers. Should we define revenue neutrality based on a carrier's actual earnings, the authorized rate of return of 11.25 percent, or some other measure?[314] Does this obligation extend only to incumbent LECs, or does it apply to other carriers as well? If revenue neutrality is not mandatory, what criteria should we use in calculating the revenue opportunity that should be provided to LECs? How should revenue received from other wholesale services be factored into this analysis? What about new revenue opportunities (or cost reductions) that might be expected to arise if there were no more access charges? We encourage price cap carriers, both individually and collectively, to provide data regarding the amount of revenue that would be lost if the Commission no longer permits the imposition of interstate access charges. We also encourage price cap companies to provide data regarding the cost reductions they would experience if they no longer had to pay to terminate calls on other carriers' networks.

101. Two of the proposals rely primarily on two mechanisms – subscriber charges and some form of universal service support – for offering price cap carriers the opportunity to recover costs previously recovered from IXCs through interstate switched access charges.[315] We ask parties to comment on whether the Commission should rely solely on end-user charges, or whether it also should rely on universal service support mechanisms (new or existing) to offset revenues no longer recovered through interstate access charges. If additional recovery is permitted through federal subscriber charges, how should such charges be implemented? Specifically, we question whether it is realistic to institute a regulated SLC for years to come, when market conditions may not allow carriers to charge such a SLC. Is there sufficient competition in the marketplace to allow us to eliminate the SLC cap and permit price

[311] See NASUCA Proposal at 2; Western Wireless Proposal at 18. *See also* CTIA Principles at 1-2.

[312] NASUCA Proposal at 2.

[313] *See* ICF Proposal at 51-54.

[314] *See Represcribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket No. 89-624, Order, 5 FCC Rcd 7507 (1990) (the Commission prescribes for the interstate access services of local exchange carriers an authorized, overall rate of return on investment of 11.25 percent). *See* 47 C.F.R. § 65.700.

[315] *See, e.g.*, CBICC Proposal at 2; ICF Proposal at 48.

cap LECs to charge end users whatever the market will bear?[316] Would such a finding preclude the need for any additional universal service funding for price cap carriers? If such an option is not feasible today, under what circumstances might it become feasible? We also solicit comment on the extent to which SLCs lead to inefficient charges by serving as a pricing umbrella for competitive LECs.

102. If a cap on federal subscriber charges is needed, we ask parties to comment on the level at which the cap should be set if the jurisdictionally interstate costs of providing switched access no longer are recovered from IXCs through access charges. For example, are the rate caps proposed by the ICF appropriate?[317] Parties advocating a cap on subscriber charges are encouraged to provide data regarding elasticity of demand for telephone service and the number of subscribers that would be expected to terminate service if the cost of subscribership increases. If there is evidence that increased subscription costs would cause users to terminate service, would it make sense to give carriers the option to offer calling plans targeted to low usage customers that would impose federal subscriber charges on a per-minute or per-call basis?[318]

103. We ask parties to discuss what type of findings the Commission must make before using additional universal service funding to offset lost access charge revenues. Must carriers demonstrate that they are unable to recover interstate-allocated costs in the absence of such funding? To the extent that the Commission provides additional universal service support, how should such an approach be implemented? Should additional funding be made available through existing universal service support mechanisms or is it necessary to create an entirely new mechanism? We note that some of the proposals include cost recovery through a combination of the existing universal service support mechanisms and new sources of support.[319]

104. Commenters should also address the competitive neutrality of any new proposed universal service mechanism with respect to competitive eligible telecommunications carriers. For example, some of the proposals appear to limit additional support to certain types of carriers.[320] Parties that favor additional or alternative universal service support funding should be explicit in proposing how much additional funding is needed for price cap LECs, how they calculate such amounts, and how such funding should be raised and distributed.

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[316]Under the ARIC proposal, the current SLC caps would continue, but would be redesigned to recover both non-traffic sensitive and traffic sensitive costs. ARIC Proposal at 68-69. Rural carriers would bill SLCs at the weighted average residential and business SLCs for the price cap carriers in each state. *Id*. at 68.

[317]*See* ICF Proposal at 60-63.

[318]*See* Michael H. Riordan, *An Economist's Perspective on Universal Residential Telephone Service, in*, The Internet Upheaval: Raising Questions, Seeking Answers in Communications Policy, 309-30 (Ingo Vogelsang and Benjamin M. Compaine, eds. MIT Press, 2000).

[319]For instance, the EPG proposal appears to retain the existing universal service support, while including a new additional source of support via the "Access Restructure Charge." EPG Proposal at 22. Similarly, the ARIC proposal would retain existing federal universal service support and add a new SEF. ARIC Proposal at 71-88.

[320]*See, e.g*., ICF Proposal at 73 (stating that the TNRM recovery mechanism is available only to a CETC that has lost access revenue); EPG Proposal at 22-23 (stating that the new ARC charge is available only to regulated carriers for usage of their local networks). *But see* Western Wireless Proposal at 15 (proposing new support that would be fully portable to all designated ETCs operating in a geographic area).

105. We solicit comment on alternative approaches that would give LECs the opportunity to recover costs previously recovered from IXCs through interstate access charges. Would some sort of flat-rated connection charge on IXCs, as proposed by EPG, be appropriate either as an end in itself, or as a transition to a regime that depends solely on subscriber charges and universal service support? Would it be feasible simply to allow IXCs to subscribe to a LEC's tariffed retail services, as we have done with ISPs under the ESP exemption? Parties that favor an approach based on flat-rated charges should be specific in identifying what costs should be recovered from IXCs, how these charges should be calculated, and the length of any transition period.

106. We ask parties to comment on the impact on consumers of replacing access charges with additional subscriber charges and/or universal service support. To the extent reduced access charges lead to reduced retail rates for interexchange services, what would be the net impact on consumers? Would it be necessary for the Commission to require IXCs to pass through reductions in access charges? Or is such an approach unnecessary given the competitive state of the interexchange market? How, if at all, does the growing prevalence of bundled "all distance" offerings affect the ultimate costs and benefits for end-user customers of a proposal to eliminate interstate access charges? Should we be concerned if high-volume users reap most of the benefits of such a proposal? Should additional funding for Lifeline service be made available to offset the impact of such a proposal on low-volume, low-income consumers?

b. Rate-of-Return LECs

107. As compared to price cap LECs, rate-of-return LECs derive a much greater share of their revenue from access charges. According to NTCA, rural LECs receive on average, 10 percent of their revenue from interstate access charges and 16 percent from intrastate access charges.[321] In comparison, it asserts that the BOCs receive only four percent of their revenue from interstate access charges and six percent from intrastate access charges.[322]

108. Because many rate-of-return LECs depend so heavily on access charge revenue, some of the proposals submitted in this proceeding include special provisions for these carriers. For example, under the ICF proposal, the TNRM support mechanism for rate-of-return CRTCs is based on a revenue requirement rather than on line count.[323] We seek comment on the extent to which the Commission should give rate-of-return LECs the opportunity to offset lost access charge revenues with additional universal service funding, additional subscriber charges, or some combination of the two. If we eliminate SLC caps for price cap LECs, should we do the same for rate-of-return LECs? Or is such an approach not yet justified given the more limited competition that exists in most rural areas? If we authorize additional federal subscriber charges, should such charges be subject to the same caps, if any, that apply to price cap

[321]Letter from Scott Reiter, National Telecommunications Cooperative Association (NTCA), to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-92, at 7 (filed Jan. 7, 2004) (NTCA Jan. 7 *Ex Parte* Letter). Fred Williamson states that rural LECs in Kansas receive 37 percent of their revenue from interstate access charges and 12 percent from intrastate access charges, while rural LECs in Oklahoma receive 28 percent of their revenue from interstate access charges and 42 percent from intrastate access charges. *See* Letter from Tom Karalis, Fred Williamson & Associates, Inc., to Marlene H. Dortch, Secretary, Federal Communications Commission, RM-10822, CC Docket Nos. 96-45 and 02-361, at Tab 2 (filed Jan. 7, 2004) (opposing the Western Wireless Petition on Elimination of Rate-of-Return Regulation of Incumbent LECs).

[322]NTCA Jan. 7 *Ex Parte* Letter at 8.

[323]*See* ICF Proposal at 54, 73.