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Public Service Commission

January 23, 2004

VIA ELECTRONIC FILING

Honorable Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, SW, Portals II TW-A325
Washington, DC 20554

RE: WC Docket No. 03-173, Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers

Dear Ms. Dortch:

Forwarded herewith are comments of the Florida Public Service Commission in the above docket(s) with regard to the TELRIC rules. Greg Shafer at (850) 413-6958 is the lead contact on these comments.

Sincerely,

/ s /

Cynthia B. Miller, Esquire
Office of Federal and Legislative Liaison

CBM:tf
cc: Brad Ramsay, NARUC

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C.

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
	)	

EX PARTE COMMENTS OF THE FLORIDA PUBLIC SERVICE COMMISSION REGARDING THE REVIEW OF THE TELRIC PRICING RULES

I. INTRODUCTION AND OVERVIEW

The Florida Public Service Commission (FPSC) submits these *ex parte* comments in response to the Notice of Proposed Rulemaking (Notice) released on September 15, 2003.[1] In this Notice (FCC 03-224) the Federal Communications Commission (FCC) seeks comment on its first comprehensive review of the rules applicable to the pricing of unbundled network elements (UNEs) pursuant to section 252(d)(1) of the Communications Act of 1934 as amended by the Telecommunications Act of 1996 (the Act).

The FPSC supports the FCC's tentative conclusion that the "TELRIC rules should more closely account for the real-world attributes of the routing and topography of an incumbent's network in the development of forward-looking costs" (¶ 52).[2] The 1996 Telecommunications Act requires that the prices charged for UNEs allow the providers of UNEs to recover their costs. Although "costs" are not defined in the 1996 Act, we believe as a matter of policy that sound pricing rules should be based on forward-looking costs to the extent practicable, should not require providers to

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[1] These comments address the FCC's methodology on a going-forward, prospective basis and should not be understood as prejudging in any way matters that may come before the FPSC, or affecting any pending judicial review of FPSC decisions.

[2] *Review of the Commissions Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, NPRM, WC Docket 03-173, Released: September 15, 2003.

provide UNEs at or below actual[3] costs of production (i.e., some markets-based rate of return, a reasonable profit, is proper), and should allow providers to recover a reasonable contribution to common and joint costs.

We also support a more simplified TELRIC methodology, where possible, and are hopeful that such a process will indeed improve the accuracy of pricing signals and predictability of outcomes. In addition, the FPSC believes that the initial pricing goals, adopted in the Local Competition Order to send efficient entry and investment signals to competitive local exchange companies (CLECs) and to provide incumbent local exchange companies (ILECs) with the opportunity to recover forward-looking costs of providing UNEs, remain viable, appropriate goals (¶ 39).[4]

The FPSC notes, however, that making the TELRIC methodology more reflective of real-world attributes may run counter to the objective of less variable outcomes–because the real-world firm and the market tend to change more than does the hypothetical firm. By necessity, employing a more real-world approach may yield as much or more variability from state to state than a more hypothetical approach. Topography and geographic location can dramatically impact factors such as loop length and density across and within states.

While the identified goals of UNE pricing are, again, appropriate, the FPSC submits that one must consider the possibility that efficient entry and investment signals, nevertheless, may not lead to entry in the wireline sector–for certain regions of the country (such as sparsely populated rural areas), the required economies of scope and scale may not exist. In such cases, whether there is an effective solution to bring competition to those portions of the country–be it a regulatory solution, or,

[3] Use of the term "actual" is not intended to imply that embedded costs should be used.
[4] *Local Competition Order*, 11 FCC Rcd at 15488, ¶ 672.

preferably, a market-based response–remains to be seen. We believe that non-traditional providers, such as VoIP and wireless providers, are increasingly providing competitive choices.

In response to the issues raised in the NPRM and as more fully explained in the following sections as noted, the FPSC encourages the FCC to:

- adopt the tentative conclusion that the TELRIC rules should more closely account for real-world attributes of the routing and topography on incumbents' networks in developing forward-looking costs (Section II.A.);

- maintain the pricing goals adopted in its Local Competition Order to send efficient pricing signals to CLECs and provide ILECs with the opportunity to recover forward-looking costs (Section II.A.);

- adopt the identified assumptions relating to network routing and construction:

  - a reasonable planning horizon for network upgrades,

  - account for the impact of installation activities, terrain, and density in the determination of structure sharing factors and refrain from an across the board default value, and

  - forward-looking utilizations must be tempered by recognition of real-world factors such as the relevant network's scale of operation, growth, and density, service obligations, and other real-world constraints (Section II.B.);

- recognize in the calculation of expense factors that an appropriate matching of investment components to expense categories requires a granular approach (Section II.C.);

- recognize that plant nonspecific expenses are more appropriately calculated on a per line basis (Section II.C.);

- recognize productivity gains from deployment of the new technology the incumbent expects to deploy over a reasonable planning horizon (Section II.C.);

- ensure non-recurring charges recover forward-looking costs and address CLEC concerns about upfront payments by encouraging the negotiation of flexible payment plans (Section II.D.);

- recognize that the recovery of certain non-recurring costs may best be negotiated by individual parties (Section II.D.);

- refrain from further action on resale pricing at this time (Section II.E.);
- continue to apply TELRIC pricing rules to local interconnection and reciprocal compensation pricing (Section II.F.);
- permit states and affected parties to determine the appropriate implementation plan in the respective states (Section II.G.); and
- not apply a true-up mechanism for the difference between what a competitor pays under current rules versus what that rate would be under the new rules (Section II.G.).

II. RESPONSE TO NPRM TOPICS

A. TELRIC ATTRIBUTES & UNE PRICING GOALS

In his separate statement attached to the NPRM, Chairman Powell stated, " . . . our commitment to retaining a forward-looking approach is unwavering–what we are debating is the extent to which realistic assumptions about the incumbent's network should be included in our pricing rules." This commitment appears to be consistent with one of the pricing goals adopted in the 1996 Local Competition Order–to provide ILECs with the opportunity to recover forward-looking costs. The FPSC supports maintaining this pricing goal. In addition, we support the FCC's tentative conclusion in the NPRM that the TELRIC rules should more closely account for real-world attributes of the routing and topography of ILECs' networks in developing forward-looking costs. Because we believe that the forward-looking costs of operating a hypothetical "perfectly efficient" network under the current TELRIC rules cannot match any firm's achievable, real-world costs of operating a network, we are of the view that the current model may not be the most economically rational.

The FPSC believes it is appropriate to determine costs for UNEs that reflect the real-world characteristics of ILECs' networks because UNEs are provided by the ILEC using such a network, not a hypothetical network. The appropriate cost analysis of any particular UNE should therefore reflect the current input prices and other real-world characteristics the ILEC will face in providing that UNE. For example, the incumbent's actual loop characteristics (such as length, quantity, geographic location, etc.) should be taken into account, with whatever forward-looking adjustments the incumbent intends to make during a reasonable planning horizon. We believe that incumbents' network plans generally reflect the effect, in the real world, of pressure from price caps and competitive market pressures from many different types of providers, including wireless and VoIP providers. The forward-looking network plans therefore present a solid basis to estimate efficient, forward-looking costs. Using a purely hypothetical network as the basis of cost studies for UNE pricing likely results in costs, and thus prices, that are lower than could result from any real network.

It is not surprising that prices based on a purely hypothetical network will themselves provide little or no incentive for new entrants to build their own networks, since a hypothetical forward-looking pricing methodology will likely produce prices for using the incumbents' networks that are less than the costs of building a new network. Beyond the incentive to use the least-cost option, firms strive to minimize their exposure to risk. Building facilities inherently carries investment risk and delays market entry. Furthermore, in an industry of rapidly changing technologies, the risk of selecting a technology other than the most efficient provides yet another deterrent to investment. These factors make it all the more important to send efficient pricing signals to potential entrants– another pricing goal adopted in the 1996 Local Competition Order that remains an appropriate and viable goal seven years later. Accurate pricing signals are necessary to promote development of facilities-based competition. TELRIC rules should not result in UNE prices that are artificially low (i.e., that are not reflective of operating a real-world network) such that CLECs are disincented from using a facilities-based entry strategy.

By employing cost studies that are more closely based on the incumbents' real-world networks and actual future deployment plans for these networks, TELRIC would produce a more reasonable estimate of actual forward-looking costs in a competitive market. Such analyses should incorporate a firm's prospective technology practices at its current and prospective prices, and thus exclude obsolete and inefficient technologies and network design practices. Since the methodology would yield incremental costs that would be representative of an ILEC's current network characteristics, but also be based on the ILEC's prospective, more efficient technology and design, network element prices set using these costs would be both compensatory and sustainable: compensatory because they cover the firm's forward-looking costs, and sustainable because they reflect current and prospective but attainable least-cost engineering practices.

B. NETWORK ASSUMPTIONS

As noted previously, the FPSC supports the FCC's tentative conclusion that TELRIC rates should more accurately account for real-world attributes of an incumbent's network in the development of forward-looking costs.

One option we believe would be reasonable is a network assumption–based on an incumbent's network–that incorporates upgrades as planned by the ILEC over a reasonable planning horizon. In an industry of rapidly changing technologies, the FCC should seek additional comments on what the appropriate planning horizon should be, recognizing the discretion needed by each carrier to adquately address investment and deployment strategies.

1. Technologies (¶ 67-70)

In a truly competitive market, with significant sunk costs and large portions of fixed infrastructure costs, one could reasonably expect most competitors to employ a mix of new and existing technologies. Even in an industry such as telecommunications with rapidly evolving technologies, the timing of new technology deployment is always tempered and constrained by the magnitude of current technology, cost of capital, and expected returns. While assuming a total replacement network using the most efficient technology will not yield realistic results, a hypothetical network that is too heavily weighted to current incumbent networks may not provide results that closely track what a more competitive market may produce, unless the costs factor in the incumbent's forward-looking plans over the foreseeable planning horizon, which in turn should reflect the diffusion rate of new technologies in a technology-based competitive market; similarly, today's prices must be used to capture the real-world constraining effect of new technologies.

2. Structure Sharing (¶ 71-72)

Structure sharing refers to the practice of a telecommunications provider sharing its outside plant supporting facilities, primarily poles and conduits, with other utilities. The FPSC recommends a somewhat conservative case-by-case approach to modeling structure sharing. Any assumption about structure sharing should reflect the current, real-world experience of incumbents, which would include variances depending on the type of structure and on the line density zone.

The FPSC also supports a methodology that takes into account differences in installation activities, terrain, and line density, and opposes a single across-the-board default value. There are too many variables that could affect the degree to which sharing is or is not possible. Of particular concern to us is the likely impact on low-density areas of use of a global sharing value; adoption of a uniform value could assume away a telephone company's legitimately incurred costs, even where another utility may not be present. We believe that the selection of an appropriate value must be determined on a case-by-case basis.

3. Fill Factors (¶ 73-75)

The FPSC adopted a modified BellSouth Telecommunications Loop Model (BSTLM) for the establishment of UNEs for BellSouth Telecommunications (the largest ILEC in Florida). Similar to the FCC synthesis model and the Benchmark Cost Proxy Model, the BSTLM is a model in which utilization is a result rather than an input to the modeling process. The design parameters proposed by BellSouth and adopted by the BSTLM assume a conservative 2 copper pairs per residential household and reflect the actual number of business pairs in service. The model builds the appropriate distribution cable size on that basis.

Based on this approach, the effective fill for distribution cable is determined by dividing the number of working distribution pairs by the number of available pairs placed. Thus, the design parameters on which the model is based, in large part, determine the effective fill factors from the model. Similar to distribution, the model divides the working pairs by the available pairs to determine the effective fill.

Applicable fills can and should vary by network component. Feeder cable, for example, does not come in every particular pair size but rather in discrete increments. Therefore, it is appropriate that feeder cable would have a different fill than distribution cable. Furthermore, actual design criteria for distribution cable varies according to the needs or projected needs of a particular area, even within particular states.

Of necessity, the appropriate utilization of various network components varies by circumstance and should be determined on a case-by-case basis. Forward-looking utilizations reflect the reality of the incumbents' networks, recognizing key factors such as an incumbent's engineering plans, which account for scale of operation of the company, growth, and density, as well as service requirements and other real-world considerations.

C. EXPENSE FACTORS (¶ 109-113)

The FPSC believes that computing plant-specific operation costs as a percentage of investment is appropriate; however, we do not believe a single set of factors should be applied nationwide. Labor costs are a major component of these expenses, and we believe it is self-evident that labor rates vary throughout the country. We believe any approach to estimating plant-specific expenses must allow for variations in labor costs. Furthermore, we believe any expense-to-investment ratios should be calculated for each Uniform System of Accounts (USOA) plant-specific expense account, rather than summary "roll-up" accounts.

It may be more appropriate to calculate certain plant non-specific network expenses, such as engineering, network operations, testing, and power, on a per line basis rather than attempting to ascribe them to a particular investment category. In this case as well, the FPSC believes that state-specific measures should be used to allow for variation in such factors as labor costs and that they should be calculated for each USOA plant non-specific account rather than summary "roll-up" accounts.

Consistency in the calculation methodology for forward-looking expense factors is one way to improve consistency between states. Typically there are at least three basic approaches to calculating expense factors. One uses historical data; the second is a pro forma approach which takes historical expenses, corrects for non-recurring items, and adjusts for predictable changes; and the third is an entirely hypothetical, projected approach. Here, the FPSC believes the second approach is preferable to the extent feasible.

The FPSC believes it is appropriate in principle to adjust for expected industry productivity and inflation in the calculation of expense factors. This will capture any forward-looking productivity gains associated with new technology the incumbent plans to deploy and the labor costs the incumbent actually will incur.

D. NON-RECURRING CHARGES (¶ 114-130)

The Notice identifies several issues relating to non-recurring costs and seeks comment on their resolution. The FPSC believes that it is appropriate to apply the tentative conclusion reached in ¶ 52 to non-recurring as well as recurring charges. It is incumbent upon the states to ensure that incumbents have the opportunity to recover their forward-looking, efficient costs of performing non-recurring work. The incumbent's non-recurring activities should be presumed efficient today because of competition, price caps, and ongoing oversight by regulators. Nonetheless, it should be noted that what comprises forward-looking, efficient costs has been and will continue to be the subject of many of the issues of the numerous state proceedings, and the FPSC welcomes the FCC's guidance in an effort to send more accurate pricing signals and to reduce unwarranted inconsistencies in UNE pricing.

The determination of what is a non-recurring UNE cost should be based on the consistent application of a standard set of criteria. The following questions can operate as the foundation for that determination:

- Is the cost associated with a one-time activity?
- Is the cost a direct result of a request by a CLEC?
- Is the work of a nature that it would not need to be performed again?

Once costs have been appropriately categorized as non-recurring, there remains the pricing decision of whether such costs should be recovered through non-recurring charges or recurring rates. It is possible that an ILEC could seek assurance of total recovery of its non-recurring costs if they were to be recovered in recurring rates; this could be accomplished via a volume and term agreement or a termination liability provision. We believe that an ILEC on balance, would be indifferent to how its non-recurring costs are recovered, as long as it is ensured recovery. However, we believe that it would be very complex to ensure such recovery if non-recurring costs are shifted to recurring rates.

The length of time a service remains in use by a CLEC is an important factor to consider if non-recurring costs are to be recovered through recurring rates. It is important to ensure that the non-recurring costs can be recovered and will not be foregone if the service is removed or disconnected too soon. The appropriate means to ensure proper recovery in this instance is to use a volume or term agreement or a termination liability, but again, this could involve substantial complexities.

The FCC noted in its Local Competition Order that extremely high up-front costs may constitute a barrier to entry that may be mitigated through payments over time. Barriers to entry that arise, not from misallocation of costs, but from high costs actually associated with the CLEC's request for service, ideally should not be recovered through a recurring rate. Instead, incumbents should be encouraged to negotiate terms with individual CLECs to arrange payment plans or similar mechanisms.

Accordingly, whether the magnitude of a given non-recurring charge erects a barrier to entry presumably can only be determined on a case-by-case basis. The issue of the term over which payments for non-recurring charges should be made may be best left to negotiations between the parties, so that they may select a payment plan that best fits individual needs.

E. RESALE PRICING (¶ 141-146)

The Notice seeks comment on whether further FCC action is necessary relating to rules to implement Section 252(d)(3) of the Act. The Notice cites the finding of the Eighth Circuit that the appropriate standard for determining avoided costs is not those costs that "can be avoided" but rather, "those costs that the [incumbent LEC] will actually avoid incurring in the future."[5] The FPSC agrees with that standard and does not believe any additional clarification of the statute is necessary. Moreover, we note that there has been no challenge to the existing resale rates in Florida and no request to revisit them to date.

F. INTERCONNECTION PRICING AND RECIPROCAL COMPENSATION (¶ 147-148)

Under section 252(d)(1), local interconnection is subject to the same cost-based pricing standard as UNEs.[6] The Notice seeks comment on whether there is any reason that changes to the current pricing rules for UNEs should not also apply to local interconnection provided pursuant to section 251(c)(2). In addition, the Notice seeks comment on whether the same standard should also apply to reciprocal compensation rates. The FPSC believes it is appropriate to continue to apply the same pricing standard to pricing for local interconnection and reciprocal compensation rate elements that is applied to UNEs.

G. IMPLEMENTATION ISSUES (¶ 149-151)

Finally, the Notice seeks comment on how any changes to the FCC's UNE pricing rules should be implemented by the states. Among the issues raised by the Notice are whether a national timetable should be established pursuant to which states would conduct new UNE cost proceedings to

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[5] *Iowa Utilities II*, 219 F.3d at 755.

[6] 47 U.S.C. § 252(d)(1).

reset all rates in accordance with any new rules; whether new proceedings should be resolved in a certain time period; and finally whether a true-up mechanism is appropriate for the difference between what a competitor pays for network elements under current rules versus what that rate would be under the new rules when they are implemented.

The FPSC strongly believes that the implementation mechanisms and reasonable timetables should be determined by each state. States should not, of course, unreasonably delay implementing new rules. However, states should not be required to implement any new rules in an artificially short time frame. The FPSC has recently completed UNE ratesetting proceedings (4th quarter of 2002) for the three major ILECs operating in our state. We currently have open proceedings on access charge reform and on our obligations relating to the Triennial Review Order. To hold the states accountable for completion of yet another round of fact-intensive UNE proceedings at the same time would be overly burdensome. The timing or necessity of such proceedings should be left to the states and the affected parties in each state.

Transitioning UNE rates to a new pricing standard can be accomplished in a variety of ways, and it is not necessary for the FCC to determine a "one size fits all" transition mechanism applicable to every state and circumstance. Generic proceedings may be the best result for some states and less satisfactory for others. The FPSC, as previously noted, has conducted separate proceedings for each of the three large ILECs operating in Florida. Depending on the outcome of the instant TELRIC proceeding, the affected carriers may wish to petition the state for a new proceeding immediately upon resolution or may choose to wait. Factors influencing those decisions may well vary by state, depending on the degree to which carriers are dissatisfied with current prices.

Finally, based on the record before us, the FPSC opposes the concept of a true-up. The FPSC has proceeded with a sense of urgency in all matters relating to competitive markets and would oppose a decision by the FCC that would create the necessity for a true-up mechanism. Furthermore, true-up mechanisms for regulatory purposes are generally reserved for situations where clear errors of facts or law are identified, or situations where full information is not available in a timely manner. This is not the current circumstance regarding the TELRIC pricing rules; therefore the FPSC would oppose any true-up mechanism for this case.

III. CONCLUSION

The FPSC recognizes the importance of the UNE pricing rules to the efficient functioning of a competitive telecommunications market. For that reason, the FPSC supports the FCC's tentative conclusion to make the TELRIC costing model more reflective of real-world attributes of the routing and topography in incumbents' networks in developing forward-looking costs. In order to achieve that end, we make the following recommendations:

- Maintain the pricing goals originally established in the Local Competition Order to send efficient pricing signals to CLECs, and to provide for recovery of forward-looking costs for ILECs.
- Follow the suggestions provided in the body of the comments in the areas of Network Assumptions (including fill factors, structure sharing, and technologies), Expense Factors, and Non-recurring Charges, that we believe will make the TELRIC model more reflective of the goals of the tentative conclusion;
- It is not necessary to revisit the current status of Resale rules;
- It is appropriate to continue to extend UNE pricing rules to local interconnection and reciprocal compensation pricing;
- The FPSC does not support the establishment by the FCC of a timetable for revisiting UNE pricing under potentially revised rules;

- The FPSC does not support the implementation of a true-up mechanism for a time period that may elapse between the establishment of new rules and the implementation of those rules; and

- Implementation matters are best left to the discretion of the states and the affected parties in each state.

Respectfully submitted,

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Cynthia B. Miller, Esquire
Office of Federal and Legislative Liaison

DATED: January 23, 2004