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*Via Electronic Filing*

Rosemary Chiavetta, Secretary  
Pennsylvania Public Utility Commission  
Commonwealth Keystone Building  
400 North Street – Filing Room (2<sup>nd</sup> Floor)  
Harrisburg, PA 17105-3265

Re: Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and The Pennsylvania Universal Service Fund, Docket No. I-00040105

AT&T Communications of Pennsylvania, LLC v. Armstrong Telephone Company - Pennsylvania, *et al.*, Docket No. C-2009-2098380, *et al.*

Dear Secretary Chiavetta:

Enclosed for filing please find the Exceptions of the Pennsylvania Telephone Association, which is being filed electronically in the above-captioned matter. Copies of this document has been served in accordance with the attached Certificate of Service.

If you have any questions with regard to this filing, please direct them to me.

Very truly yours,

THOMAS, LONG, NIESEN & KENNARD

By:

  
Norman J. Kennard

NJK:tlt  
attachments

cc: Administrative Law Judge Kandace F. Melillo  
James H. Cawley, Chairman  
Tyrone J. Christy, Vice Chairman  
Wayne E. Gardner, Commissioner  
Robert F. Powelson, Commissioner  
John F. Coleman, Jr., Commissioner  
Cheryl Walker-Davis, Office of Special Assistants

BEFORE THE  
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Investigation Regarding Intrastate Access :  
Charges and IntraLATA Toll Rates of Rural : Docket No. I-00040105  
Carriers, and the Pennsylvania Universal :  
Service Fund :  
  
AT&T Communications of Pennsylvania, *et al.* :  
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 :  
 v. : Docket No. C-2009-2098380, *et al.*  
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 :  
 Armstrong Telephone Company of :  
 Pennsylvania, *et al.* :

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**EXCEPTIONS OF  
THE PENNSYLVANIA TELEPHONE ASSOCIATION**

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Dated: September 2, 2010

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## I. SUMMARY OF EXCEPTIONS

The Pennsylvania Telephone Association's ("PTA" or "PTA Companies")<sup>1</sup> primary position continues to be that, until the Federal Communication Commission ("FCC") gives a clearer indication of the direction it intends to pursue, this Commission should retain the status quo. Interexchange carriers ("IXCs")<sup>2</sup> serving in Pennsylvania have enjoyed over \$500,000,000 in access savings since this Commission began reform in the *Global Order*,<sup>3</sup> and rural local rates have increased by an average of 55%.

The potential scope of the changes sketched out in the National Broadband Plan is potentially immense and will likely have profound impacts on Pennsylvania rate setting. Given the pending FCC investigation into a complete revamp of both inter- and intrastate access charges, and the impact on state and interstate intercarrier compensation, local rates and universal service funding issues, now is not the right time to reduce intrastate access rates further. Moving too soon could impose a substantial, additional penalty on Pennsylvania ratepayers, who are already net contributors to the federal universal service funds, and well

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<sup>1</sup> The Pennsylvania Telephone Association is the representative of the following companies at the above-captioned docket: Armstrong Telephone Company - Pennsylvania, Armstrong Telephone Company - North, Bentleyville Telephone Company, Buffalo Valley Telephone Company, Citizens Telecommunications Company - New York, Citizens Telephone Company of Kecksburg, Commonwealth Telephone Company LLC d/b/a Frontier Communications Commonwealth Telephone Company, Frontier Communications of Breezewood, LLC, Frontier Communications of Canton, LLC, Frontier Communications of Lakewood, LLC, Frontier Communications of Oswayo River, LLC, Frontier Communications of Pennsylvania, LLC, Conestoga Telephone & Telegraph Company, Denver and Ephrata Telephone and Telegraph Company, Hickory Telephone Company, Ironton Telephone Company; Lackawaxen Telecommunications Services, Laurel Highland Telephone Company, TDS Telecom/Mahanoy & Mahantango Telephone Company, Marianna and Scenery Hill Telephone Company, The North-Eastern Pennsylvania Telephone Company, North Penn Telephone Company, Consolidated Communications of Pennsylvania Company, Palmerton Telephone Company, Pennsylvania Telephone Company, Pymatuning Independent Telephone Company, South Canaan Telephone Company, TDS Telecom/Sugar Valley Telephone Company, The United Telephone Company of Pennsylvania d/b/a Embarq Pennsylvania, Venus Telephone Corporation, Windstream Pennsylvania, LLC, and Yukon-Waltz Telephone Company.

<sup>2</sup> They are referred to in PTA's testimony, briefs and exceptions as "IXCs," because they are complaining about the rates they are charged when handling toll calls. These companies also have other, more financially important lines of business, such as wireless carrier, cable company, broadband provider or other. While these other businesses are distorting their recommendations in this case, it is the rates they pay as an IXC that are in controversy here.

<sup>3</sup> *Re Nextlink Pennsylvania, Inc.*, Docket Nos. P-00991648 and P-00991649 (Order entered September 30, 1999) ("*Global Order*") at 54.

ahead of most states in terms of both broadband policy development and intrastate access reform. The eligible benefits, if any, that may accrue to Pennsylvania ratepayers under the Recommended Decision do not warrant undertaking this risk.

The PTA Companies have demonstrated on the record of this case that existing access rates are “just and reasonable,” compliant with all provisions of the Public Utility Code and consistent with their Chapter 30 Plans. While the ALJ found that the thirty PTA Companies should each have presented a cost study, this is not a requirement under any statute, order, or regulation and has never been previously required by the Commission. Compliance with their Chapter 30 Plans is a complete defense of existing rates. Rates set under the price caps plans “shall be deemed just and reasonable under section 1301.”<sup>4</sup> As the Plans themselves provide, “complaints against existing rates ... may be sustained only if such existing rates do not comply with the terms of this Plan.”<sup>5</sup> These provisions, at least, are sufficient to require the IXCs to then justify the rate decreases they seek.

The Recommended Decision then concludes that access reductions will benefit the public interest and recommends that access rates be dropped by 65% to an average \$.019 per minute. Yet, there is no evidence that the PTA Companies’ current average \$.048 per minute access rates have impeded, restricted, retarded or otherwise harmed the toll markets, the presumed beneficiaries of further reductions.

Nor is there any hard evidence that end use customers will benefit from further access reductions. Certainly, the access reductions sought by the IXCs from the PTA Companies (\$64 million, a 65% decrease) create an equal and corresponding local rate increase (\$7.32 per month, a 47% increase), resulting in local tariffed rates exceeding \$23.00 per month (and a billed rate of

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<sup>4</sup> 66 Pa.C.S. § 3015(g).

<sup>5</sup> See e.g., ALLTEL PA Chapter 30 Plan, Part 3.E.1., at 30-32; Denver & Ephrata Telephone Co. Chapter 30 Plan, Part 3.E.1, at 19.

over \$32.00), without any support provided from the Pennsylvania Universal Service Fund (“PA USF”). There is no calculation in the record of this case comparing the benefits to customers of lower access rates to the attendant local rate escalation. When access rates were reduced in the *Global Order*, the Commission demanded verifiable guarantees. “Customers, particularly those that stand to see their local rates increase substantially, deserve to know that they will see some relief on the other side.”

While the IXC’s assure the Commission, based upon simplistic economic platitudes, that the efficiency of competitive markets will create lower toll rates and better services to the benefit of Pennsylvania customers, no IXC (with the exception of a *de minimus*, vague and unenforceable offer from AT&T) has promised anything, but rather all have noted the Commission’s jurisdictional inability to require any sort of reduction in toll rates charged to the Pennsylvania consumers.

That access reduction will produce public benefits is accepted as an article of faith in the Recommended Decision. Yet, the IXC’s are no longer actively developing the toll market, but rather are abandoning it for reasons relating to changing technology and customer preferences. AT&T, Sprint, Verizon et al. have been in the process of abandoning the long distance market for years due to factors much more powerful than the rural local exchange companies’ (“RLEC”)<sup>6</sup> access rates. Indeed, access rates were never mentioned by them as a reason, among the many, for doing so. To the contrary, wireless, texting and the Internet, are exploding because of the convenience, unique value, applications and technological innovation they offer, not pricing.

Reductions should not occur simply because AT&T, Verizon and a few other national and international corporate “mega-carriers” are seeking to reduce their expenses and advantage

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<sup>6</sup> All of the PTA Companies have been classified by the Commission as rural telephone companies.

their corporate affiliates. The IXCs have determined that driving out wireline business is actually beneficial to their overall corporate interests and business strategy. As the IXCs seek to convince this Commission to increase the RLECs' local service rates (or simply deny the RLECs any real opportunity to recover the lost revenues), AT&T Wireless, Sprint Nextel and Verizon Wireless all stand to realize even greater competitive gains because of the accelerated line losses created by higher local rates.

Having determined, *sua sponte*, that access rates should now be cost-based, the Recommended Decision reaches the federal result (parity), but wholly fails to follow the means by which the federal rate was achieved upon the mistaken belief that the interstate rate still recovers loop costs from access customers. This is highly inaccurate. *The FCC expressly removed loops costs* from interstate access rates in 2000-2002 and shifted loop cost recovery to *both* end users (through a \$3.00 subscriber line charge increase) *and* to two, newly created federal universal service funds. The FCC did not force it all upon local ratepayers. In the Recommended Decision, however, the ALJ rejects any expansion of the PA USF to mirror the FCC's creation of its own funds.

Loop costs, to the extent costs are relevant, are a shared cost. Where this Commission has addressed access cost studies (in a pre-*Global Order* attempt and again most recently for CLECs seeking to justify rates higher than the incumbent), it has adamantly refused to push all loop costs upon the end user. Consistently, the Commission has followed the logic that both the local customer and the IXC make use of the same local network to complete both local and toll calls. "If it were not for the existence of the local network, AT&T would be required to construct at considerable expense an alternative means of access to the local customer."<sup>7</sup>

Moreover, the results are unacceptable. By excluding the PA USF as a part of the

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<sup>7</sup> *Pa. PUC v. Brezewood Telephone Co.*, 74 Pa. PUC 431, 494 (1991).

solution, the Recommended Decision would raise monthly local rates on average by \$7.32 (some will double). This creates an *average* monthly residential tariff rate of \$23.00 for the PTA Companies in aggregate and an average billing rate of \$32.07.<sup>8</sup> Some tariffed rates will be in the high twenties and low thirties. By comparison, the national average local tariffed rate is \$15.00 per month. Verizon's own Pennsylvania rural rates of \$12.00 to \$15.50, as well as its urban average rate of \$16.50, are all markedly lower.

The Recommended Decision limits its consideration to only affordability (the OCA's *maximum* affordability ceiling is \$22.00-23.00) and "gradualism" (defined as increases of \$3.50 per year, but then applied in such a way so that some companies' rates will increase by \$7.00 in the first year). The PTA submits that pushing rates to (and over) the limits of affordability and defining gradualism so as to justify first year rate increases of over 50% is in error and not sound public policy for Pennsylvania rural local ratepayers.

Other principles, including comparability and sustainability, are ignored. Setting rates by comparison is standard telephone ratemaking. Here, the continued use of benchmarking for local rates is rejected as not legally required without discussing the merits of the concept.<sup>9</sup> In the original access investigation, ALJ Schnierle found that the comparability standard applies and the *Global Order* rates were set using a Verizon-based local rate target. The PTA proposes that the comparable rate here should be based upon 115% of Verizon's urban rate, which is currently equal to \$18.94. The ALJ does not address the PTA's proposal.

Finally, there is the issue of sustainability in setting local rates. Currently, the RLEC

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<sup>8</sup> Local rates in Pennsylvania are already 55% higher than they were 10 years ago due largely to ongoing intrastate access reform. Access rates during that same period have decreased from \$.066 per minute to the current \$.048 per minute.

<sup>9</sup> The Recommended Decision ignores the contradiction that access reductions are not statutorily required either, but proceeds to do so nevertheless. Indeed, the essence of setting intrastate rates at parity with interstate rates is benchmarking.

territories are a mix of strong competition in more populated areas and less to (or none) in the more rural areas. The record shows that cable voice coverage is available to 58.5% of the total households in Pennsylvania on a *state-wide* basis and to a lesser degree in the RLECs' territories. Wireless service overlap is not complete in rural Pennsylvania either where "large gaps" in coverage still exist. Whether the degree of competition is 30, 40, or 50%, there are still substantial areas of Pennsylvania served by only one carrier -- the PTA Companies.

The dilemma is that one, unified tariffed rate is set and applied to both sectors of the RLEC's business, competitive and noncompetitive. The Commission must continue to be mindful, as it always has, of the customer who has no options, and set rates that continue to be comparable and affordable. At the same time, the rate should not be set so high that it cannot be sustained by the RLEC in the competitive areas. With little or no changes in local rates, the PTA Companies have experienced a 17% decline in access lines over the last three years.

Large increases above current rates will, quite obviously, accelerate customer migration in the competitive areas, resulting in less revenue, not more. Over the last four years, the RLECs have been able to implement less than two-fifths (2/5) of their regulatorily "allowable" (price cap) rate increases (mostly in ancillary services), and are accepting the permanent lapse of those banked revenues. Their own behavior clearly and convincingly proves that there is little or no "headroom" in the RLECs' markets for higher local rates. The RLECs, unanimously, have refused to use the "allowable" revenue increases calculated under their Chapter 30 plans to increase local rates (and their own profitability).

The dollars at risk with the recommended access rate reductions are significant, with

more than 80% of the RLECs' operating income in jeopardy.<sup>10</sup> The PTA Companies use this money, earned under their Chapter 30 Plans, to maintain and improve their networks, the only network that guarantees voice and broadband access for all. Providing universal and ubiquitously high quality voice and broadband coverage today, as only the RLECs do in their rural service areas, requires an expansive network, not only to build, but also to maintain. That in turn requires substantial and continued investment.

An outcome in which the new, higher local rates cannot be recovered in the RLECs' competitive areas is not lawful either. The IXCs assert that, if the PTA Companies cannot recover their costs in a competitive marketplace by raising local rates, then they should not be in business. The Recommended Decision accepts this "pro-competition" point of view, concluding that "[t]here simply is no substantial basis on which to conclude that the PA USF must 'guarantee' revenue replacement for RLEC access reductions to protect universal service/COLR obligations."<sup>11</sup>

However, "dollar for dollar" recovery *is* specified in their Plans and Chapter 30 requires the RLECs be provided with revenue neutrality. Not just simply in theory, but as a realistic opportunity to increase revenues. The Commission must design access reductions so that the PTA Companies have a real chance in the market to actually recover the lost revenue and not be indifferent, as is the Recommended Decision, to whether recovery will occur.

The comparative differences between the operations of the PTA Companies and Verizon are obvious in the RLECs' lack of urban/suburban service territory over which to internally support ("average down") rural rates. When compared to cable companies and wireless carriers,

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<sup>10</sup> With the loss of all "at-risk" revenues, the companies operating income of \$109 million (2008) would precipitously plummet to \$21.5 million. These figures include ALJ Colwell's recommendation that the current PA USF be eliminated.

<sup>11</sup> Recommended Decision ("RD") at 149-50.

the differences also includes the RLEC's carrier of last resort obligation and regulatory compliance. These uneven burdens have been traditionally addressed through explicit universal service funding mechanisms.

Universal service funding has been available in all the prior instances where access was reduced in Pennsylvania, and has been consistently available on the federal side as well. From the very beginning, the goal has been to *replace* the system of implicit subsidies with 'explicit and sufficient' support mechanisms to attain the goal of universal service in a competitive environment, not to shift all responsibility to local ratepayers. The ALJ dismisses these concerns, concluding that it is unreasonable to expect other carriers and their customers to fund the RLECs' operations through an expanded PA USF.

The Recommended Decision is determined to drive access to interstate levels and, having taken this aggressive view of the objective, focuses too narrowly on the means to get there. As noted, the FCC used two universal service funds to achieve the result. The *Global Order* also employed a mix of local rate increases and PA USF. The PTA has previously proposed, and continues to urge, that the Commission adopt the same rational and pragmatic approach to access rates which it utilized in 1999 (*Global Order*) and again in 2003 (Phase II).

The PTA suggests that the Commission's first focus should be on local rate levels and a comparability benchmark of \$18.94. This would be the first source of access reductions. For example, setting the traffic sensitive component of intrastate access rates at parity with interstate would result in a \$10.4 million rate reduction for the IXCs. If the Commission desires a reduction also in the CCL component (where the loop recovery is contained), then a percentage reduction that does not require that local residential rates be set higher than that \$18.94 level should be identified.



If the Commission desires greater access decreases, then the PA USF should be used. The PTA has advocated reforms to the structure of the fund itself, which include increasing the scope of contributors to include wireless and VoIP carriers as many states have done. If the Commission does not want to expand the PA USF, then a lesser access charge reduction should be accepted.

Each component is an integral part of the overall reform and provides a stable and predictable transition, which should be the Commission's objective. Certainly, the RLECs and their rural customers deserve more than a two year flash cut to 50% (and greater) rate increases, particularly where the IXCs promise nothing in return. Simply selecting "parity today" as the access rate objective and then choosing between the opposing poles of AT&T/Verizon's "all local rates" and the OCA's "all USF," as reflected in the Recommended Decision, is neither rational nor moderate.

## II. EXCEPTIONS

### A. **Exception No. 1 – Burden of Proof. The ALJ Erred When Finding That Current Access Rates Could Not Be Found Just and Reasonable (RD at 46-78; COL Nos. 10-14, 16, 20).**

The PTA agrees that the RLECs bear the *prima facie* burden to demonstrate current access rates are "just and reasonable."<sup>12</sup> The PTA takes exception, however, to the ALJ's conclusion that the RLECs could only meet this burden by submitting a detailed cost study for each of the thirty-one (31) RLECs, including CenturyLink, demonstrating that access rates do not exceed the cost of providing access service. PTA contends that the ALJ applied an erroneous evidentiary standard upon the RLECs, and, as a result, the Recommended Decision's assessment of the evidence is flawed and deficient.

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<sup>12</sup> See PTA Main Brief ("MB") at 20-21.

Moreover, the PTA disagrees with the ALJ's alternative finding that, even if the RLECs had established a *prima facie* case, the IXCs, AT&T, Verizon, Sprint, Qwest and Comcast,<sup>13</sup> presented more than co-equal evidence to demonstrate that intrastate access rates should be reduced to the interstate level.<sup>14</sup> As the ALJ's Recommended Decision notes, this is an important issue, based upon which the ALJ rejected positions taken by the PTA, OSBA and OTS:<sup>15</sup>

. . . a determination as to burden of proof can have a profound effect on the *viability* of a party's position. For example, the OSBA and OTS positions are based, at least in part, upon the failure of the IXCs to meet their burden of proof as to the unreasonableness of existing access charges. Since the IXCs no longer have the burden of proof concerning this issue, my ability to consider the OSBA and OTS positions is clearly impacted.<sup>16</sup>

The determination that the RLECs' current intrastate access rates are not just and reasonable should be reversed.

#### **1. The RLECs' Existing Intrastate Access Rates Are Just and Reasonable**

The PTA presented unrefuted evidence that the RLECs' rates are in full compliance with existing statutory and regulatory law, including their Chapter 30 Plans.<sup>17</sup> No party has argued otherwise. The PTA Companies currently charge the access rates contained in their Commission-approved tariffs, which have been found to be just and reasonable, and are in

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<sup>13</sup> PTA Direct at 32. They are referred to here as "IXCs" (interexchange carriers), because they are complaining about the rates charged for the origination and termination of toll calls. These companies also have other, more financially important lines of business, such as wireless carrier, cable company, broadband provider or other. While these other businesses are distorting their recommendations in this case, it is the rates they pay as an IXC that are in controversy here.

<sup>14</sup> RD at 74.

<sup>15</sup> RD at 50.

<sup>16</sup> RD at 50 (footnote omitted) (emphasis added).

<sup>17</sup> PTA MB at 20-42; PTA Reply Brief ("RB") at 15-38.

compliance with Sections 1301<sup>18</sup> and 1303<sup>19</sup> of the Public Utility Code.

With respect to the setting of rates (including access rates), the Plans exclude “rate base/rate of return regulation” as follows:

The PSP set forth in the Plan is a complete substitution for rate base/rate of return regulation and is the exclusive basis upon which the Company’s noncompetitive service rates are regulated on and after the date of Commission approval of this Plan. All tariff filings for noncompetitive services will be subject to review under the terms of this Plan.<sup>20</sup>

With respect to challenges to existing rates, the RLECs’ Chapter 30 Plans provide that compliance is a complete defense:

Complaints under Section 1309 of the Public Utility Code against existing rates may be filed only if such rates fail to comply with the terms of this Plan. Section 1309 shall be the exclusive basis for filing complaints against existing rates and such a complaint may be sustained only if such existing rates do not comply with the terms of this Plan. In proceedings under this part, the burden of proof shall be on the complainant to show, by a preponderance of the evidence, that the rates are not just and reasonable under Section 1309.<sup>21</sup>

Indeed, with respect to challenges to existing rates, Act 183 itself provides that compliance is a complete defense. The rates that the Commission had declared to be just and reasonable post-Global, as well as those to be subsequently established pursuant to the terms of those Plans, are deemed just and reasonable pursuant to Section 3015(g) of Act 183, which provides as follows:

(g) Rate change limitations. – Nothing in this chapter shall be construed to limit the requirement of section 1301 (relating to rates to be just and reasonable) that rates shall be just and reasonable. The annual

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<sup>18</sup> “Every rate made or demanded, or received by any public utility, or by any two or more public utilities jointly, shall be just and reasonable, and in conformity with regulations or orders of the commission” 66 Pa.C.S. § 1301.

<sup>19</sup> “No public utility shall . . . demand or receive from any person . . . a greater or less rate for any service. . . than that specified in the tariffs of such public utility applicable thereto.” 66 Pa.C.S. § 1303. Public utility tariffs have the force and effect of law and are binding on both the utility and the customer. *Pennsylvania Electric Company v. Pa. PUC*, 663 A.2d 281 (Pa. Cmwlth. 1995).

<sup>20</sup> See e.g. ALLTEL PA Chapter 30 Plan, Part 3, Price Stability Plan For Noncompetitive Services, at 20-21; Denver & Ephrata Telephone Co. Chapter 30 Plan, Part 3, Price Stability Plan For Noncompetitive Services, at 8.

<sup>21</sup> See e.g., ALLTEL PA Chapter 30 Plan, Part 3.E.1., at 30-32; Denver & Ephrata Telephone Co. Chapter 30 Plan, Part 3.E.1, at 19.

rate change limitations set forth in a local exchange telecommunications company's effective commission-approved alternative form of regulation plan or any other commission-approved annual rate change limitation shall remain applicable and shall be deemed just and reasonable under section 1301.<sup>22</sup>

Thus, under any interpretation of existing statutes, Commission orders, or the PTA Companies' Chapter 30 Plans, all of which with which the Companies remain in compliance, the Companies' existing rates and ratemaking processes were found just and reasonable.<sup>23</sup>

The PTA recognizes that the justness of rates may change over time and acknowledges the *dicta* contained in prior Commission Orders that it contemplated further changes. In particular, during the period of intrastate access reductions which began under the *Global Order* and continued under a Phase II round in 2003, the Commission stated that these changes were not the final word and that further reductions could be anticipated.<sup>24</sup> However, this statement of intent carried no substance and only indicated the direction (down) without setting forth any specific terms for doing so. PTA disputes the ALJ's apparent conclusion that the existence of the current investigation is an implicit Commission mandate for further reform unless "cost justified."<sup>25</sup> The Investigation Order in this proceeding makes no reference to cost as an issue -- only whether intrastate access (and toll) rates "should be further reduced or rate structures modified..."<sup>26</sup>

"Just and reasonable" under price cap regulation is different from traditional rate of return rate setting. The Commission has previously agreed that an inquiry into earning levels

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<sup>22</sup> 66 Pa.C.S. § 3015(g); also codified in the PTA Companies' Chapter 30 Plans (as amended under Act 183).

<sup>23</sup> See e.g. ALLTEL PA Chapter 30 Plan, Part 3, Price Stability Plan For Noncompetitive Services, at 20-21; Denver & Ephrata Telephone Co. Chapter 30 Plan, Part 3, Price Stability Plan For Noncompetitive Services, at 8.

<sup>24</sup> *Access Charge Investigation Per Global Order of September 30, 1999*, Docket No M-00021596 (Order entered July 15, 2003) ("*July 15, 2003 Order*").

<sup>25</sup> RD at 79. ("No party to this proceeding has provided any Commission citation indicating that RLEC intrastate access reform has been concluded, and the instant *Investigation* would dispel such assertions in any event.")

<sup>26</sup> *Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers, and the Pennsylvania Universal Service Fund*, Docket No. I-00040105 (Order entered December 20, 2004) at 5 (Issue 1(a)) ("*December 2004 Investigation Order*").

(i.e., revenues overall based upon rate base/rate of return standard) is not appropriate for price cap companies (“complete substitution for rate base/rate of return regulation and is the exclusive basis upon which the Company’s noncompetitive service rates are regulated...”<sup>27</sup>).

Under price cap regulation, a telephone company may pursue profitability (consistent with its utility obligations) in an increasingly competitive market, while remaining customers are insulated from the losses that a competitive market may engender.<sup>28</sup> The percent change in GDP-PI is the substitute measure of these companies’ revenue needs under alternative regulation. Indeed, access rates are included within the noncompetitive rates that are permitted to increase under the plans. To require that individual rates be set at cost would be an impermissible back door form of rate of return regulation. “If individual RLEC rates were limited to some cost basis, then the overall company revenues would no longer be price cap regulated.”<sup>29</sup>

For price cap companies the “just and reasonable” standard is judged on the basis of compliance with the terms of the Chapter 30 Plans. If compliant, as the PTA demonstrated they are, the Companies’ rates by statute are deemed just and reasonable. The Commission has previously agreed that, “[i]ndeed one clear purpose of Chapter 30 is to provide an alternative standard for judging just and reasonable rates.”<sup>30</sup> No party has asserted that any RLEC is not in compliance with those Plans, any applicable statute, or Commission order.

AT&T’s allegations that current intrastate access rates violate the “public policy” provisions of Act 183 do not rise to the level of substantive statutory legal violations. As

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<sup>27</sup> See note 20, *supra*.

<sup>28</sup> Price cap companies may not seek to recover lost revenues from remaining customers. However, this should not act as an incentive to set rates so high that competition losses are accelerated.

<sup>29</sup> PTA Surrebuttal at 10.

<sup>30</sup> *Pa. PUC v. Frontier Communications of Pennsylvania, Inc.*, Docket No. R-00984411 (ALJ Order entered December 22, 1998) at 4-5, *affirmed Pa. PUC v. Frontier Communications of Pennsylvania, Inc.*, Docket No. R-00984411 (Order entered February 11, 1999) at 10-11.

witnesses in this proceeding have agreed,<sup>31</sup> the matter of intrastate access reform is purely a matter of Commission policy and the public interest.

## 2. Access Rate Reductions Are Not Legally Required

No statute or Commission ruling *mandates* access rate decreases. The best that the Recommended Decision can say is that “Act 183’s silence about specific access levels should not be interpreted as legislative disfavor for access reductions.”<sup>32</sup> However, when the Pennsylvania General Assembly contemplated and subsequently passed Act 183, it carefully balanced accelerated broadband deployment while carefully aligning those goals with end user consumer protections, expressly including “affordable rates” and “universal service.”<sup>33</sup> Access rates are nowhere mentioned. While provision was made for revenue neutrality in the event that some level of access reductions might be authorized by the Commission, placing sizeable local rate increases on rural Pennsylvanians to the benefit of major corporations with absolutely no discernible benefit to those consumers affected was never the legislative intent of Act 183, and has the potential to undermine much of the good promulgated by the statute.

Nor has the Commission previously stated definitively that it would reduce access rates. On the contrary, the Commission consistently has held throughout this process that the existing PA USF “will continue beyond December 31, 2003, until amended through a rulemaking proceeding,”<sup>34</sup> after consideration in a further investigation “*whether* there should be further intrastate access charge reductions[.]”<sup>35</sup> Mandatory reductions were never imposed.

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<sup>31</sup> Tr. at 239 (AT&T); 319, 338-39, 349, 356-67, 384, 428, 453, 511 (CenturyLink); PTA Direct at 46; OTS Direct at 10; Sprint Rebuttal at 34; Verizon Rebuttal at 28.

<sup>32</sup> RD at 75.

<sup>33</sup> See 66 Pa. C.S. §§ 3011(2), (8) and (12).

<sup>34</sup> *July 15, 2003 Order* at 11.

<sup>35</sup> *December 2004 Investigation Order* at 1.

The Recommended Decision relies heavily on a single passage of the FCC’s National Broadband Plan (“NBP”) to justify mirroring now by this Commission, without understanding the context.<sup>36</sup> With respect to intercarrier compensation (“ICC”), the NBP primarily states that *the FCC itself* “should move carriers’ intrastate terminating switched access rates to interstate terminating switched access rate levels in equal increments over a period of two to four years.”<sup>37</sup> This is a recommendation only, with the FCC’s initial Notice of Proposed Rulemaking expected in the fourth quarter of this year. Until the specific details are known, it would be premature to anticipate the result. Further, the NBP also recommends the establishment of a benchmark residential local rate and “calculating support levels under the new CAF [replacement and redirected USF, the “Connect America Fund”].”<sup>38</sup> Thirdly, the NBP in suggesting that the FCC “should also encourage states to complete rebalancing,” also states that “some carriers may also need support from the reformed Universal Service Fund to ensure adequate cost recovery.”<sup>39</sup> Notably, the FCC’s target audience here are those states with “artificially low \$8–\$12 residential rates”<sup>40</sup> (while the current Pennsylvania RLEC average rate is much higher in the \$16.00 range). The Recommended Decision fails to acknowledge that the NBP also suggests the need for *both* a local benchmark *and* further fund support to accomplish the result. The PTA suggests that it is better for Pennsylvania to see how the FCC develops the details in its NPRM than it is to rush in ahead of it.<sup>41</sup>

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<sup>36</sup> See COL No. 20 (“AT&T has met its burden of proof with respect to the justness and reasonableness of intrastate mirroring of interstate access rates and structure. *Citizens and Wellsboro DSP Order*; 66 Pa. C.S. §§ 332(a), 1309(a); National Broadband Plan, Recommendation 8.7.”)

<sup>37</sup> FCC, National Broadband Plan at 148 (Recommendation 8.7).

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> *Id.* at 143. (Guiding Principle No. 3 “...*Reform requires federal and state coordination.* The FCC should seek input from state commissions on how to harmonize federal and state efforts to promote broadband availability.”)

If the Commission ultimately determines, as a matter of policy that, on a going-forward basis, it desires to reduce access rates to more closely approximate their interstate counterpart, the Commission may do so (and, like the FCC, should do so with support funding). However, while the Commission may choose to pursue this policy, it clearly is under no legal – statutory or regulatory – mandate to do so. Thus, absent this finding of a statutory violation, the ALJ’s ruling that the RLECs’ did not satisfy their burden of proof cannot stand because it is based upon the ALJ’s imposition of a cost of service standard as a *sine quo non*, but for which there is neither statutory nor regulatory support.

Thus, after the PTA’s evidentiary showing that existing rates were set by the Commission in compliance with existing law, the burden of proving the necessity of further rate decreases fell squarely upon the IXCs.

**3. A Cost Study is Not a Condition Precedent to the RLECs’ Satisfaction of Their Burden to Prove the Justness And Reasonableness of Intrastate Access Rates**

The gravamen of both this investigation and AT&T’s complaint was never whether the rates were or should be cost-based, but rather *whether* rates should be reduced further and, if so, how far. The IXCs principally claim that, because access rates are not imposed equally upon all providers (including, particularly, wireless carriers under FCC rulings), access rates are anti-competitive and discriminatory. AT&T also contends that, even if RLECs’ access rate were just and reasonable “when they were last set,” they are no longer because the market “has changed so substantially” since then.<sup>42</sup> AT&T has recognized this investigation not as a mandated reduction-absent-support matter, but rather “*whether* the RLECs’ intrastate access charges

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<sup>42</sup> AT&T MB at 17.



should be reduced to mirror the interstate access charges.”<sup>43</sup> This is substantively a far different inquiry than whether cost studies justify the rates.

In setting this next access investigation phase for hearing, the Commission did not suggest a cost standard on the RLECs to justify their existing rates. Rather, the Commission determined it would “reexamine[e] the area of intrastate carrier access charges for the RLECs” while balancing the “intention . . . to gradually lower intrastate access charges [while recognizing the mandates of Chapter 30] require that local service rates be reasonable and affordable in all areas of this Commonwealth.”<sup>44</sup> At no point did the Commission state cost studies would be required or that the objective of this case is to set cost-based rates. Cost-of-service is not even listed as an issue for investigation.

The ALJ’s observation that “generally” parties present cost data to establish the reasonableness of individual rates was framed within her familiarity of the historic public utility regulatory framework.<sup>45</sup> That framework never existed for the RLECs, and the Commission has *never* imposed the requirement of cost studies on the RLECs in achieving intrastate access reform.

There is no legal requirement that state access charges be set at cost. Act 183, as the ALJ acknowledges, is completely silent on the subject. Cost is not and has never been this Commission’s relevant pricing standard when setting RLEC revenues or designing specific rates. Cost-based rates have never been required.<sup>46</sup> The Commission has never stated that all implicit subsidies must be removed, let alone established how the subsidy, if any, could be defined. The

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<sup>43</sup> *Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund*, Docket No. I-00040105 (Order entered August 5, 2009) at 16 (“August 2009 Investigation Order”) (characterizing AT&T’s position) (emphasis added).

<sup>44</sup> *August 2009 Investigation Order* at 18, 20.

<sup>45</sup> RD at 75.

<sup>46</sup> The Commission only indicated its desire to reduce access “closer to cost.” *December 2004 Investigation Order* at 3. Cost has never been set as *the* objective.

Commission, in approving the RLECs' Plans, rejected AT&T's proposal that "above-cost access charges" be proscribed.<sup>47</sup>

Similarly, there is no federal requirement that states adopt access rates in relation to costing theory. As the 10<sup>th</sup> Circuit agreed: "The [FCC] has repeatedly stated that the [TCA-96] does not mandate that states transition from implicit to explicit subsidies."<sup>48</sup>

Congress intended that the states retain significant oversight and authority and did not dictate an arbitrary time line for transition from one system of support to another.... Nor did Congress expressly foreclose the possibility of the continued existence of state implicit support mechanisms that function effectively to preserve and advance universal service.... we will not disturb the Commission's statutory interpretation.<sup>49</sup>

Nevertheless, the Recommended Decision rules that the RLECs should have presented "cost data to establish that rates are not excessive in relation to costs."<sup>50</sup> This is in contravention of the ALJ's explicit recognition that "*both the RLECs and IXCs agreed that [cost] information was unnecessary to resolve the issues.*"<sup>51</sup> The ALJ's requirement of cost studies wrongly influenced her evaluation of the evidence:

Absent a conclusive legal determination of rate reasonableness and absent any cost studies, the RLECs focused on the revenue support provided by access rates for RLEC compliance with the regulatory and legislative priorities of COLR/universal service and broadband service. ... I am unaware of relevant cases, and none have been cited to by the RLECs, wherein regulated rates have been determined to be just and reasonable solely because any excess amount was necessary to provide affordable rates to other classes of customers.<sup>52</sup>

Citing *Lloyd*,<sup>53</sup> the ALJ supported this erroneous assessment of the evidentiary burden by stating that in a Commission-initiated investigation into rates, the party with the burden of proof

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<sup>47</sup> *Re: Armstrong Telephone Company-Pennsylvania v. Pa. PUC*, 2000 WL 350440 at \*22 (Pa. PUC) (reciting AT&T Exceptions at 5).

<sup>48</sup> *Qwest v. FCC*, 398 F.2d 1222, 1231 (10<sup>th</sup> Cir. 2005).

<sup>49</sup> *Id.* at 1232 (citations omitted).

<sup>50</sup> RD at 75.

<sup>51</sup> RD at 75 (emphasis added).

<sup>52</sup> RD at 75-76 (emphasis in original).

<sup>53</sup> *Lloyd v. Pa. PUC et al.*, 904 A.2d 1010, 206 Pa. Cmwlt. LEXIS 438 (2006) ("*Lloyd*").

“[g]enerally . . . presents cost data to establish that rates are not excessive in relation to costs.”<sup>54</sup>

*Lloyd* is acknowledged by the ALJ to be “distinguish[ed from] the instant situation, in many respects[.]”<sup>55</sup> *Lloyd* involved a voluntary proposed increase in rates filed by PPL under Section 1308 of the Public Utility Code,<sup>56</sup> a section specifically repealed as to ILECs under the original Chapter 30 law in 1993, and which remains repealed under Act 183.<sup>57</sup> Moreover, the requirement of cost-of-service pricing was founded in Chapter 28 of the Public Utility Code, which applies only to the electric industry. As Commonwealth Court noted in reversing the rates set for PPL: “Section 2804(3) of the [Electric] Competition Act mandates rates for services as unbundled charges for transmission, distribution and generation and requires that rates and rate structures be set for each service primarily on a cost-of-service study.”<sup>58</sup> The electric statutory rate setting scheme at issue in *Lloyd* is clearly inapplicable to the RLECs here.

The PTA thoroughly documented the Commission’s prior difficulties in defining cost studies for the telephone industry and its subsequent discontinuation of them.<sup>59</sup> The Commission’s efforts to develop a cost methodology during the latter half of the 1990’s became so bogged down in a battle of the cost studies that the Commission abandoned the effort -- never to take it up again. As the PTA’s witness Gary Zingaretti explained:

The Commission had to sort through no fewer than four models: (1) the Bell Model; (2) the AT&T/MCI Hatfield Model, including what those parties subsequently modified and introduced as an “improved” version which alleged to incorporate aspects of Sprint’s model but was also alleged to be a wholesale alteration intended to produce low USF requirement (and which in fact did produce some of the lowest basic service costs); (3) the Sprint Benchmark Cost Model (BCM), which was also later reintroduced by Sprint as an “improved” BCM 2; and (4) the OCA’s Johnson Cost Model.

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<sup>54</sup> RD at 75 (emphasis added).

<sup>55</sup> RD at 76.

<sup>56</sup> 66 Pa.C.S. § 1308.

<sup>57</sup> 66 Pa. C.S. § 3019(h).

<sup>58</sup> *Lloyd*, 904 A.2d at 1020.

<sup>59</sup> PTA MB at 59-67. *See also* PTA Surrebuttal at 3-9.

Of course, as the Commission acknowledged, each respective sponsor claimed its model was superior to the rest. Some models used embedded costs (e.g. the Bell model as described by others, although Bell insisted it used forward looking costs), while others used TSLRIC (or forward looking costs).<sup>60</sup>

In attempting to reconcile these battling cost studies in its Universal Service Order, the Commission defined the local loop as a joint cost and not a direct cost of local service.<sup>61</sup> The result was not satisfactory. “Even that model pushed what the Commission considered to be too much revenue responsibility on the local ratepayer and setting access upon any cost model was never adopted... The reality is that there is no accepted cost methodology upon which the RLECs could develop a study.”<sup>62</sup>

Instead, the Commission adopted a practical revenue-based solution in the 1999 *Global Order* and again in 2003.<sup>63</sup> It approved an access reform plan that reduced and reformulated access rates on a revenue-neutral basis, *and* established a PAUSF that provided for universal service support based upon the revenues lost as a result of the access reductions.<sup>64</sup> Phases I and II of RLEC access reform were not based upon individual RLEC cost studies or individual review of access line densities.<sup>65</sup> While the PTA’s proposal adhered to these same standards in this third phase of the investigation, it was derailed by the ALJ’s interjection of a new standard.

Finally, the ALJ acknowledged the “crucial universal service/COLR and broadband public policy objectives in telecommunications which distinguish the instant situation” from *Lloyd*,<sup>66</sup> but in the absence of a cost study, these costs were ignored. A cost study to demonstrate

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<sup>60</sup> PTA Surrebuttal at 6.

<sup>61</sup> *Formal Investigation to Examine and Establish Updated Universal Service Principles and Policies for Telecommunications Services in the Commonwealth*, Docket No. I-00940035 (Order entered January 28, 1997) at 83.

<sup>62</sup> PTA Surrebuttal at 6-7.

<sup>63</sup> *Id.*

<sup>64</sup> *Id.* at 4.

<sup>65</sup> *Id.* at 4.

<sup>66</sup> RD at 80.

this simple fact, long recognized by this Commission, is unnecessary. Nor can such a study be performed. Sprint's witness, Mr. Appleby, the party that raised this issue, could not describe how COLR costs would be measured.<sup>67</sup> As the PTA's witness testified "I have never seen the cost of the COLR obligation identified by any type of cost study and would not know how to do so without separate account tracking and special accounting systems, which do not exist."<sup>68</sup> The task is made more difficult not just because the areas of competition are imprecisely defined, but also because the "costs" themselves are undefined and an appropriate methodology has never been set.<sup>69</sup>

Simply because the cost of providing COLR service may be impossible to accurately calculate, does not mean it does not exist.<sup>70</sup> Nor does the inability to measure the cost lead to the conclusion that the costs are inconsequential.<sup>71</sup> Providing ubiquitous high quality coverage (voice and broadband), as only the RLECs do, requires an expansive network, not only to build but also to maintain, and that in turn requires substantial investment.

#### **4. The Purported Public Interest Benefits of Further Access Reform Are Overstated**

##### **i. Impact on Competition**

The ALJ adopted the IXCs' economic theory that, under the current \$.048 per minute access rates (state RLEC average), "consumers are being denied the real benefits of competition."<sup>72</sup> "Reductions in access costs will lead to lower long-distance rates."<sup>73</sup> A

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<sup>67</sup> PTA Ex. GMZ-17.

<sup>68</sup> PTA Surrebuttal at 30.

<sup>69</sup> PTA Direct at 29.

<sup>70</sup> *Id.*

<sup>71</sup> Sprint Rebuttal at 56.

<sup>72</sup> FOF Nos. 10; *See also* FOF No. 20.

<sup>73</sup> FOF No. 21. The Recommended Decision does not note that only AT&T has made any commitment to do so, but does recognize that AT&T's proposal is limited to reduce its "In-State Connection Fee (ISCF) and prepaid calling card charges." FOF No. 22. The Recommended Decision does not discuss the *de minimus* value to the customer

reduction to an average RLEC access rate of \$.019<sup>74</sup> per minute (a 65% reduction) is recommended.

To find this huge windfall to access customers, the Recommended Decision proposes that local rates to rural customers be increased by almost \$8.00 (50%) to a *minimum* tariff rate of \$23.00, resulting in a billed rate of \$32.00 for the PTA Companies' basic local service.<sup>75</sup> With the exception of AT&T's *de minimus* claim that it will reduce its "in state service charge" by pennies, no IXC has promised anything, but rather has noted the Commission's jurisdictional inability to require any sort of reduction in toll rates charged to the Pennsylvania consumers.<sup>76</sup> That toll reductions and other benefits will be forthcoming is accepted on faith. There is no calculation in the record of this case demonstrating that the benefits to rural customers of lower toll rates will be anywhere near equal the attendant local rate increases.

The IXC's claims of consumer benefits are based solely upon the generic Economic 101-level theory that "decreases in the incremental costs of producing a service lead to a decrease in retail prices of that service, and the lower prices will, in turn, stimulate demand."<sup>77</sup> This abstraction, not actual evidentiary proof of benefits, is what the ALJ relies upon in concluding that a beneficial market impact will result.<sup>78</sup> The facts are much different.

Toll customer benefits were not forthcoming during the 2003 access reductions, where the IXCs refused to identify the flow back of access reductions, claiming that they were "unable to verify the access reductions made" and questioned the Commission's legal authority (since

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compared to the \$64 million in local rate increases proposed. The Recommended Decision bases its conclusion largely on AT&T's testimony, which was long on economic theory and short on facts. See PTA RB at 6-7 and 20.

<sup>74</sup> PTS Direct at 16 and Exh. GMZ-8.

<sup>75</sup> FOF Nos. 72-74. The Recommended Decision equivocates on this point, stating that, "I am not treating the \$23.00 rate as a benchmark for purposes of triggering PA USF support." RD at 162. Instead, the question of whether even higher rates should be required or USF support provided beyond that level should await the outcome of the PUC rulemaking recommended by ALJ Colwell. *Id.*

<sup>76</sup> 66 Pa. C.S. §3018(b)(1).

<sup>77</sup> AT&T Direct at 42.

<sup>78</sup> See e.g. FOF Nos. 20-22.

IXC toll rates are not subject to Commission regulation).<sup>79</sup> After the RLECs' Phase II USF/Access Reform approved in the Commission's *July 15, 2003 Order*, which included additional RLEC access reductions in excess of \$20 million, AT&T actually *raised* rates for its all-distance bundles in Pennsylvania, anywhere from \$2.00 to \$5.00, and also increased the monthly recurring charge on many plans, typically by either \$1.00 or \$2.00.<sup>80</sup> For the ensuing period, 2006 through 2008, AT&T's long distance per minute prices actually increased from 3.8 cents to 4.4 cents, despite the fact that during this time period RLEC access rates were stable.<sup>81</sup>

Nor is this case any different, since the IXCs have refused to explain, much less commit to, any real benefits in the toll market. In terms of guaranteeing to the Commission that tangible benefits will flow through to customers in exchange for higher local rates, the carriers have done no more than continue to offer up more economic theory and platitudes.

- **AT&T.** AT&T is most blunt, saying “it would be premature for AT&T to commit to any price reductions.” Espousing “basic economics principles,” AT&T admits that “all firms, even a pure monopolist, completely unconstrained by government regulation, *will maximize profit*” but suggests that long distance service prices “would be expected to fall[.]”
- **Comcast.** Exaggerating the position of the RLECs as carriers with “substantial market power” vis-à-vis Comcast, Comcast dismisses the “pass-through issue [as] a red herring” that is “irrelevant” and “should not be factored into this proceeding[.]” Instead, Comcast asks the Commission to “accept the logical policy judgment” that it will do the right thing and pass through benefits to consumers.
- **Sprint.** Offering nothing concrete, Sprint describes “potential consumer benefits” suggesting that carriers “*could* . . . expand service coverage, improve service quality, improve customer care or develop new products and services the customers will want” while simultaneously suggesting that “[a]ll consumers benefit by competitive choice.”
- **Verizon.** Similarly offering zero concrete benefits, while also warning the Commission it has no authority at all to even consider imposing the type of pass-through commitment required in the *Global Order*. Verizon urges the Commission

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<sup>79</sup> PTA Surrebuttal at 52-53.

<sup>80</sup> PTA MB at 24, citing PTA Ex. GMZ-15.

<sup>81</sup> PTA MB at 35, citing AT&T Direct at Ex. H.

to rely solely on competition to “ensure that such benefits [e.g. advanced technology, improved service quality or customer service, new features/services] are passed along to consumers in one way or another[.]”<sup>82</sup>

Beyond these platitudes, the *only* specific benefit offered by the IXC’s is AT&T’s offer to reduce (by an unspecified amount, but pennies) its “instate connection fee,” a charge implemented after the 2002 access reductions. In the PTA’s opinion, this “offers very little to very few.”<sup>83</sup> “AT&T refused to disclose the number of customers receiving this reduction as well as the total annualized access expense reductions AT&T expected to receive.”<sup>84</sup> The reduction in rate for AT&T’s customers cannot, however be substantial. Only those customers subscribing to AT&T’s stand-alone long distance service (the same service that AT&T abandoned in 2004 allowing customers to “dwindle away over time through churn”<sup>85</sup>) will see a benefit from that small reduction. Finally, even if the entire fee were eliminated, not just reduced, it would not begin to even remotely approximate in value the level of local rate increase being proposed on RLEC customers in this case,<sup>86</sup> nor is it likely to match or even approximate in magnitude the amount of access savings that AT&T will realize.<sup>87</sup>

Nor are any meaningful benefits likely to be realized in toll rates, as the IXC’s are no longer actively developing the toll market, but rather are abandoning it. The PTA demonstrated, through the IXC’s own words, that AT&T, Sprint, Verizon et al have been in the process of abandoning the long distance market for years due to factors much more powerful than RLEC access rates. These forces primarily include changing technology and customer preferences. In a 2005 declaration before the FCC, AT&T explained its 2004 decision to abandon the local and

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<sup>82</sup> PTA Surrebuttal at 53-54 (record citations in original omitted).

<sup>83</sup> PTA Surrebuttal at 51.

<sup>84</sup> PTA Surrebuttal at 50.

<sup>85</sup> PTA Ex. GMZ-15 at ¶ 9.

<sup>86</sup> PTA Direct at 37.

<sup>87</sup> PTA Surrebuttal at 50.



long distance market as owing to a variety of reasons – none being rural intrastate access rates. Competition from “powerful competitors” like Verizon Wireless, Comcast and other lightly or wholly unregulated VoIP providers, as well as Internet functionality including email, instant messaging and social networking, and from the all-you-can-eat wireless package plans, were all cited reasons that contributed to AT&T’s decision to abandon toll service.<sup>88</sup> AT&T’s filings before the SEC likewise demonstrated that AT&T intends to place little to no more investment into the wireline segment because of a shift in technology.<sup>89</sup> The story is no different for the other aligned parties. It is more accurate to presume that IXC’s access savings will flow directly to the IXC for whatever purposes chosen.

When access rates were reduced in the 1999 *Global Order*, the Commission demanded verifiable guarantees from the IXCs that the benefits would be flowed through to customers, refusing to accept the economic platitudes again now proffered by the IXCs.<sup>90</sup> “Customers, particularly those that stand to see their local rates increase substantially, deserve to know that they will see some relief on the other side.”<sup>91</sup>

Reductions in the intrastate access charges of the RLECs to their interstate levels will produce annual savings of \$64 million to these national and international mega-carriers, an inconsequential amount to them, but immensely important to the RLECs.<sup>92</sup> This “rain in the

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<sup>88</sup> PTA MB at 23-25.

<sup>89</sup> PTA Direct at 32-44, quoting *In the Matter of International Comparison and Consumer Survey Requirements in the Broadband Data Improvement Act, A National Broadband Plan for Our Future, Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion*, GN Docket Nos. 09-47, 09-51, and 09-137, Comments of AT&T Inc. on the Transition from the Legacy Circuit-Switched Network to Broadband, filed December 21, 2009 (“*AT&T FCC Network Comments*”) at 2 (emphasis in original).

<sup>90</sup> *Global Order* at 54 (“In order to carefully monitor the extent to which customers receive toll rate reductions due to the access charge reductions ordered herein, we shall require all IXCs that experience access charge reductions as ordered herein, to file an annual report with the Commission demonstrating how the access charge reductions have flowed through to the appropriate classes.”)

<sup>91</sup> PTA Surrebuttal at 54.

<sup>92</sup> AT&T and Verizon are huge, “mega-carriers” compared to the Pennsylvania RLECs. Nationally, in 2007 the holding companies of these top two ILECs accounted for 76% of the local loops. By revenue, AT&T is the largest

desert” will have little or no effect on the promotion of wireline toll competition in a market that no longer exists in any meaningful way. On the other hand, there is no question that the mega-carriers are urging \$64 million in rate increases on local service without any countervailing public benefit.

## ii. Arbitrage Reduction

The only other basis offered in the Recommended Decision to support the finding of public interest benefits is a claimed reduction in rate arbitrage.<sup>93</sup> AT&T postulated that interstate parity “will help to avoid or mitigate problems associated with various arbitrage schemes.”<sup>94</sup> True, arbitrage is a problem for some carriers.<sup>95</sup> However, where carriers attempt to skew the compensation scheme, the RLECs have sought to address these problems through enforcement.<sup>96</sup> To the extent that AT&T has claims regarding “traffic pumping,” although not arbitrage, it should raise those in the same fashion.<sup>97</sup>

The remedy for arbitrage is to enforce existing regulations and requirements that carriers properly and fully identify their traffic, that tandem providers only switch traffic for which the proper carrier identifying information is included, and that carriers pay for traffic they terminate on the RLECs’ networks. Arbitrage between inter and intrastate compensation is *one* reason to

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communications holding company *in the world*. Within the telecommunications industry, Verizon, Sprint, and Comcast are ranked 2<sup>nd</sup>, 3<sup>rd</sup>, and 4<sup>th</sup>, respectively, behind AT&T, which is 1<sup>st</sup>, among the Fortune 500 telecommunications companies, and 17<sup>th</sup>, 64<sup>th</sup>, and 68<sup>th</sup>, respectively among all 2009 Fortune 500 companies. Of the 32 RLECs in this proceeding, only Embarq (now CenturyLink) and TDS made the top 500, near the bottom at 405<sup>th</sup> and 465<sup>th</sup>, respectively. PTA Direct at 31.

<sup>93</sup> RD at 77.

<sup>94</sup> AT&T MB at 27.

<sup>95</sup> Inter/intrastate (Percent Interstate Use or “PIU”) arbitrage is only one form of access avoidance. Some carriers also disguise traffic as local or decline to include their carrier identification so the call cannot be billed to them. Other carriers simply refuse to pay, a course previously pursued by Sprint. PTA Direct at 45.

<sup>96</sup> *Palmerton v. Global NAPs*, Docket No. C-2009-2093336, is an example of a complaint proceeding enforcing compensation rules.

<sup>97</sup> PTA RB at 32-33.

bring the two closer to parity, but in a way that is moderate and rational and recognizes all other competing factors. Arbitrage, in and of itself, is not a basis for lowering intrastate access rates.

**B. Exception No. 2 – The Recommended Interstate Access Rates Do Not Recover Costs. The Recommended Decision Erroneously Concludes That the Intrastate Access Rates Should Match Interstate Access Rates Without Matching the Interstate Methods of Achieving the Interstate Rate Level (RD at 21, 90-93; FOF Nos. 30-35, 39, 41, 43, 46 and 89; COL Nos. 20, 23 and 30).**

Having erroneously concluded that only cost-based access charges are “just and reasonable,” the Recommended Decision next asserts that interstate access rates affirmatively met this criteria and should be adopted.

First of all, I note that the interstate rates sought to be mirrored are already approved access rates that are currently being charged by the RLECs. A prima facie case of reasonableness of these rates for mirroring purposes was established by AT&T, through testimony (which was un rebutted) that there is no material technical difference between the termination of an interstate long distance call and the termination of an intrastate long distance call. Also, AT&T obtained an acknowledgement from PTA’s witness, in effect, that interstate access rates cover their costs and provide a reasonable return. Tr. 608-609. In addition, at the interstate rate level, intrastate access rates will still include a contribution to the local loop, according to AT&T’s un rebutted evidence, and this serves to address the OCA, OSBA and OTS concerns that access charges contribute to the costs of the local loop.<sup>98</sup>

These assertions are incorrect.

Interstate access rates do not include any recovery of local loop costs. While the federal jurisdiction has excluded loop costs from interstate access rates, it also allocated a substantial portion of loop cost, not recovered from the consumer, to the federal universal service fund.

By forcing local rates to absorb the entire difference between intra and interstate access rates, without assigning any revenue recovery to the PA USF, the Recommended Decision compels local ratepayers to pay for the entire amount of state loop costs, contrary to prior Commission rulings and fair rate design. By denying any PA USF recovery, the ALJ ignores the

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<sup>98</sup> RD at 90-91.

method by which the FCC achieved those lower interstate rates which are being used as the intrastate target. If Pennsylvania is to mirror interstate rates, including the carrier common line (“CCL”) charge (which is not advisable), then, so too, it must mirror the interstate means used to accomplish that result.

Numerous basic factual disconnects are reflected in the Recommended Decision. First is the (only partially correct) observation that “at the federal level, loop costs are not recovered through access charges to LECs’ *competitors* but rather from the LECs’ own customers.”<sup>99</sup> Then, two sentences later, the Recommended Decision correctly notes that: “In addition, a new Universal Service Support mechanism was established” in the FCC’s *CALLS Order*.<sup>100</sup> This conclusion is then at odds with other findings, such as: “Even at the level of parity with interstate access charges, the RLECs’ intrastate access charges would still include a contribution to the cost of the local loop.”<sup>101</sup> And else where, as inconsistently, that “[t]he RLECs’ interstate rates cover their costs and provide a reasonable return.”<sup>102</sup> There are several layers of confusion to deconstruct.

First, however, it is important to understand that the principle difference between inter and intrastate access rates today is the CCL element, which is *only* contained in *state* rate design. State access rate design is a combination of usage-based (traffic sensitive or “TS”) rates and the monthly flat CCL rate (non-traffic sensitive or “NTS”).<sup>103</sup> The *Global Order* agreed with the

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<sup>99</sup> RD at 21 (there is no record citation for this statement).

<sup>100</sup> See discussion of the MAG and CALLS orders, *infra*.

<sup>101</sup> FOF No. 31 (citing AT&T St. No. 1.3, pp. 6, 8).

<sup>102</sup> FOF No. 30 (citing Tr. 608-09).

<sup>103</sup> The *Global Order* uses the terms “traffic” and “non-traffic sensitive”: “In providing switched access for the completion of a toll call, a LEC will incur both non-traffic-sensitive (NTS) costs and traffic-sensitive (TS) costs. NTS costs are those associated with providing and maintaining the local loop. They consist of the facilities required to connect the customer’s premises to the local central office. NTS costs are not dependent on the number or length of telephone calls and cover parts of the local telephone network such as cables and poles. TS costs, on the other hand, vary with the amount of usage of the telephone network. They cover the costs of, for example, the switching equipment that must be sized to meet the volume and length of calls.” *Id.* at 12.

RLECs' position to mirror their interstate traffic sensitive (i.e., variable) charges (i.e., the per minute switching and mileage based rates). As to the non-traffic sensitive component (i.e., the non-variable loop component), the Commission restructured the rate to a flat-rated carrier charge -- the CCL -- and targeted an intrastate monthly rate of \$7.00 per line.<sup>104</sup>

This state CCL is *the* only principal difference between federal and state access rate elements billed to carriers. The PTA Companies' interstate access rates (in all cases except one) are lower than their intrastate counterpart, *but only* when the state CCL is included in the calculation. Half of the PTA Companies' intrastate traffic sensitive rates are actually lower than their interstate TS rates, and would have to be increased to achieve TS rate parity.<sup>105</sup> Across all of the PTA Companies, mirroring just the traffic sensitive component (which is the component that the Commission calibrated in 1999 and 2003) would reduce aggregate access revenues by \$10.4 million<sup>106</sup> as compared to the \$64 million total reduction if the CCL is also eliminated.

The CCL is an intentional and integral element of Pennsylvania access rate design, as the Commission has previously explained: "The Carrier Common Line Charge compensates the [RLEC] for the use of its local loops by Interexchange carriers in the origination and termination of long distance calls."<sup>107</sup>

The question presented by THE Recommended Decision is whether the IXC's, as users of access services, should continue to pay for a portion of the RLECs' fixed, non-variable network costs. The Commission has consistently held that it should. As far back as 1991, the Commission refused to eliminate loop costs from access charges, despite AT&T's arguments to

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<sup>104</sup> *Global Order* at 47.

<sup>105</sup> PTA Direct at 14. The Recommended Decision incorrectly finds that the TS intrastate switched access rates "range from about one (1) cent to as high as eleven (11) cents per minute for either originating or terminating access." FOF No. 2 (citing AT&T St. No. 1.0, p. 34). These rates are a combination of both the traffic sensitive *and* CCL elements.

<sup>106</sup> PTA Ex. GMZ-9; PTA Direct at 14.

<sup>107</sup> *Pa. PUC v. North Pittsburgh Telephone Company*, Docket No. R-00016681, (Order entered November 30, 2001) at 2 (footnote 1).

the contrary:

There is no dispute that both the local customer and AT&T make use of the same local network to complete both local and interLATA calls. If it were not for the existence of the local network, AT&T would be required to construct at considerable expense an alternative means of access to the local customer. We find that CCLC is the cost of compensating [the RLEC] for the use of the common line, and as such, CCLC clearly pays for a service received by AT&T. Thus, dial tone line costs are joint costs.<sup>108</sup>

In 1995<sup>109</sup> and again in 1996,<sup>110</sup> the Commission held that 100% of dial tone line costs cannot be solely allocated to local exchange customers.

In its 1997 generic ruling, the Commission defined the local loop as a “joint cost” and not a direct cost of only local service:

We do not find the arguments of Bell’s expert witness Dr. Kahn persuasive on this point. In particular, we do not accept the basis of Dr. Kahn’s argument that because the loop is needed for local service and the incremental cost of the loop does not increase to provide other services, that its full cost must be attributed to local service. This same argument could be made with respect to toll service. Since the loop is necessary to provide toll service, it would at the same time be argued that the full cost should be allocated to toll, and in doing so the incremental cost to provide local service would be zero.<sup>111</sup>

Thus, in 1999 when the current rate design was established in the *Global Order*, the CCL was designed to represent this element - the IXC’s share of the RLEC’s fixed costs.

The Commonwealth Court, in the appeals taken from the *Global Order*, affirmed the Commission, concluding that access charges should not be reduced so as to eliminate loop recovery and rejecting AT&T’s argument that the Commission was compelled to do so:

The Office of Consumer Advocate responds to AT&T by submitting that there is

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<sup>108</sup> *Pa. PUC v. Brezewood Telephone Co.*, 74 Pa. PUC 431, 494 (1991).

<sup>109</sup> *Formal Investigation to Examine and Establish Updated Universal Service Principles and Policies for Telecommunications Services in the Commonwealth*, Docket No. I-00940035 (Order entered September 5, 1995) at 12.

<sup>110</sup> *Pa. PUC, et al. v. Bell Atlantic-Pennsylvania, Inc.*, Docket No. R-00963550 (Order entered December 16, 1996), at 23-24.

<sup>111</sup> *Formal Investigation to Examine and Establish Updated Universal Service Principles and Policies for Telecommunications Services in the Commonwealth*, Docket No. I-00940035 (Order entered January 28, 1997) at 83.

no legal authority requiring the PUC to reduce access rates to the incremental cost of access service. OCA witnesses testified that such a reduction could require customers other than the long distance carriers to pay all of the joint and common costs of the network and therefore should be rejected. The logic of that analysis commends it . . . the cost of excessively priced elements must be reduced. . . , but not so greatly as to eliminate the support such revenue provides to other areas of the system that need that support.<sup>112</sup>

Continuing, the Court also expressly affirmed the “soundness” of the Commission’s position that “users of all services, including access, should share in the payment of total network costs, with the cost of the loop included as an element of that total network.”<sup>113</sup>

The LECs, both incumbent and competitive, as well as the statutory advocates, have consistently argued that the loop is shared. Verizon argued in its own access proceedings against the elimination of the intrastate common carrier charge.<sup>114</sup> The CLECs have also argued the same, notably both CTSI and Penn Telecom, in complaint proceedings brought against them by Verizon wherein Verizon attempted to impose an “incremental cost” theory.<sup>115</sup>

Nor has the Commission moved away from its position that loop is a shared cost. In its most recent discussion of the issue, in the context of a challenge by Verizon to a CLEC’s access rates, the Commission stated:

Traditionally, the Commission has treated local loop costs as joint costs. Although Verizon argues that CLECs should be prevented from recovering any portion of their local loop costs in intrastate access charges, Verizon PA currently recovers a portion of its own local loop costs through its intrastate access rates. It therefore follows that CLECs should be permitted to do the same. This holding

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<sup>112</sup> *Bell Atlantic - Pennsylvania, Inc. v. Pa. PUC*, 763 A.2d 440, 480 (Pa. Cmwlth. 2000) (“*Global Order Appeal*”).

<sup>113</sup> *Global Order Appeal*, 763 A.2d at 480.

<sup>114</sup> *AT&T Communications of Pennsylvania, Inc. v. Verizon North Inc. and Verizon Pennsylvania Inc.*, Docket No. C-20027195 (Recommended Decision of ALJ Cynthia Williams Fordham dated December 7, 2005).

<sup>115</sup> *Verizon Pennsylvania Inc., Verizon North Inc., Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance, Verizon Select Services, Inc., Verizon Global Networks, Inc., MCImetro Access Transmission Services, LLC d/b/a Verizon Access Transmission Services and MCI Communications Services, Inc. v. Penn Telecom, Inc.*, Docket No. C-20066987 (Order entered August 29, 2008) (“*PTI CLEC Access Rate Order*”); and *Verizon Pennsylvania Inc., Verizon North Inc., Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance, Verizon Select Services, Inc., Verizon Global Networks, Inc., MCImetro Access Transmission Services, LLC d/b/a Verizon Access Transmission Services and MCI Communications Services, Inc. v. CTSI, LLC*, Docket No. C-20077332 (Order entered September 29, 2008).

maintains parity between the various types of regulated telecommunications service providers and is consistent with current Commission policy.

*The Commission has consistently adopted the position that the fixed costs associated with the loop plant and facilities of ILECs should be allocated and recovered by services that utilize the local loop, including the ILECs' intrastate carrier access services.* This position was clearly enunciated in a number of our prior proceedings. Although the Commission undertook extensive access charge reforms in the context of both its landmark *Global Order* proceeding and subsequent case adjudications, it did not enunciate a position that the loop plant and facilities costs of ILECs are anything but joint. The *Global Order* held that the recovery of the jurisdictional non-traffic sensitive costs of such loop plant and facilities should continue from all intrastate services that utilize them including access. This led to substantial reform of the intrastate carrier charge component of the switched carrier access services of both major and rural ILECs, but it did not result in its outright elimination. This non-elimination of the carrier charge was sustained by the Commonwealth Court of Pennsylvania in its in-depth review of the *Global Order*. Most notably, the benefits of the ILEC intrastate access charge reforms adopted in the *Global Order* were required to be passed through by the interested long-distance interexchange carriers (IXCs) to the IXCs' respective end-user customers.<sup>116</sup>

In the meantime, federal interstate access rates have moved lower due to the *FCC's removal of all contribution for the shared local loop* from interstate switched access rates and the establishment of two explicit USF support mechanisms in its place.<sup>117</sup> The FCC's restructuring of switched access rates has evolved through numerous decisions over the course of many years and has followed separate paths for rural and non-rural carriers.<sup>118</sup>

The ALJ relies heavily upon a transcript passage of the PTA's witness for the proposition that federal access rates are cost-based. When the PTA witness stated that the FCC rates are cost-based he clearly did so with the caveat "for the elements which it is being applied, yes...for the traffic sensitive portion..."<sup>119</sup> This detail, overlooked by the ALJ, makes all the difference in the world.

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<sup>116</sup> *PTI CLEC Access Rate Order* at 13-14 (citations omitted and emphasis added).

<sup>117</sup> PTA Direct at 10-11.

<sup>118</sup> *Id.* at 11.

<sup>119</sup> Tr. 609.



Loop and other fixed costs were removed from interstate per minute charges by the FCC immediately following the passage of the TCA-96 and transferred to several fixed, per line charges, predominantly the CCL, which continued to be charged to the IXCs.<sup>120</sup> It is this rate structure that this Commission mirrored with the *Global Order*. In 1999, the per minute (traffic sensitive) intrastate rates were set to be identical in 1999 (and again in 2003) and, as noted previously, today there is an aggregate difference of only \$10.4 million between the PTA RLEC's inter and intrastate traffic sensitive access rates. The CCL rate was not mirrored.

Thereafter, the FCC transitioned away from the CCL by a *combination* of *both* increases in end user rates *and a universal service support mechanism*. The FCC concluded that all federally allocated loop costs should be recovered from end users, but found that the resulting local rates were too high.<sup>121</sup> The FCC's *CALLS Order* in 2000<sup>122</sup> and *MAG Order* in 2001 made specific reductions to remove all implicit support from the interstate access rates of non-rural and rural telephone companies, respectively, and initiated an increase in the end-user charge,<sup>123</sup> as well as new explicit federal universal service mechanisms.

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<sup>120</sup> *In the Matter of Access Charge Reform*, CC Docket No. 96-262 (First Report and Order, released May 16, 1997) at ¶ 6 (“First, we will reduce usage-sensitive interstate access charges by phasing out local loop and other non-traffic-sensitive (NTS) costs from those charges and directing incumbent local exchange carriers (LECs) to recover those NTS costs through more economically efficient, flat rated charges.”). Other fixed charges on the IXCs were also implemented, including the PICC and RIC.

<sup>121</sup> *In the Matter of Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers; Federal-State Joint Board on Universal Service; Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation; Prescribing the Authorized Rate of Return For Interstate Services of Local Exchange Carriers*; CC Docket Nos. 00-256, 96-45, 98-77 and 98-166; Second Report and Order and Further Notice of Proposed Rulemaking In CC Docket No. 00-256, Fifteenth Report and Order In CC Docket No. 96-45, and Report And Order In CC Docket Nos. 98-77 and 98-166, released November 8, 2001 (“*MAG Order*”) at ¶ 17 (“For example, the costs of the common line or loop that connects an end user to a LEC central office should be recovered from the end user through a flat charge, because loop costs do not vary with usage. Yet the SLC, a flat monthly charge assessed directly on end users to recover interstate loop costs, has, since its inception, been capped due to affordability concerns.”)

<sup>122</sup> *In the Matter of Access Charge Reform Price Cap Performance Review for Local Exchange Carriers Low-Volume Long-Distance Users Federal-State Joint Board On Universal Service*, CC Docket No. 96-262, CC Docket No. 94-1, CC Docket No. 99-249 and CC Docket No. 96-45, Sixth Report and Order In CC Docket Nos. 96-262 and 94-1 Report and Order In CC Docket No. 99-249 Eleventh Report and Order In CC Docket No. 96-45 released May 31, 2000 (“*CALLS Order*”).

<sup>123</sup> The residential and single line business SLC was increased by \$3.00, from \$3.50 to a cap of \$6.50 per line, where it stands today.

Two federal funds, the Interstate Access Support Fund (“IAS”) and the Interstate Common Line Support Fund (“ICLS”), were created for price cap carriers and rate of return carriers, respectively, and represent the “explicit” support that was created when the “implicit” support from interstate access rates was reduced.<sup>124</sup> These funds are similar to the PA USF in that they operate as revenue substitution mechanisms.<sup>125</sup> Interstate access charge reductions were not all shifted to the end user through higher local rates, as the IXCs propose, and the ALJ recommends, here. The IXCs want the federal result, but ignore the federal mechanism, namely use of universal service funds, instead focusing solely on parity and opposing the use of the PA USF.

Nor do the “reciprocal compensation” rates used for the exchange of local traffic, the second standard employed by the ALJ to justify her Recommended Decision, have any application in this proceeding. Reciprocal compensation rates are based upon forward-looking cost models. While the FCC has endorsed these forward-looking cost models for the non-rural companies, it likewise recognized that “the forward looking cost mechanisms available at that time could not predict the costs of serving rural areas with sufficient accuracy.”<sup>126</sup> “Forward looking models have yet to be endorsed by the FCC for RLECs, and in fact thus far have been rejected for rural costing purposes.”<sup>127</sup> This Commission also expressly rejected incremental cost studies in the CLEC access rate proceeding:

If we were to adopt the “incremental cost” theory of Verizon in the instant proceedings, then the intrastate common carrier charges of Verizon PA and all other ILECs would have to be eliminated. Furthermore, the treatment of the non-traffic sensitive loop plant and facility costs required by the “incremental cost” theory may not only run counter to established Commission precedent under

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<sup>124</sup> PTA Direct at 33-34.

<sup>125</sup> PTA Direct at 34.

<sup>126</sup> *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8937-45 paras. 297-313 (1997).

<sup>127</sup> PTA Surrebuttal at 7.

applicable Pennsylvania law, but it may also implicate relevant provisions of the federal TA-96 [citing 47 U.S.C. § 254(k)].<sup>128</sup>

The problem with the TELRIC method and the lack of loop allocation, is that nobody pays for the loop. Again, the ALJ's recommended cost recovery proposal contravenes all established Commission precedent.

*The major driver of a wireline carrier's cost is the rural nature of its loops.*<sup>129</sup> The economics of rural service are a straight forward direct relationship between density and cost, as Mr. Laffey explained:

Of course, the major driver of cost is the overall "ruralness" of the area served by a local exchange carrier. The lesser the population density within the service territory, the longer the average loops required to serve the customer base, physical facts which result in higher capital and maintenance costs. The greater the population density, the lesser the investment and cost per subscriber.<sup>130</sup>

No party disagreed with this rather obvious statement. AT&T's witnesses described it as a "truism of network economics."<sup>131</sup>

As Mr. Kubas of OTS accurately observed, telephone regulation has always been about policy, a balance of competition and universal service, a focus that continues.<sup>132</sup> Were all fixed costs to be recovered from the end user, and none from access customers or an increased USF, the resulting rate structure would defeat these very same policies.

Nothing has been presented in the record of this case that should cause the Commission to abandon its consistent opinion, stated in 1991 and as recently as 2008, that loop costs are jointly shared costs. The FCC's decision to exclude fixed network costs from interstate access rates is not binding in any way on this Commission's authority to set intrastate access rates.

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<sup>128</sup> *PTI CLEC Access Rate Order* at 15.

<sup>129</sup> *PTA Direct* at 28.

<sup>130</sup> *Colwell Benchmark/USF Proceeding*, PTA St. No. 1R (Rebuttal) at 51.

<sup>131</sup> *Colwell Benchmark/USF Proceeding*, AT&T St. No. 1SR (Surrebuttal) at 20.

<sup>132</sup> *OTS Direct* at 10.

Moreover, should the Commission determine to do so, it should follow the FCC's path more fully and spread recovery between a rational local rate increases and increased USF support.

**C. Exception No. 3 - The ALJ Erred by Proposing that Local Rates be Set Without Also Considering Comparability, Sustainability and Revenue Neutrality (RD at 115-116 and 106-108; FOF Nos. 11-12, 43, 47-53 and 79; COL Nos. 29-32 and 36-38).**

**1. The Scope of the Recommended Decision is Too Narrow**

The dollars at issue in this proceeding are substantial from the vantage point of the RLECs and their local service customers. Applying the PTA RLECs' interstate rates to intrastate access minutes will result in an immediate revenue reduction of \$63.9 million<sup>133</sup> or 17.5% of their *total* intrastate revenues.<sup>134</sup> A loss of this amount would cause an 80% reduction in the PTA RLECs' operating income, which in 2008 was \$109 million.<sup>135</sup> CenturyLink has identified its loss as \$27.9 million.<sup>136</sup> Intrastate parity, therefore, represents a \$91.8 million revenue reduction to Pennsylvania's rural telephone companies (and, of course, a corresponding and equal expense reduction to the IXC).

If recovered from RLEC local rates, this level of revenue shift is equal to a *tariff rate* increase of \$7.32 per line on average -- a 47% rate increase.<sup>137</sup> For several of the PTA Companies, their local service rates would more than double. This creates an average residential *tariff rate of \$22.89* for the PTA RLECs in aggregate<sup>138</sup> and an *average billing rate of 32.07*.<sup>139</sup>

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<sup>133</sup> *Id.* at 16.

<sup>134</sup> PTA Surrebuttal at 39-40.

<sup>135</sup> PTA Ex. GMZ-11 and GMZ-13; PTA Direct at 17-18.

<sup>136</sup> CenturyLink Direct at 17.

<sup>137</sup> PTA Ex. GMZ-13; PTA Direct at 18.

<sup>138</sup> PTA Ex. GMZ-13. Tariffed local rates for several RLECs will ascend to \$26.00-\$27.00 range, with two companies at \$32.00.

<sup>139</sup> The *billing rate* is what the end user customer actually pays after adding the mandatory Federal Subscriber Line Charge, 911 Surcharge, Relay Service Surcharge and Federal Universal Service Surcharge, which total \$8.57, if a 911 fee of \$1.25 is used. *Colwell Benchmark/USF Proceeding*, PTA Direct at 5. The Federal Subscriber Line Charge ("SLC") (\$6.50); 911 Surcharge (typically \$1.25 - \$1.50); Relay Service Surcharge (\$0.08) and Federal

Due largely to intrastate access reform, local rates in Pennsylvania are already 55% higher than they were 10 years ago.<sup>140</sup> Access rates during that same period have decreased from \$.066 per minute to the current \$.048 per minute.

By comparison, the national average local tariffed rate is \$15.03 per line (2008).<sup>141</sup> An average PTA RLEC residential tariff rate of \$23.00 also far exceeds Verizon's own Pennsylvania rural rates (Density Cells 3 and 4), which currently range from \$11.95 to \$15.40, as well as Verizon's urban rates (Density Cells 1 and 2) of between \$16.32 and 16.62.<sup>142</sup>

The Recommended Decision limits its consideration of the effect of access charge reductions upon local rates to only issues of affordability and gradualism.<sup>143</sup> Rates would be pushed to the OCA's *maximum* affordability ceiling of \$23.00 and beyond.<sup>144</sup> "Gradualism" is defined as increases of \$3.50 per year, but then applied in such a way so that some companies' rates will increase by \$7.00 in the first year.<sup>145</sup>

The ALJ disregards the fact that the resulting RLEC local rates will be considerably higher than the rates charged by Verizon, the dominant local exchange carrier in the Commonwealth, as an irrelevant standard.<sup>146</sup> The ALJ also ignores the (in)ability of the RLECs to collect the higher local rates, concluding that such an inquiry would insulate them from competition. Moreover the Recommended Decision concludes, inconsistently, that local rates

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Universal Service (\$0.74). The additive is \$8.82 if a 911 fee of \$1.50 is used. PTA Surrebuttal at 48. The tariff rate additive used by the OCA, which also includes the categories of touch tone charges and "other," is \$9.12. \$8.86 for SLC, 911, Relay and USF surcharge plus \$0.26 for "other" charges equals \$9.12. Tr. 508-09.

<sup>140</sup> PTA Ex. GMZ-7. The average RLEC local rate have increased from \$10.12 to \$15.57, or by 54%. During this same time frame the residential subscriber line charge cap was increased from \$3.50 to \$6.50 per month. Combined, this represents an increase of \$8.46 per month, or a 62% rate increase for residential service. PTA Direct at 10.

<sup>141</sup> Colwell Benchmark/USF Proceeding, PTA Ex. JJJ-3.

<sup>142</sup> PTA Surrebuttal at 48.

<sup>143</sup> RD at FOF Nos. 43 and 79.

<sup>144</sup> Tr. 508 (Loube) ("the affordable rate is somewhere around \$22 to \$23.")

<sup>145</sup> RD at Annex C.

<sup>146</sup> The Recommended Decision concludes that: comparability standard is "not [statutorily] applicable to the Commission"; Verizon's rates may change; and adoption would not be "consistent with ALJ Colwell's determination that comparability should not be considered." RD at 115.

can be raised without accelerating RLEC line losses, despite the presence of substantial competition.<sup>147</sup>

## **2. The PTA's Position is That Other Factors Should Also Be Considered**

In Briefs, the PTA took the position that, against the overarching standard of “just and reasonable,” telephone ratemaking considerations should include:

1. Compliance and consistency with Chapter 30 Plans and statute;
2. The RLECs' regulated revenue allowance levels;
3. Comparability/benchmarking;
4. Affordability and reasonableness;
5. Gradualism; and
6. Customer benefits.

PTA continues to argue that all of these principles should be considered.

## **3. The RLECs Have No Ability to Average Down Rural Costs**

The PTA Companies serve very rural areas. The smaller RLECs serve an average of 30.5 lines per square mile.<sup>148</sup> The “larger” RLECs, FairPoint, Frontier, Consolidated and Windstream, are denser, but still serve only 49.4 lines per square mile.<sup>149</sup> Verizon, by comparison, has a density factor of 193.2 customers per square mile, almost four times denser than the average “mid-tier LEC” and approximately six times more dense than the average small LEC. Moreover, Verizon's density factor is well above the state average of 130.3 lines per square mile.<sup>150</sup>

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<sup>147</sup> See FOF Nos. 13 and 14 (competition) and 51-53 (market indifference to price increases).

<sup>148</sup> PTA Direct at 28.

<sup>149</sup> PTA Ex. GMZ-14.

<sup>150</sup> PTA Direct at 27.

Verizon serves *all* the urban areas of Pennsylvania without exception: Pittsburgh, Philadelphia, Altoona, Wilkes-Barre, Scranton, Harrisburg, Hershey, Erie, Johnstown, Lancaster, Allentown, Uniontown, Bethlehem, York, etc. By contrast, the largest “city” served by any of the Commission-designated RLECs is Chambersburg, served by CenturyLink, which is a town of 18,000 residents. Beyond that, the service territories of the RLECs are composed of “villages and hamlets.”<sup>151</sup>

The PTA Companies are investing in rural wireline consumers, while other companies are abandoning this still critical industry segment. The rural LECs are more entrenched in traditional rural telephone voice service than ever before.<sup>152</sup> When Denver & Ephrata Telephone sold its three Pennsylvania RLECs, it was Windstream that purchased these companies. Consolidated Communications purchased North Pittsburgh Telephone. Frontier Communications purchased the rural Commonwealth Telephone. Century Telephone subsequently purchased the rural wireline assets spun-off by Sprint (Embarq).

“Verizon is selling off most of its operations in rural areas and is spending billions to wire most of the rest of its territory with its fiber optic network, or FiOS....”<sup>153</sup> As Verizon has sold 6.3 million rural access lines, it was FairPoint (1.5 million lines) and Frontier (4.8 million lines) that purchased the assets serving these customers. As Verizon’s Chief Financial Officer John Killian stated with respect to Verizon’s rural divestiture, “[t]hese are good properties, but *they’re much more rural in nature, and they really don’t fit with the strategy we have for FiOS and broadband[.]*”<sup>154</sup>

The PTA does not dispute that Verizon and Sprint serve rural areas as they have claimed.

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<sup>151</sup> *Id.* at 26-27.

<sup>152</sup> *Id.* at 26.

<sup>153</sup> *Id.* at 24.

<sup>154</sup> PTA Surrebuttal at 33 citing *Wall Street Journal*, May 14, 2009, “Verizon Sells Phone Lines In 14 States To Frontier,” Amol Sharma, page B1 (emphasis added).

Verizon states that its 1.1 million rural customers are greater “than all of the RLECs put together.”<sup>155</sup> Sprint asserts that it provides service to more customers in RLEC service territories than all but three RLECs.<sup>156</sup> “These observations simply point to the sheer magnitude of these carriers.”<sup>157</sup>

Such observations, however, tell only part of the story. “It is a question of degree and composition . . . they are in no way rural carriers.”<sup>158</sup> While Verizon’s 2006 network biennial update reported over “1.1 million rural access lines” served, it also inventoried a total of 5.1 million access lines served. Sprint points to its rural facilities as proof of its “ruralness.” As with Verizon, however, Sprint produces a self image to suit its present purposes, and avoids describing its more pervasively urban operations so as to appear rural. Sprint reports that its new investment is targeted for large metropolitan areas nationally<sup>159</sup> and its largest Pennsylvania investments are in the more densely populated counties and those surrounding them, like the five county Philadelphia area. Sprint’s coverage map and statements on its website show large portions in rural Pennsylvania that are either not served or where service is rated as only good to fair.<sup>160</sup>

The PTA is not denigrating these other carriers’ networks. It is simply pointing out that, in the geographic and customer mix of these companies, these carriers have been allowed to develop selectively, to focus on lower-cost urban areas against which higher rural costs can be averaged.<sup>161</sup>

The benefits of serving primarily high-density areas are several-fold. The Verizon

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<sup>155</sup> Verizon Rebuttal at 22; recited in the RD at 132 and FOF No. 86.

<sup>156</sup> Sprint Rebuttal at 32.

<sup>157</sup> PTA Surrebuttal at 35.

<sup>158</sup> *Id.* at 32.

<sup>159</sup> *Id.* at 34 citing “Sprint Nextel Reports Third Quarter 2009 Results” at 2.

<sup>160</sup> PTA Ex. GMZ-18.

<sup>161</sup> PTA Surrebuttal at 35.



ILECs, for example, “because of their significantly larger customer base and service to Pennsylvania’s most dense population areas, can average costs better than the RLECs.”<sup>162</sup> This is not a new issue. In the original 1996 access reform docket, ALJ Schnierle observed:

BA-PA’s assertion is largely correct, but does not tell the entire story. To the extent that BA-PA has the most urban service territories in the state, its service costs can be expected to be the lowest because, as discussed earlier, a major cost factor of telephone service is the cost of the loop, and the loops tend to be much shorter in an urban environment. On the other hand, the small rural ILECs are likely to have higher costs because their loops are longer. If a system is to be devised to have generally equal prices between urban and rural customers (as required by the Telecommunications Act), then the urban customers, of necessity, will be subsidizing the rural.<sup>163</sup>

Verizon, with a 20/80 split of rural to urban wireline customers, has conceded that its urban customers subsidize its rural customers. In a prior proceeding:

... Bell claimed that the urban residential customers paid more than their fair share of costs and, consequently, subsidized rural and other high cost residential customers [clarified as “residential dial tone line service”]. By lowering urban residential rates and raising rural and other high cost residential rates, Bell proposes moving both groups within one market basket closer to cost.<sup>164</sup>

“Given that rates in urban areas of Verizon are still higher than those in Verizon’s rural areas, it would appear that this internal cross-subsidization continues.”<sup>165</sup> This is an advantage to Verizon in keeping its rural rates, both local and access, lower comparatively speaking.

The PTA Companies, on the other hand, lack the size and scope in customer base that allows them internally to “average down” their costs per customer. As Mr. Zingaretti concluded: “Without an urban customer base to ‘average down’ their costs per customer, the RLECs are legitimately seeking external support for rural telephone consumers.”<sup>166</sup>

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<sup>162</sup> PTA Direct at 27.

<sup>163</sup> *Generic Investigation of Access Charge Reform*, Docket No. I-00960066 (Recommended Decision dated June 30, 1998) at 55-56.

<sup>164</sup> *Pa. PUC et al. v. Bell Atlantic-Pennsylvania, Inc.*, Docket No. R-00963550 (Order entered December 16, 1996) at 9 (footnote omitted).

<sup>165</sup> PTA Surrebuttal at 33.

<sup>166</sup> PTA Surrebuttal at 33; *See also* PTA Direct at 27.

Corporate affiliation does not affect the higher network costs of a rural territory. The mid-size RLECs and the small independent RLECs, all of which comprise the PTA Companies, share “significant service similarities.”<sup>167</sup> They provide service in areas of the state where access line density is generally very low. It is the service area characteristics, and not the size of the serving carrier or level of success, that determines their eligibility for universal service support.<sup>168</sup> Federal USF support is not based upon size. There is no distinction drawn for rural companies on the basis of size or success or consolidated results. To the extent carriers served rural areas, support is available.

Notably, the RLECs have other costs imposed upon them, as well, that their competitors do not possess. The obligation to serve, a basic, fundamental precept of regulation, existed before the advent of competition and the RLECs have never been relieved of it. “The obligation to serve is deeply embedded in the RLECs’ DNA and is a guiding aspect of their credo.”<sup>169</sup> Notably this Commission, in comments before the FCC, has recognized the incumbents’ continuing COLR obligation in Pennsylvania.<sup>170</sup>

Unregulated carriers, cable voice and wireless have no obligation to serve. They may, as Sprint says, “want to,” but that is different from “have to.” Perfect evidence of this is Sprint’s letter to customers terminating service because Sprint’s customer service center received too

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<sup>167</sup> *Id.* at 27.

<sup>168</sup> *Id.* at 31.

<sup>169</sup> *Id.*

<sup>170</sup> *Connect America Fund, a National Broadband Plan For Our Future*, FCC Docket Nos. WC 10-90, GN 09-51, WC 05-337 and FCC 10-51, Pa.PUC Comments at 36 (“The duties and/or responsibilities of COLRs include not only the provision of ubiquitous narrowband voice services at just, reasonable and affordable retail rates under state regulatory oversight and quality of service standards, but also include the provision of wholesale access and interconnection facilities and services to other telecommunications carriers and other communication services providers. COLRs are often the backbone providers of critical connectivity facilities and services for the processing of 911/E911 emergency calls, whether or not such calls have originated from their own retail end-user customers. In short, COLRs - and by implication the ILECs - have provided and continue to provide many of the traditional universal service aspects to the public at large.”) See also *Colwell Benchmark/USF Proceeding* PTA Ex. JLL-7 (“CETCs do not have identical service obligations [as rural carriers]. CETCs are not required to provide service ubiquitously throughout a rural carrier’s study area. CETCs are not required to undertake expensive broadband deployment commitments under state law.”).

many calls from the customer regarding billing and account information.<sup>171</sup> Regulated CLECs have no duty to serve *all* customers in the territories in which the CLEC receives certification.<sup>172</sup>

Regulation itself imposes costs. Only wireline LECs are regulated by the Commission. Wireless, cable voice and broadband VoIP providers are *all* expressly excluded from any Commission regulation as public utilities. This means no rate or service regulation. Regulatory approval of merger (“change of control”) applications are not required. No “merger commitments.” No tariffs. No broadband commitments. No BFRRs. No BARPs. No annual financial and broadband reports. No informal BCS complaints. No customer formal complaint proceedings. No access line reports. No service reports. These obligations are imposed upon the regulated RLEC in order to serve the public policy as defined by the General Assembly and the Commission. To reject any acknowledgement of the costs of these burdens simply because quantification of cost is difficult is wrong.

Providing universal and ubiquitously high quality voice and broadband coverage today, as only the RLECs do in their rural service areas, requires an expansive network, not only to build but also to maintain. That in turn requires substantial investment. These uneven cost burdens must be addressed through explicit universal service funding mechanisms or through contributions from other rate elements. As this Commission has previously recognized, “[t]he carriers with the obligation to serve clearly have the disadvantage and merit universal service support.”<sup>173</sup>

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<sup>171</sup> Tr. 225-26; CenturyLink CX Ex. 3.

<sup>172</sup> PTA MB at 65-66.

<sup>173</sup> *Colwell Benchmark/USF Proceeding*, PTA Ex. JJJ-6, PA PUC Staff Reply Comments at 5. *See also* OCA St. 1 (Direct) at 32 (“Thus, if one competitor is required to serve all customers and other competitors do not have to serve all customers, the competitor with the obligation to serve is at a disadvantage.”).

#### 4. RLEC Rates Set At \$23.00 Are Not Comparable

Setting rates by comparison (i.e, benchmarking) is standard telephone ratemaking practice and a hallmark for universal service support. The ALJ here rejects the RLECs' continued use of benchmarking for local rates as not legally required and without discussing the merits of the concept.<sup>174</sup> The Recommended Decision ignores the fact that access reductions are not statutorily required either, but proceeds to do so nevertheless.<sup>175</sup>

The federal "comparability" standard prescribes that customers in rural areas must have access to services at rates comparable to rates charged for similar services in urban areas.<sup>176</sup> As the FCC has explained:

Congress adopted section 254 to help ensure that, as competition develops, explicit support mechanisms would replace, as far as possible, implicit support mechanisms in order to preserve the fundamental communications policy goal of providing universal telephone service in all regions of the nation at reasonably comparable rates.<sup>177</sup>

The FCC has consistently recognized that the states set local rates and are best positioned to meet the standard:

States, of course, retain primary responsibility for local rate design policy and, as such, bear the responsibility to marshal state and federal support resources to achieve reasonable comparability of rates.<sup>178</sup>

The FCC has subsequently reaffirmed that authority over the comparability standard lies with

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<sup>174</sup> COL No. 32 ("Federal law regarding rate "comparability" at 47 U.S.C. § 254(b)(3) is not applicable to the Commission and does not act as a constraint on intrastate retail rates. *Buffalo Valley Telephone Company et al. v. Pa. PUC*, 990 A.2d 67 (Pa. Cmwlth. 2009).")

<sup>175</sup> RD at 79 ("Also, Act 183's silence about specific access levels should not be interpreted as legislative disfavor for access reductions.")

<sup>176</sup> 47 U.S.C. § 254(b).

<sup>177</sup> *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Order On Remand*, Further Notice of Proposed Rulemaking, and Memorandum Opinion and Order (Order released October 27, 2003) at ¶ 16. ("In this Order....[we] adopt measures to induce states to ensure reasonable comparability of rural and urban rates in areas served by non-rural carriers.")

<sup>178</sup> *Seventh Report & Order and Thirteenth Order on Reconsideration*, FCC 99-119, CC Docket Nos. 96-5, 96-62 (Order released May 28, 1999) at ¶ 31.

“the states [who] retain primary responsibility for ensuring reasonable comparability of rates within their borders.”<sup>179</sup> The United States Court of Appeals for the Fifth Circuit held that section 254 of the TCA-96 did not affect the proscription in section 2(b) against FCC regulation of intrastate rates.<sup>180</sup>

In the original access investigation, ALJ Schnierle found that the comparability standard applies:

The Telecommunications Act of 1996 requires that rates for service in rural, insular and high cost areas be “comparable to rates charged for similar services in urban areas.” 47 U.S.C. §254(b)(3). While this would prohibit rural basic service rates that are far in excess of urban basic service rates, it also prohibits urban rates that are far in excess of rural rates. Under any universal service program, urban customers will be required to subsidize the basic local service of rural customers. . . . AT&T suggests that ILECs whose basic service rates are less than the BA-PA average should raise them to that level in exchange for reductions in access charges, before receiving universal service funding. (AT&T M.B. at 39-40). I agree with this suggestion in principal, in that it recognizes that any solution to the access charge situation requires both rate rebalancing and universal service funding.<sup>181</sup>

Following up, the original *Global Order* set rural local rates by comparison to Verizon’s rates. Other states have expressly adopted the comparability standard, including Arkansas, California, Colorado, Hawaii, Idaho, Indiana, Maine, Missouri, Nebraska, Nevada New Hampshire, Oregon, and Wyoming.<sup>182</sup>

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<sup>179</sup> *Id.*

<sup>180</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5<sup>th</sup> Cir. 1999) at 421, 424, 446-48.

<sup>181</sup> *Generic Investigation of Access Charge Reform*, Docket No. I-00960066 (Recommended Decision dated June 30, 1998) at 55-56.

<sup>182</sup> *Colwell Benchmark/USF Proceeding*, OCA Direct at 10; *Home Telephone Co. of Pittsboro, Inc. v. Verizon North, Inc.*, 904 N.E.2d 223, Ind.App. (March 31, 2009); *Investigation and rulemaking to adopt, amend, or repeal regulations pertaining to Chapters 703 and 704 of the Nevada Administrative Code regarding a regulatory scheme intended to promote more competition in the local telephone market, establish the terms, conditions and procedures under which an incumbent local exchange carrier may be excused from its obligations as the provider of last resort, and reinstatement of those obligations, and other related utility matters in accordance with Assembly Bill 518*, Docket 07-06016, Nevada Public Utilities Commission, Order Adopting Phase V Temporary Regulations (December 23, 2008).

The dictionary definition of the word “comparable” is “equivalent” or “similar.”<sup>183</sup> Dr. Loube of the OCA proposes that the Commission adopt a standard under which residential rates should be no higher than 120% of Verizon’s *statewide* weighted residential rate. This was rejected by the ALJ as inconsistent with the federal standard.<sup>184</sup> The PTA proposes that the comparable rate should be based upon 115% of Verizon’s *urban* rate, as Mr. Laffey explained based upon the FCC’s approach to high cost support.<sup>185</sup> Applying the 115% adjustment, *the comparable rate is \$18.94* (the simple average of Verizon’s Density Cell 1 and 2 rates x 1.15).<sup>186</sup> The ALJ does not address the PTA’s proposal.

The comparable rate of \$18.94 should be adopted by the Commission. If the \$23.00 (minimum) tariff rate proposed in the Recommended Decision is adopted, Pennsylvania will have created RLECs with very high local rates, as contrasted with Verizon’s rural (\$12.00-\$15.00) and urban (\$16.50) rates, as well as the national average (\$15.00).<sup>187</sup> Even if this Commission concludes it is not mandated by federal law to maintain strict “comparability,” it certainly would be good public policy to do so, as it would ensure that rural local rates remain affordable and reasonable, both of which are state goals.

**5. RLEC Rates Set at \$23.00 are Not Competitively Sustainable and Increases to this Level are Not Revenue Neutral.**

The RLECs and their customers are placed in a very precarious position by the Recommended Decision. The RLECs’ local service territories are not fully competitive, yet

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<sup>183</sup> PTA Rebuttal at 22.

<sup>184</sup> RD at 115 and FOF Nos. 68-70.

<sup>185</sup> *Id.*, PTA Surrebuttal at 4.

<sup>186</sup> PTA Surrebuttal at 48 (updated from the \$18.08 rate that the PTA presented in *Colwell Benchmark/USF Proceeding* to accommodate the most recent Verizon figure. PTA St. No. 1SR at 4. *Colwell Benchmark/USF Proceeding*, Verizon has two city (urban) cells, Cells 1 and 2. Density Cell 1 is for all Philadelphia and Pittsburgh City Exchange Areas with working pairs per square mile greater than 9,000, and Density Cell 2 is all remaining Philadelphia and Pittsburgh City Exchange Areas or Zones. PTA Surrebuttal at 3.

<sup>187</sup> PTA Surrebuttal at 48.

there is substantial competition.<sup>188</sup> As a result, a tariffed rate that is too high relative to competition will accelerate customer losses. A tariffed rate set too high, nevertheless, must be paid by the customer who has no competitive option.

There can be no question that there is competition in the RLECs' service areas. The line losses experienced by the PTA Companies are "staggering and reflect the reality of the major shift now occurring in telecommunications."<sup>189</sup> The PTA Companies served 841,981 access lines in 2005. By 2008, this figure dropped to 717,935, a 17% decline over 3 years.<sup>190</sup>

*But* the RLECs *also* stated that alternative service is not ubiquitously available in the more rural areas.<sup>191</sup> The Recommended Decision ignores this evidence and claims that: "The RLECs' factual presentation was contradictory as, on the one hand, RLECs claimed that access reform would cause harmful local service rate increases through rebalancing, but on the other hand, they claimed an inability to increase local service rates due to competitive pressure."<sup>192</sup> Both observations are true, but the nuances were not recognized by the ALJ.<sup>193</sup>

The RLECs continue to be the only service providers and guarantors of universally available voice (and broadband) service for an unknown, but substantial percentage of its citizens. The ALJ rejected the PTA's estimate that "perhaps, forty percent (40%)" of customers have no option,<sup>194</sup> but competitive presence is difficult to establish and is not always known. While admittedly 40% is an estimate, the lack of competitive coverage in rural Pennsylvania was

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<sup>188</sup> PTA Surrebuttal at 26.

<sup>189</sup> *Id.*

<sup>190</sup> *Id.*

<sup>191</sup> *E.g.* Tr. 604-05.

<sup>192</sup> FOF No. 11.

<sup>193</sup> A further example of the ALJ's failure to recognize the nuances of the PTA's evidence regarding the constraints of competition in increasing local rates as the only means of achieving revenue neutrality is her statement that "[w]hile claiming rate increases on one hand, the RLECs also asserted, on the other hand, that they cannot effectively increase local rates to offset access charge reductions because there is too much competition. This inconsistency in presentation does not help with the establishment of a prima facie case." RD at 76.

<sup>194</sup> RD at 107 ("Furthermore, PTA's contentions that perhaps 40% of rural customers are without competitive options is also unsupported by the record.").

fully explored in the record and showed that there are still sizable rural areas where other carriers have chosen not to serve, particularly residential customers.

The record shows that cable voice coverage is not ubiquitous. By estimates derived from BCAP discovery, cable voice service is available to only 58.5% of the total households in Pennsylvania on a *state-wide* basis.<sup>195</sup> The cable voice service *availability in rural areas is even less* than this 58% state-wide figure, Mr. Zingaretti explained.<sup>196</sup> The Department of Community and Economic Development (“DCED”) shows large areas of rural Pennsylvania completely unserved by cable broadband service.<sup>197</sup> Comcast, the largest cable company (and a BCAP member), has refused to commit to ETC status and, hence, is only required to place cable facilities where financially advantageous. Verizon, itself certificated as a CLEC in RLEC territories, conceded that it solicits business, not residential, customers.<sup>198</sup>

Wireless service overlap is not complete in rural Pennsylvania either. The Legislative Budget and Finance Committee (“LB&FC”) study of cellular coverage found: “Gaps in cell phone coverage exist in some regions of this Commonwealth, which result in interruption of (dropped calls) or lack of (dead zones) telecommunication coverage.”<sup>199</sup> The source of the data was the cellular carriers themselves and data reporting services. The report states that “Statistics are not maintained on the number of dropped calls and dead zones in Pennsylvania or

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<sup>195</sup> Tr. 136; *See also, Colwell Benchmark/USF Proceeding*, PTA St. No. 1R at 24-25; PTA St. No. 1R at 23; Tr. 474.

<sup>196</sup> Tr. 675.

<sup>197</sup> *Colwell Benchmark/USF Proceeding*, PTA St. No. 1R at 24-25. PTA Ex. JJJ-9.

<sup>198</sup> Verizon MB at 6 (MCIMetro, Verizon’s CLEC, provides competitive retail service to enterprise (large business) customers).

<sup>199</sup> *Colwell Benchmark/USF Proceeding*, PTA St. No. 1R at 24-25. The LB&FC also reported: “The areas with the largest “dead zones” are in the Northern Tier of Pennsylvania, with little of Potter, Cameron, and Clinton counties having cell phone coverage (see map on page 4). There are also areas of Wayne, Susquehanna, Bradford, Sullivan, Columbia, Lycoming, Tioga, Somerset, and Greene counties with no coverage from any provider. Although coverage in the Northern Tier is incomplete, there is at least some coverage in every county, and there are areas in each county where there is a choice of four or more carriers. Statistics are not available on the actual number of dropped calls.” *Id.*



nationwide.... The cell phone companies we spoke with were unable to provide this information.”<sup>200</sup>

Whether the degree of competition is 30, 40, or 50%, there are still substantial areas of Pennsylvania served by only one carrier -- the RLECs. The Commission must continue to be mindful, as it always has, of the customer who has no option, and set rates that continue to be comparable and affordable.

Where competition does exist, however, a \$23.00 RLEC rate (the Recommended Decision’s minimal rate target) is not competitive. This will leave the RLECs with a continuing cycle of accelerated customer losses.<sup>201</sup> While this Commission is charged with promoting competition, so too is it charged with protecting universal service. It cannot forsake one for the other.

More than 80% of RLEC operating income is in jeopardy, with that income shifting to the IXCs.<sup>202</sup> With the loss of all “at-risk” revenues, the companies operating income of \$109 million (2008),<sup>203</sup> would precipitously plummet to \$21.5 million. The RLECs use this money, earned under federal regulations and their Chapter 30 Plans, to maintain and improve their networks, the only network that guarantees voice and broadband access for all.<sup>204</sup> The IXCs cannot advocate RLEC access rate reductions, in a meaningful way, without acknowledging the RLECs’ equitable and legal claims to revenue neutrality.

The Recommended Decision accurately recognizes that the question of what portion of the revenue shift will actually be realized is of critical importance:

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<sup>200</sup> *Colwell Benchmark/USF Proceeding*, PTA Rebuttal at 29.

<sup>201</sup> *Id.*; PTA Direct at 6.

<sup>202</sup> *Id.* at 18.

<sup>203</sup> PTA Ex. GMZ-11.

<sup>204</sup> *Id.*

In my assessment of the myriad issues herein, the most critical from a policy perspective is the level of certainty to be provided to RLECs with respect to actual, realizable recovery of revenue to offset access reductions.<sup>205</sup>

The IXCs do not claim that the higher local rates are sustainable in a competitive marketplace. Raising local rates is referred to as “discretionary,” “an opportunity,” or, at times more candidly, as “exposing the inflated access revenue to the discipline of a marketplace.” Otherwise stated, if the RLECs cannot recover needed revenues in a competitive marketplace, then they should not be in business apparently.

The Recommended Decision accepts this callous co-competitive view without criticism.<sup>206</sup> The pro-competition point of view is that the RLECs have no right to realistically obtain the lost revenues due to access rate rebalancing:

There simply is no substantial basis on which to conclude that the PA USF must “guarantee” revenue replacement for RLEC access reductions to protect universal service/COLR obligations.<sup>207</sup>

Just as all evidence of competition not being ubiquitous is disregarded by the ALJ, so too is the testimony that substantially higher prices are not recoverable in the areas where there is competition.

The RLECs’ own behavior clearly and convincingly proves that there is little or no “headroom” in the market for higher local rates. The RLECs, unanimously, have refused to use the “allowable” revenue increases calculated under their Chapter 30 plans to increase local rates (and their own profitability). As of June 2008, there were approximately \$22 million in allowable, but unused, revenue increases, and, as of January 2010, this figure ballooned to

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<sup>205</sup> RD at 99.

<sup>206</sup> See FOF No. 44 (“In seeking to recover revenue associated with access reductions from an expanded PA USF rather than through local rate increases, the RLECs are seeking a guaranteed dollar-for-dollar recovery of revenue losses.”); and FOF No. 45 (“Access rate reform should not be used as a windfall to the RLECs or to lock in their current levels of access revenues which are otherwise continuing to decline due to competition.”).

<sup>207</sup> RD at 107.

almost \$30 million. During the time frame that these “banks” were accumulated, only \$18.8 million in rate increases were taken (mostly to ancillary services).<sup>208</sup>

In other words, the RLECs have been able to implement less than two-fifths (2/5) of their regulatorily “allowable” rate increases.<sup>209</sup> The remainder is unused. Citizens Telephone Company of Kecksburg, “which faces stiff competition from the local cable company,” has a bank of \$234,594 and has not increased its local rate for at least the last four years.<sup>210</sup> Similarly, Consolidated PA (formerly North Pittsburgh Telephone), with a bank of \$3.5 million and an additional \$1.8 million of banked revenues waived, has not raised its average local rate due to cable and wireless competition.<sup>211</sup> In another example, when the Commission declined Denver & Ephrata’s request to increase access rates and, instead, offered to waive the \$18.00 residential rate cap, the company declined to increase the rates.<sup>212</sup> These pricing limitations are “typical situations among the RLECs.”<sup>213</sup> This evidence is not considered in the Recommended Decision, except to note that the PTA raised it.

The RLECs are legally entitled to these revenues as part of Act 183’s broadband acceleration and would have taken these rate increases, if they could, to generate higher revenues and income for themselves. The fact they have not speaks volumes about pricing in this market.<sup>214</sup> This is proof positive that local rates are already maximized under current market conditions or close to being so.

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<sup>208</sup> PTA Direct at 19.

<sup>209</sup> *Id.*

<sup>210</sup> *Id.*

<sup>211</sup> *Id.*

<sup>212</sup> ALJ Melillo finds that D&E was able to increase local rates with no decline in sales. FOF No. 53. Actually, AT&T Cross-Examination Exhibit 5 shows an acceleration in line loss to 2% during that period. Tr. 604.

<sup>213</sup> *Id.*

<sup>214</sup> Chapter 30 is clear that *all* noncompetitive rates, including access rates, may increase with the rate of inflation. Access rates, however, have not been increased at all. Only local rates have increased. The fact that access rates have not increased, as permitted by the statute has been an unrecognized benefit to access customers. Having foregone allowed revenue increases, the IXCs now want the RLECs to absorb further access decreases, by setting local rates without regard to marketability or sustainability.

The PTA Companies also refute Verizon's claim, adopted by the ALJ,<sup>215</sup> that unnamed, "other noncompetitive services" can absorb some of the rate shock created by interstate parity. As Mr. Zingaretti explained: "In the increases that they have taken, the RLECs have **already** maximized the revenue available from these other services, such as vertical features, non-recurring charges, etc."<sup>216</sup> Verizon claimed that through "better rate design" the RLECs surely could squeeze additional revenue-neutral rebalancing dollars, in fact Verizon conducted no analysis of which RLEC rates could withstand further increases, and if so, by how much. Nevertheless, the ALJ adopted it without skepticism. Indeed, prior Commission orders provide many examples of RLECs that have already increased other noncompetitive services substantially in order to squeeze out what price cap changes they could obtain.<sup>217</sup>

Rate increases above current rates will simply accelerate customer migration and line losses. "In other words, increasing local rates will actually result in less revenue, not more," stated Mr. Zingaretti.<sup>218</sup> CenturyLink's customer poll, which tested the wireline customers' reaction to various levels of price changes and found great levels of resistance, certainly is entitled to more consideration than a mere dismissal.<sup>219</sup> As Mr. Zingaretti stated: "It confirms statements made to me by the PTA Companies that the customer polling performed by CenturyLink is an accurate depiction of today's telecommunications marketplace."<sup>220</sup>

Simply stated, a \$23 local rate may never be realized by the RLECs. One would think that the IXCs would seek to balance their interest in lower rates with preserving the RLECs'

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<sup>215</sup> RD at 107; FOF No. 63 ("Other RLEC noncompetitive service rates (other than residential local service rates) could also be increased.").

<sup>216</sup> PTA Surrebuttal at 45.

<sup>217</sup> See for example, PSI Orders for Ironton (R-00072566), Windstream (Docket No. R-00061461), Lackawaxen (R-00061485), Buffalo Valley (R-00061375, R-00072193 and R-2009-2106671), Conestoga (R-00061376, R-00072194 and R-2009-2105884), Denver & Ephrata (R-00061377, R-00072195 and R-2009-2106666) where multiple miscellaneous and nonrecurring charges were increased.

<sup>218</sup> *Id.*

<sup>219</sup> RD at 76 and 108.

<sup>220</sup> PTA Surrebuttal at 50.

wirelines, since it is those wireline customers that pay them toll revenue. It is a symbiotic relationship. No other carrier is required to allow its customers to subscribe to an IXC. Wireless and cable simply provide their own toll service without a customer option to select an IXC. If the RLECs are out of business, so too is the IXCs' retail toll service.

The IXCs' have determined that driving out wireline business is actually beneficial to the overall corporate interests and business strategy. As the IXCs increase the RLECs' local service rates, AT&T Wireless, Sprint Nextel and Verizon Wireless all stand to realize even greater competitive gains because of line losses created for the RLECs.<sup>221</sup> True, they loss some toll revenue, but gain the whole customer (wireless dial tone, texting, broadband, etc.). In other words, it is a win-win scenario for the mega-carriers, AT&T, Sprint, Verizon and Comcast, and a lose-lose for the RLECs, if these carriers are able to simultaneously reduce their expenses and increase revenues. It is also a lose-lose for many of the RLECs customers, as local rates go up and not all customers have options.<sup>222</sup>

The Commission should expect that the wireless and cable affiliates of the IXCs will take full and complete advantage of the opportunity created in those areas (where they provide service): "The likelihood of massive customer attraction campaigns waged by the cable and wireless carriers in the (relatively) higher density areas of an RLEC's service area while this transition is taking place, with promotional and other offers, seeking to take advantage of what they've accomplished in the regulatory arena, is guaranteed," said Mr. Zingaretti,<sup>223</sup> and the "[l]osses to the rural carriers and the burden upon their remaining customers, the ones without options because the competitors will not serve them, will be, without exaggeration,

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<sup>221</sup> *Id.* at 44.

<sup>222</sup> *Id.* at 44-45.

<sup>223</sup> *Id.* at 49.

staggering.”<sup>224</sup>

“The access revenues that the RLECs receive are extremely important to their day-to-day operations and maintenance of their networks.”<sup>225</sup> This revenue shortfall will compel the RLECs to reduce the capital expenditures needed to continue to provide quality service to rural customers in Pennsylvania.<sup>226</sup> The risk of this result is clearly not worth gambling in exchange for noncommittal and vague IXC assurances of customer benefits in the toll market.

Nor is the outcome lawful as to the RLECs’ financial position. Exogenous change clauses contained in Chapter 30 Plans recognize that “[s]ubsequent regulatory and legislative changes (state and federal) which affect revenues or expenses, to the extent not captured in GDP-PI” may occur,<sup>227</sup> and specifies that such an “[exogenous event] shall be flowed through on a dollar-for-dollar basis, utilizing the most recent per book revenue levels, without any investigation or review of earnings.”<sup>228</sup> Dollar for dollar recovery *is* specified.

With the enactment of Act 183, the concept of “revenue neutrality” was formally codified into Pennsylvania statute. The Pennsylvania Public Utility Code states: “The commission may not require a local exchange telecommunications company to reduce access except on a revenue neutral basis.”<sup>229</sup> Revenue neutrality must provide the PTA Companies with a *realistic* opportunity for recovery of revenues that are regulated by this Commission, in a manner which will offset access reductions on a dollar-for-dollar revenue basis. In other words, the Commission must design access reductions so that the RLECs have a real chance, in the

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<sup>224</sup> *Id.*

<sup>225</sup> PTA Direct at 50.

<sup>226</sup> *Id.*

<sup>227</sup> PTA Surrebuttal at 41; See e.g. Amended Alternative Form of Regulation and Network Modernization Plan of Alltel Pennsylvania, Inc., Part 3.A, p. 23.

<sup>228</sup> *Id.*

<sup>229</sup> 66 Pa. C.S. § 3017(a).

marketplace, to actually recover the lost revenue.<sup>230</sup> Even under traditional rate regulation there is a world of difference between providing an opportunity to recover and being indifferent as to whether recovery will occur.

**D. Exception No. 4 - Universal Service Support. The Recommended Decision Incorrectly Rejects Any Funding From The PA USF To Mitigate End User Impact. (RD at 118-137; FOF Nos. 44-46, 56-67, 75-89; COL Nos. 10-11, 30-33, 35-40).**

The Recommended Decision finds that RLEC access reductions should be implemented solely through rate rebalancing (i.e., upon local ratepayers) without any additional PA USF support at this time. In recommending revenue neutrality solely from rate rebalancing, the ALJ appears to have been persuaded primarily by Verizon's advocacy on two points: (1) the current PA USF regulations do not provide for increasing the fund to account for additional access reform; and (2) further funding of the PA USF will negatively impact Verizon's own wireline customers.<sup>231</sup> As the ALJ concluded, "[t]here simply has been no showing of need for these massive subsidy transfers" and, in a competitive market, "it is unreasonable to expect other carriers and their customers to fund the RLECs' operations through an expanded PA USF[.]"<sup>232</sup>

Based upon these conclusions, the ALJ suggests a phase-in of local rate increases over a 2 to 4 year period. This process would coincide with the proposed rulemaking recommended by ALJ Colwell, with the goal of setting local service rates at a \$23.00 level (or higher). If the Commission were to determine that continued PA USF was appropriate, the ALJ recommends a modified AT&T proposal that provided for temporary (indeed, very brief) PA USF support.<sup>233</sup>

The ALJ rejects the path proposed by the PTA, CenturyLink, and OCA to implement

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<sup>230</sup> *Id.* at 52.

<sup>231</sup> RD at 132.

<sup>232</sup> RD at 133.

<sup>233</sup> RD at 135-36.

further access and local rate reform in tandem with universal service support. The PTA takes exception to the ALJ's primary recommendation that additional RLEC access reductions be achieved solely through rate rebalancing.

**1. Additional PA USF Support to Accommodate Additional Access Reductions is Appropriate**

Universal service funding has been available in all the prior instances where access was reduced on the state side, and has been available on the federal side as well.<sup>234</sup> From the very beginning at both the federal level and for this Commission in the *Global Order*, the goal has been to “*replace* the system of implicit subsidies with ‘explicit and sufficient’ support mechanisms to attain the goal of universal service in a competitive environment.”<sup>235</sup> Elimination of all support has never been the Commission's goal.

Universal service must be balanced with, not forsaken for, competition. Commencing with the *Global Order* and continuing thereafter, the issue was never *whether* to fund universal service, but rather how best to fund it. The purpose of further investigation was not to eliminate support, but to determine whether the present funding mechanism should be changed, for example to a customer-based charge rather than a carrier pool. Universal service is vital to the common good of Pennsylvania. It is an important public policy issue that should not be determined by the advocacy of parties who only selectively serve rural areas and rural customers, and whose non-rural, non-wireline affiliates stand to benefit most. Over a decade ago, original size estimates placed the Pennsylvania Universal Service Fund at over \$122 million.<sup>236</sup> Substantially downsized and its terms established in the *Global Order*, the issue should remain not whether the PA USF should continue to support access reform, but how.

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<sup>234</sup> PTA Direct at 20.

<sup>235</sup> *Global Order* at 26-27 (emphasis added).

<sup>236</sup> PTA Surrebuttal at 8.



The PA USF was never set to expire without some form of replacement funding. In fact, the PA USF adopted by the Commission clearly provided that, if the PA USF were eliminated and no replacement funding adopted in its place, the access rate reductions and existing PA USF credits on customer bills would be immediately reversed.<sup>237</sup> As stated above, the goal was never the removal of “subsidies,” but rather the replacement of *implicit* support with *explicit* support,<sup>238</sup> as Verizon itself acknowledged.<sup>239</sup>

The Commission expressly considered future implementation of some other form of explicit support, such as the Toll Line Charge:

Since no party has advocated the initiation of an intrastate Subscriber Line Charge (SLC) or Toll Line Charge (TLC) in this proceeding, we shall not authorize one at this point but will examine the appropriateness of such a charge in the context of the Commission Investigation in 2001.<sup>240</sup>

Sprint confirmed this in the Global Proceeding:

The small/rural company fund is a *transitional* fund to be used until the Commission establishes a *permanent* universal service fund, *consistent with federal rules*. The Commission will initiate an investigation on or about January 2, 2003 to *develop a long-term solution to universal service*. This proceeding should be coordinated with the *long-term review of the Carrier Charge*.<sup>241</sup>

Thus, this phase of the Commission’s rural access investigation should focus on a final solution to rendering implicit support explicit, not wholesale elimination of support as the ALJ recommends.

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<sup>237</sup> *Id.* As the Commission noted in the *Global Order*, in the event that “no alternative funding has been established through that investigation,” then “residential and business universal service credits will be eliminated.” *Global Order* at 151. Further, the terms of the Small Company USF adopted by the Commission allowed for the access and toll reductions to be reversed. *Colwell Benchmark/USF Proceeding* PTA Ex. JLL-1; Settlement at 4-5 (¶ B.5(d)(6)) and 8 (¶ C.11(g) and Appendix A at 4 (¶ ILC.2).

<sup>238</sup> See note 327 (*Global Order* at 26-27) above.

<sup>239</sup> PTA Surrebuttal at 18 citing Verizon Direct at 7 (before ALJ Colwell).

<sup>240</sup> *Global Order* at 59.

<sup>241</sup> *Id.* at 46, quoting Sprint’s Main Brief (emphasis added).

**2. ALJ's Reliance on Verizon's Claim of a Negative Impact on Verizon's Customers is Misplaced and Overstated**

The ALJ was persuaded by the IXCs' protests to recommend no additional PA USF support for further access decreases, particularly Verizon's claims that its own customers, some 1 million of whom are also rural, will be negatively impacted.<sup>242</sup> However, Verizon's rural customers comprise only 20% of its customer base, the remainder of which is substantially urban. Through the remainder of its urban and suburban customer base, Verizon is able to counterbalance the costs of its service to rural customers such that Verizon's rural customers today enjoy local rates that are actually *lower* than Verizon's urban rates. Thus, even if Verizon's one million rural customers see some rate impact in order to provide contributions to a PA USF, Verizon's rural and urban rates would still be comparable, and still substantially lower, than the proposed rates to be paid by the RLECs' exclusively rural customer base. In fact, if the local rate increases recommended by the ALJ are implemented, the RLECs' customers stand to pay almost two times more for basic local service than do Verizon's rural customers.

As to the reasonableness of the level of USF support Verizon currently pays, and would pay under an expanded PA USF, the ALJ disregarded two relevant points raised by the PTA. First, the current PA USF support (upon which additional support is structured) is precisely what Verizon agreed to in the Global Proceeding. As Commonwealth Court noted in affirming the Commission and rejecting Verizon's attack on the legality of the PA USF:

The PUC accordingly points out that Bell and other[s that oppose the USF] are barred at the outset under judicial estoppel principles from questioning the PUC's statutory power to employ the USF concept by their on-record advocacy of the above-described \$20.5 million dollar USF proposal, expressly stated by them in the 1649 Petition as *designed to address universal service issues in a pragmatic, but equitable, manner that provides benefits to all parties and promotes the public interest.*<sup>243</sup>

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<sup>242</sup> RD at 132.

<sup>243</sup> *Global Appeal*, 763 A.2d at 495.

Thus, as Verizon itself had agreed to in proposing the PA USF, the PA USF presented a pragmatic solution to a problem in a manner that benefitted all parties and promoted the public interest.

Second, the structure of the PA USF and its manner of funding was also of Verizon's own design. In other words, if as Verizon claims it may wind up paying more in PA USF support than the access reductions it will realize, it is because the present contribution formula is based upon a percentage of total intrastate revenues, which includes local revenues (and not just a calculation of the relative access revenues and expenses). As PTA witness Zingaretti noted, the only fact proven by the magnitude of Verizon's contribution to the USF is its status as the dominant carrier in Pennsylvania.

ALL CARRIERS contribute the SAME PERCENTAGE of intrastate revenue to the PAUSF. So Verizon contributes the same percentage as Yukon Waltz Telephone Company. If Verizon had less retail revenue, it would pay less. The fact that Verizon pays more into the PAUSF than other carriers indicates simply that Verizon earns more intrastate revenues than other carriers.<sup>244</sup>

### **3. The Current PA USF Regulations Do Not Present a Regulatory Hurdle to Expansion of USF Funding to Support Expansion of Access Reductions**

As a legal matter, the ALJ concluded that, while expansion of the fund to accommodate additional access reductions is consistent with the fund's original purpose, the fund could not be expanded because the current regulations contain no language that would allow it. The ALJ's recommended rejection of additional USF support on the basis that the current regulations do not provide a mechanism to account for additional contributions is an overly restrictive recommendation, which is easily and readily avoidable.

This Commission has always contemplated that further access reform could necessitate

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<sup>244</sup> PTA Rejoinder at 9 (emphasis in original).

further regulatory reform. In approving the RLECs' Phase II USF/Access reform in 2003, the Commission agreed "to open a rulemaking proceeding to be initiated no later than December 31, 2004, to address what if any modifications should be made to the PaUSF regulations[.]"<sup>245</sup> In the myriad orders that followed, the Commission continued to contemplate a potential rulemaking to effectuate whatever results it ordained following its concomitant investigation whether access rates should be further reduced, and if so, what rates or other forms of support would be impacted.<sup>246</sup>

The Commission already has pending before it ALJ Colwell's recommendation to open a rulemaking to address changes to the PA USF. While the PTA, in pending exceptions to that recommendation, disagrees with the Judge's proposed restrictions on the future structure of the PA USF, the PTA does agree that a rulemaking should be an available avenue of recourse if the Commission is going to continue to pursue access reform. In that rulemaking, the Commission may easily adjust its formula in Section 63.165 of the USF regulations to provide for contributions that are calculated based upon the implementation of additional access reductions.<sup>247</sup>

Such action would precisely mirror the Commission's actions following the adoption of the *Global Order*, in which the Commission adopted access reform, and then implemented it through a subsequent rulemaking. The only difference between then and now is that in the *Global Proceeding*, the 1648 and 1649 Petitioners both had substantially agreed to, and attached

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<sup>245</sup> *July 15, 2003 Order* at 12.

<sup>246</sup> See e.g. *November 15, 2006 Investigation Order* at 16 ("Since there has been no resolution to access charge reform, the *status quo* stays in place, and the Pennsylvania Universal Service Fund shall continue under the existing regulations codified at 52 Pa. Code §§ 63.161-63.171 until such time as regulations are promulgated eliminating or modifying the Fund."), as repeated in the *August 5, 2009 Investigation Order* commencing this investigation, at 22, Ordering Paragraph No. 7.

<sup>247</sup> During this rulemaking, the Commission could also implement the PTA's recognition that in order not to "guarantee" revenue neutrality on a going forward basis, the size of the USF receipts for price cap carriers would no longer be based upon the number of access lines.

to their respective petitions, proposed regulations that served as the Commission's spring board for the subsequent rulemaking. In this proceeding, while the parties disagree over the continued life of the PA USF, the existing regulations, whether repealed or modified, likewise will again serve as the spring board for the Commission's rulemaking.

**E. Exception No. 5 - Reasonable Glide Path and Rates. The Recommended Decision Fails to Adopt Rationale and Balanced Resolution of Access Reductions. (RD at 131-140; FOF Nos. 75-89; COL No. 39-40).**

The PTA has previously proposed, and continues to urge, that the Commission adopt the same rational and pragmatic approach to access rates that prevailed in 1999 (*Global Order*) and again in 2003 (Phase II).

There are three "legs" to telephone company rate design – local rates, access rates and USF. If one aspect is impacted too aggressively, then adverse consequences are created elsewhere. Hence, the ALJ's recommendation to precipitously reduce access rates to interstate levels without USF support then forces RLEC local rates to escalate dramatically. The solution is a more moderate approach.<sup>248</sup>

The Commission should not force rapid escalations in local rates. Since lowering state access rates to interstate parity without USF support has this result, either USF support must be provided or access rates not set so low. If the Commission does not want to expand the USF, then a lesser access charge reduction should be considered that would increase local rates only up to an acceptable benchmark. For example, setting the traffic sensitive component of access rates at parity is a \$10.4 million rate reduction for the IXCs. If the Commission desires a

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<sup>248</sup> FCC, National Broadband Plan at 141 ("Sudden changes in USF and ICC [Intercarrier Compensation] could have unintended consequences that slow progress. Success will come from a clear road map for reform, including guidance about the timing and pace of changes to existing regulations, so that the private sector can react and plan appropriately.").

reduction also in the CCL component, then the reduction should be set so that local rates are not set higher than a reasonable level (the PTA suggests \$18.94).

Beyond this level, the PA USF should be used. Even were the Commission to use a cost basis of rate setting, which it never has and should not now, some portion of the loop should be recovered from the IXCs and their contribution to the PA USF would accomplish this purpose. The USF is hardly as odious as the IXCs make it appear.<sup>249</sup>

If the PA USF is not employed, then the state CCL charge, which is the only meaningful difference between intrastate and interstate access rates, should not be eliminated. This rate element recognizes the IXCs' use of the local loop and resulting revenue responsibility of access customers. Further, because local rates cannot accommodate the large revenue shifts that parity would create and, since the IXCs are not willing to increase PA USF funding levels, solutions appear difficult to realize. The IXCs already enjoy substantial rural access reductions (one-half *billion* dollars over the last ten years<sup>250</sup>), and have shown no compelling reasons for the Commission to act further at this time.

The role of the PA USF was critical to past success and will continue to be important. As the PTA has noted elsewhere, part of the next stage of this proceeding should address expanding the PA USF contributors to include VoIP and wireless carrier funding. While the Commission has decided that this topic should not be raised in this phase of the proceeding, it needs to be resolved as part of the "puzzle."

Finally, there should be no RLEC reductions using a statewide policy that does not also apply to Verizon. Verizon represents approximately 85% of the ILEC access lines in Pennsylvania and changing the rates for RLECs only based upon a new policy of complete

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<sup>249</sup> At the federal level, Verizon and AT&T are the largest universal service fund recipients "by far." PTA Direct at 23.

<sup>250</sup> PTA Direct at 10.

mirroring of both traffic sensitive and non-traffic sensitive rate elements is hardly “generic reform.”

While the PTA Companies continue to believe that premature action will penalize Pennsylvania, to the extent that the Commission feels compelled to act, the PTA supports a collaborative process. Litigation is not the best way to resolve the IXCs’ concerns. In the past, access reductions have moved forward because the parties worked together to make the change possible. That was true in the Global Proceeding, where the PTA was able to construct a plan that the other parties found acceptable. It was the same means used again in 2003 (Phase II). Litigation of public policy issues is not effective. That is particularly true here, where the issues have been bifurcated (even trifurcated, if PA USF contributions from wireless and VoIP carriers are included in a subsequent rulemaking phase).

The PTA suggests, instead, that the parties agree to a collaborative process, which is confidential so candor is encouraged, where the parties work out their differences instead of engaging in litigation bravado. For its part, the PTA commits to work with the parties to make progress on access changes. The solution must remain focused on the three acknowledged moving parts, access rates, end user rates and the PA USF, which are balanced to obtain a reasonable result which benefits them all.

The PTA proposes the following principles be followed:

- **Benchmark Rate.** A reasonable current residential benchmark rate is \$18.94 based upon comparability, which would be revised based upon Verizon urban rate changes.
- **Intrastate Switched Access Rates.** Intrastate access rates should be reduced to interstate parity over a reasonable period of time, offset by a combination of local rate increases and USF support. Other states have adopted a seven to ten year “glide path” with equal access charge reductions over that period of time.
- **Local Rate Increases and USF.** Subject to working out the specific numbers and details, retail rates up to the benchmark rate, as adjusted every year, would be the

first source of access charge reduction revenue neutrality, with the incremental PAUSF only relied upon after the benchmark is reached.<sup>251</sup>

- **PA USF Design for Price Cap Companies.** Any incremental amounts distributed from the PAUSF to offset intrastate switched access charge reductions (after retail increases are accounted for) should be reduced as Price Cap Companies experience reductions in the number of access lines.<sup>252</sup>
- **Broadening the Contribution Base.** The contribution base for the PA USF should be expanded to include wireless carriers and VoIP service providers.
- **Federal Changes.** Any Pennsylvania changes need to be harmonized with the Federal outcome.<sup>253</sup>

The PTA Companies propose that these principles, which are an accommodation of all parties' perspectives, represent a moderate and rational point of view, and, importantly, would minimize harmful impacts to rural Pennsylvania consumers. This template should be adopted by the Commission, with the parties allowed to develop the details and present an implementation plan.

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<sup>251</sup> Since rates for business customers vary greatly between local exchange carriers (as well as between residential and business customers in the rate structure of each RLEC), and are often subject to contracts, business rates could follow a similar rate of change subject to the current business rate mark-up above residential rates, market conditions, and/or contractual restrictions, and the Commission's decision in the Colwell proceeding regarding the business rate cap.

<sup>252</sup> This should be achieved by initially calculating incremental PAUSF support on a per line basis for each Price Cap Company and distributing the support based on the number of access lines, adjusted annually, in service for each Price Cap Company.

<sup>253</sup> PTA Surrebuttal at 61-62.



### III. CONCLUSION

For the reasons discussed above, the Pennsylvania Telephone Association respectfully requests that these Exceptions be granted.

Respectfully submitted,



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**APPENDIX A**

**PENNSYLVANIA  
TELEPHONE ASSOCIATION**

**PROPOSED FINDINGS OF FACT  
AND CONCLUSIONS OF LAW**

## PENNSYLVANIA TELEPHONE ASSOCIATION

### PROPOSED FINDS OF FACT AND CONCLUSIONS OF LAW

#### I. PROPOSED FINDINGS OF FACT

1. Until the FCC gives a clear indication of the direction it intends to pursue, the Commission should retain the status quo. PTA Direct at 48-49; PTA Surrebuttal at 55.

2. There should be no RLEC reductions using a statewide policy that does not also apply to Verizon. PTA Direct at 56.

3. Verizon represents approximately 85% of the access lines in Pennsylvania and changing the rates for RLECs only based upon a new policy of complete mirroring of both traffic sensitive and non-traffic sensitive rate elements is not generic reform. PTA Direct at 56.

4. A reasonable benchmark is appropriate. PTA Direct at 3-4; PTA Surrebuttal at 61-62.

5. A reduction in intrastate access rates to interstate parity over a reasonable period of time is reasonable. PTA Direct at 3-4; PTA Surrebuttal at 61.

6. Subject to working out the specific numbers and details, retail rates up to the benchmark rate, as adjusted every year, would be the first source of access charge reduction revenue neutrality, with the incremental PA USF only relied upon after the benchmark is reached. PTA Surrebuttal at 61.

7. Business rates could follow a similar rate of change subject to the current business rate mark-up above residential rates, market conditions, and/or contractual restrictions, and the Commission's decision in the Colwell proceeding regarding the business rate cap. PTA Surrebuttal at 62.

8. Any incremental amounts distributed from the PA USF to offset intrastate switched access charge reductions should be reduced as Price Cap Companies experience reductions in the number of access lines. This should be achieved by initially calculating incremental PA USF support on a per line basis for each Price Cap Company and distributing the support based on the number of access lines, adjusted annually, in service for each Price Cap Company. PTA Surrebuttal at 62.

9. There are two principal regulated telecommunications services provided by the RLECs: retail local service (dial tone service); and the use by other carriers of the local network to originate and terminate phone calls (switched access service). PTA Direct at 5.

10. Access customers are charged a combination of usage-based (traffic sensitive) rates and a monthly flat carrier common line charge (CCL). PTA Direct at 6.

11. Per the *Global Order*, the RLECs mirrored their interstate traffic sensitive charges (i.e., the per minute and mileage based rates). As to the non-traffic sensitive component, the Commission restructured the rate to a flat-rated carrier charge -- the CCL -- and targeted an intrastate monthly rate of \$7.00 per line. PTA Direct at 8.

12. Under the *Global Order*, the PTA Companies' access rates were reduced by \$15.8 million from \$0.066 per minute to an average level of \$0.051 per minute. PTA Exs. GMZ-3, 4, 5.

13. To replace the reduced access rate revenues, the PTA Companies' local rates were increased by \$3.3 million and the PA USF was implemented. PTA Ex. GMZ-5.

14. These actions were deployed in a revenue neutral fashion. PTA Direct at 8.

15. Access rates were declared by the Commission to be just and reasonable. PTA Direct at 8.

16. Verizon specifically declined receipt of universal service funding as part of its own access rate changes. PTA Direct at 8.

17. Additional RLEC access reductions followed those ordered in the *Global Order*. PTA Direct at 9-10.

18. The PTA Companies' access rates were not tied to Verizon's access rates in any fashion. PTA Direct at 8, 47.

19. After a collaborative effort that included all stakeholders the Commission approved a Joint Access Proposal to further reduce the RLECs' access charge (Phase II). All changes in Phase II were accomplished on an explicitly revenue neutral basis. PTA Direct at 9.

20. As a result of the PTA Companies' Phase II access rate efforts, the RLECs further decreased access rates by \$27.2 million. PTA Direct at 9-10.

21. The PTA Companies increased their basic residential and business local service rates and received an additional \$2.2 million from the PA USF. PTA Direct at 9-10.

22. These access rates were also declared by the Commission to be just and reasonable. PTA Direct at 9-10.

23. Throughout these generic proceedings, individual companies have submitted filings that reduced access charges. PTA Direct at 9-10.

24. In total, the sum of all access rate changes, generic and individual undertaken as of the time the *Global Order* was entered, the PTA Companies have reduced their collective access charges by an average of \$44.3 million annually. PTA Ex. GMZ-6.

25. Changes in intrastate access rates equates to almost one half one half a billion dollars of rate relief for the IXCs over the last ten years. PTA Direct at 10.

26. The beginning access rate in 1984 averaged \$.10 per minute. The average PTA Company access rate today is \$0.048 or 50% less than the original just and reasonable rates. AT&T Direct at 13.

27. Over the same time frame, local rates have increased in the magnitude of 55%. PTA Direct at 10.

28. The average RLEC local rate increased from \$10.12 to \$15.57 during the last 10 years. During this same time frame the residential subscriber line charge increased from \$3.50 to \$6.50 per month. Combined, this represents an increase of \$8.46 per month, or a 62% increase for residential service. PTA Direct at 10.

29. Interstate access rates have moved lower than intrastate rates due to the FCC's removal of all contribution for the shared local loop that were previously included in interstate switched access rates and the establishment of several explicit USF support mechanisms. PTA Direct at 10-11.

30. Interstate services still contribute to universal service. The only difference is that the contribution has been made explicit through the interstate end-user SLC and federal universal service support. PTA Direct at 11.

31. Were it not for Subscriber Line Charges and the federal universal service fund, interstate switched access rates likely would be much higher today and much closer to or possibly even higher than the levels of intrastate switched access rates. PTA Direct at 11.

32. The FCC has always recognized that smaller carriers must be treated differently to ensure that they can continue to serve customers in high-cost areas. PTA Direct at 12.

33. Service areas served by rural carriers are vastly different from those served by the Regional Bell Operated Companies (RBOCs), and, therefore, their access reform needs to reflect such differences. PTA Direct at 12-13.

34. The RLECs' interstate access rates are lower than their intrastate counterpart (in all cases except one), only when the state CCL is included in the calculation. PTA Direct at 14.

35. The RLECs' traffic sensitive intrastate rates are not greatly higher than their traffic sensitive interstate rates. PTA Ex. GMZ-8.

36. Half of the PTA Companies have intrastate traffic sensitive rates that are actually lower than their interstate TS rates, and would have to be increased to achieve TS rate parity. PTA Direct at 14.

37. Mirroring just the traffic sensitive component, which is the component that the Commission calibrated in 1999 and 2003, would reduce the PTA Companies' access revenues by \$10,422,627 or 23% net overall. PTA Ex. GMZ-9; PTA Direct at 14.

38. The PTA has previously recommended and the Commission has agreed that the *traffic-sensitive* components should be recalibrated periodically to match the interstate component. On two occasions post divestiture, in 2000 and 2003, this was done as part of the overall generic changes. However, this was not inclusive of the non-traffic sensitive CCL, nor were intrastate traffic sensitive components required to continue to mirror, hence the deviation over time. PTA Direct at 15.

39. The impact of complete mirroring (eliminating the CCL) on the PTA Companies would be a reduction in intrastate revenue of \$63,910,478 or 65%. PTA Ex. GMZ-10; PTA Direct at 16.

40. Current PA USF universal service support represents an additional \$23.5 million in annual revenues to the PTA Companies. Combined, this means more than \$87 million (of PTA Company revenue) is at risk, representing 24% of total regulated intrastate operating revenue, if access rates are further reduced with no further USF support. PTA Ex. GMZ-11; PTA Direct at 16.

41. The median revenue reduction would be 27%. PTA Direct at 16.

42. AT&T and Verizon are huge, mega-carriers compared to the Pennsylvania RLECs. Nationally, in 2007 the holding companies of these top two ILECs accounted for 76% of the local loops. PTA Direct at 31.

43. AT&T, Verizon, Sprint, and Comcast are ranked 1<sup>st</sup>, 2<sup>nd</sup>, 3<sup>rd</sup>, and 4<sup>th</sup>, respectively, among the Fortune 500 telecommunications companies. PTA Direct at 31.

44. Of the 32 RLECs in this proceeding, only CenturyLink (formerly Embarq) and TDS made the top 500, near the bottom at 405<sup>th</sup> and 465<sup>th</sup>, respectively. PTA Direct at 31.

45. Many of the RLECs represented in this proceeding by the PTA are much, much smaller and not publicly traded. PTA Surrebuttal at 35-36.

46. The RLECs in this case cannot compare in terms of size and scope with the IXC's seeking reduced access rates. PTA Surrebuttal at 35.

47. AT&T is the largest communications holding company *in the world* by revenue. PTA Direct at 31.

48. AT&T's 2008 reported consolidated revenue was more than \$124 billion, with \$12.9 billion in profits, up 7.7% from 2007. PTA Direct at 32.

49. Verizon's operating revenues for 2008 were \$97.4 billion, an increase of 4.2%, or 5.1% on an adjusted basis over the prior year. PTA Direct at 32.

50. In 2008, Comcast grew its consolidated revenue by 10.9%, to approximately \$34.3 billion and increased consolidated operating income by 20.7% to approximately \$6.7 billion. PTA Direct at 32.

51. In early 2009, Comcast announced that it had surpassed Qwest as the third largest residential phone service provider in the county. PTA Direct at 32.

52. In published articles and sworn testimony to the FCC, the IXCs and their parent companies have listed many reasons for the pressures on their long distance businesses. The level of the Pennsylvania RLECs' intrastate access rates is not among them. PTA Direct at 4-5.

53. The toll market is declining for a variety of reasons, none of which relates to intrastate access charge levels. The IXCs have been in the process of abandoning the IXC market due to factors much more powerful than access, including primarily changing technology and customer preferences. PTA Direct at 37-38, 40-41; PTA Ex. GMZ-15.

54. After the RLECs' access charge reductions in the Phase II reform, AT&T raised rates for its all-distance bundles in Pennsylvania by anywhere from \$2 to \$5, and increased the monthly recurring charge on many plans typically by either \$1 or \$2, as well as increased a number of basic rates for international service. PTA Ex. GMZ-15.

55. AT&T's claims of historic benefits and promises of future Pennsylvania customer benefits resulting from intrastate access charge reductions are illusory and deceptive. PTA Direct at 39.

56. AT&T has decided to grow its revenues in its other businesses, including wireless and broadband, and put little to no more investment into the wireline segment, because of a shift in technology, not because of the level of rural intrastate access charges. PTA Direct at 40.

57. For AT&T, Verizon, Sprint, and Comcast, today's operations are clearly driven by changes in technology, particularly the growth in the wireless and data sectors. PTA Direct at 41.

58. Reductions to the intrastate access charges of 14% of Pennsylvania's access lines, which if reduced to their interstate levels will mean a combined savings of less than \$64 million to these national and international entities, will have little or no effect on further promotion of wireline toll competition, particularly in rural service territories. PTA Direct at 41.

59. Intercarrier compensation rules have not allowed an unlevel playing field to develop with respect to wireless services. Wireless service is growing because of mobility, convenience and the high tech functionalities of the phones. PTA Direct at 42-43.

60. This overall maturation of technology and usability has driven the growth of competitors' lines, including the wireless carriers, at the expense of the traditional fixed lines. Access rates have nothing to do with it. PTA Direct at 43.

61. While the IXCs complain that the FCC has approved a different intercarrier compensation scheme for wireless carriers, this is a federal policy decision. PTA Direct at 44.

62. The principal wireless carriers that have benefited from the FCC's rate design are the biggest ones – AT&T Wireless, Verizon Wireless and Sprint/Nextel. PTA Direct at 43.

63. Any conclusion the Commission reaches in this case will not impact wireless carrier's ability to bill access charges for terminating interexchange traffic. PTA Direct at 44.

64. Reducing the RLECs' intrastate access rates simply benefits the IXCs' wireless affiliates even more. PTA Direct at 44.

65. The PTA RLECs' access rates do not create a competitive disadvantage for CLECs. PTA Surrebuttal at 22.

66. Cable telephony providers and CLECs in general are permitted to charge the same rate level as the RLECs. Sprint Rebuttal at 22.

67. When a CLEC serving area includes multiple LECs, it is also allowed to develop and bill a blended access rate for all traffic. PTA Surrebuttal at 23.

68. Comcast's tariffs both call for the application of different intrastate switched access rates based on the incumbent LEC. PTA Surrebuttal at 23.

69. All intrastate access customers pay the same rates. PTA Direct at 46.

70. The Commission has approved these tariffed rates and the tariffs are applied uniformly. PTA Direct at 46.

71. The same applies to an interstate call, for which carriers all pay the FCC tariffed rate. PTA Direct at 46.

72. The lack of parity between interstate and intrastate rates is not discriminatory. PTA Direct at 45-46.

73. The PTA Companies currently charge the access rates contained in their Commission-approved tariffs, which rates have been found to be just and reasonable. PTA Ex. JLL-1 (Colwell Benchmark/USF Proceeding); PTA Direct at 8-10.

74. There is no such prescription in PTA Companies' Chapter 30 Plans that intrastate access charges be reduced to interstate levels or some other arbitrary benchmark. PTA Direct at 46.

75. The issue whether to reduce intrastate access rates further is one of policy, not law. Tr. at 239, 319, 338-39, 349, 356-67, 384, 428, 511; PTA Direct at 46; OTS Direct at 10; Sprint Rebuttal at 34; Verizon Rebuttal at 28; PTA Ex. GMZ-4.

76. In terms of guaranteeing to the Commission that hard and fast benefits will flow through to Pennsylvania consumers, the IXCs do no more than offer up more economic theory and platitudes. PTA Surrebuttal at 53-54.

77. In terms of real benefits, the carriers offer little the Commission, or any consumer, can wrap their hands around. PTA Surrebuttal at 54.



78. The purported benefits espoused by the carriers are speculative, and in fact disproved by past performance. PTA Direct at 39.

79. While AT&T promises in this proceeding to reduce its \$0.94 per line In-State Connection Fee, the total amount of the reduction is unspecified, and unenforceable. PTA Direct at 37.

80. Even were the entire \$.94 eliminated, this would not come close to offsetting the huge local rate increases that will result. PTA Direct at 37.

81. AT&T's access savings will flow directly to AT&T for whatever purposes it chooses. PTA Direct at 37-38.

82. Verizon and Sprint do not agree to provide any specific benefits. PTA Direct at 38.

83. The FCC is under intense pressure to move its intercarrier compensation proceeding along, notably from Verizon and AT&T. PTA Direct at 4.

84. Several proposals hint at or directly suggest federal preemption over state access rates. Others propose a further manner of federal funding that would harm Pennsylvania consumers if this Commission acted now. PTA Direct at 47-48.

85. On March 16, 2010, the FCC released its much awaited National Broadband Plan (NBP). PTA Surrebuttal at 55.

86. With regard to intercarrier compensation, the FCC states that it will adopt a framework for long term reform that lowers per minute access charges. In the initial stages of the NBP, intrastate switched access rates would be reduced to interstate levels over a period of time. To offset the revenue reductions, the NBP would allow gradual increases in SLC rates and provide support from the new "Connect America Fund," intended to support the provision of affordable broadband and voice service. PTA Surrebuttal at 55.

87. It would be a mistake for Pennsylvania to get out in front of the FCC's NBP efforts. PTA Surrebuttal at 55.

88. Depending on the outcome of that proceeding, a Pennsylvania customer's total monthly bill may increase substantially even without any further action by this Commission. PTA Direct at 48.

89. Further, to undertake state access reductions at this time may jeopardize additional federal funding to Pennsylvania consumers. PTA Direct at 48.

90. Pennsylvania ratepayers may have to absorb the FCC plan's higher SLCs and USF surcharges in addition to the local rate increases that resulted from this Commission's state access rate reductions. PTA Direct at 49.

91. Acting before federal changes are in place could exacerbate Pennsylvania's current status as a net contributor into federal universal service support. PTA Direct at 49.

92. A reduction of the RLECs' intrastate access charges, particularly without the concomitant provision of replacement external support through a universal service fund, will result in a direct transfer of almost \$100 million from the RLECs and their customers to AT&T, Verizon, Sprint, Comcast, and Qwest. PTA Direct at 17.

93. In 2008, the PTA Companies reported a combined \$109 million in total company regulated operating income in their PUC Annual Reports. PTA Ex. GMZ-11; PTA Direct at 17.

94. More than 80% of the RLEC operating income would be in jeopardy, with that income shifting to the IXCs. PTA Direct at 18.

95. The RLECs use this money, earned under federal regulations and their Chapter 30 Plans, to maintain and improve their networks, the only network that guarantees voice and broadband access for all in rural service territories. PTA Direct at 18.

96. The access revenues that the RLECs receive are extremely important to their day-to-day operations and maintenance of their networks. PTA Direct at 50.

97. Prior access reductions in 2000 and 2003 were undertaken on an expressly "revenue neutral basis" by the Commission. This was accomplished by a combination of local rate increases and the state USF funding. PTA Direct at 8-9.

98. In a complimentary fashion, the Chapter 30 Plans, contemporaneously adopted by the Commission, recognize exogenous events as recoverable for the PTA Companies, including subsequent regulatory and legislative changes (state and federal) which affect revenues or expenses, to the extent not captured in GDP-PI. PTA Direct at 41.

99. Exogenous revenue changes shall be flowed through on a dollar-for-dollar basis, utilizing the most recent per book revenue levels, without any investigation or review of earnings. PTA Surrebuttal at 41.

100. Revenue neutrality must provide the PTA Companies with a realistic opportunity to increase revenues that are regulated by this Commission, in a manner which will offset access reductions on a dollar-for-dollar revenue basis. PTA Direct at 51-52; PTA Surrebuttal at 41.

101. In other words, the Commission must design access reductions so that the RLECs have a real chance to actually recover the lost revenue. PTA Direct at 52.

102. Basic local service rates and the PA USF are the only practical sources available to insure revenue neutrality. PTA Direct at 52.

103. The IXCs' proposals are not revenue neutral. PTA Surrebuttal at 42-47.

104. Imposing more increases on already high, local rates, when this Commission is well-aware that those levels of revenues will never be realized, is inappropriate. PTA Direct at 52.

105. The RLECs' local service territories are not fully competitive, yet there is substantial competition. PTA Surrebuttal at 26.

106. RLECs face the inequitable situation of being highly regulated carrier with obligations to serve everywhere, but facing competitor carriers that have no requirement to serve and no regulation. PTA Surrebuttal at 26-30.

107. The PTA Companies serve very rural areas. As a group, the small companies serve an average of 30.5 lines per square mile. PTA Direct at 28; PTA Ex. GMZ-14.

108. The "larger" RLECs, FairPoint, Frontier, Consolidated and Windstream, are only marginally more dense with only 49.4 lines per square mile. PTA Ex. GMZ-14.

109. Verizon, by comparison, has a density factor of 193.2 customers per square mile, almost four times more dense than the average "mid-tier LEC" and approximately six times more dense as the average small LEC, and well above the state average of 130.3 lines per square mile. PTA Direct at 27.

110. Verizon serves *all* the urban areas of Pennsylvania without exception and nationally, is divesting much of its rural operations. PTA Direct at 26-27; PTA Surrebuttal at 33.

111. By contrast, the largest city served by any of the Commission-designated RLECs is Chambersburg, served by CenturyLink, which is a town of 18,000 residents. Beyond that, the service territories of the RLECs are composed of villages and hamlets. PTA Direct at 26-27.

112. The prospective business plans of the IXCs and their parent companies do not endorse strengthening and maintaining the rural wireline network. PTA Direct at 24-25.

113. Sprint's coverage map and statements on its website show large portions in Pennsylvania that are either not served or where service is rated as only good to fair. PTA Ex. GMZ-18.

114. While Sprint has made some rural investment, Sprint's largest investments are made in the more densely populated counties and those surrounding them, like the five county Philadelphia area. PTA Surrebuttal at 34.

115. The PTA Companies remain ever more fully committed to serving rural, wireline customers. PTA Direct at 26.

116. In the geographic and customer mix of the IXCs and their parent companies, these carriers have been allowed to develop selectively to focus on lower-cost urban areas against which higher rural costs can be averaged. PTA Surrebuttal at 35.

117. Because of their significantly larger customer base and service to Pennsylvania's most dense population areas, the IXCs and their parent companies can average costs better than the RLECs. PTA Direct at 27.

118. Given that rates in urban areas of Verizon are still higher than those in Verizon's rural areas, it would appear that Verizon's internal cross-subsidization between urban and rural rates continues. PTA Surrebuttal at 33.

119. The PTA Companies, on the other hand, lack the size and scope in customer base that allows them internally to "average down" their costs per customer. PTA Direct at 27.

120. Without an urban customer base to "average down" their costs per customer, the RLECs are legitimately seeking external support for rural telephone consumers. PTA Surrebuttal at 33.

121. The RLECs simply do not have the same scope or scale or economies enjoyed by companies, like AT&T and Verizon, former RBOCs that are now even larger following multiple mergers and acquisitions, taking them well beyond their original RBOC size immediately post-divestiture. PTA Direct at 27.

122. The major driver of a wireline carrier's cost is the rural nature of the area served. PTA Direct at 28.

123. Rural service territories lack the other characteristics (dense populations, low cost service areas, large business customer bases) that more readily provide large non-rural carriers the ability to sustain and internally support affordable local rates. PTA Direct at 28.

124. It is the service area characteristics, and not the size of the serving carrier or level of success, that determines the PTA Companies' eligibility for universal service support. PTA Direct at 31.

125. Corporate affiliation does not affect the higher network costs of a rural territory. The mid-size RLECs and the small independent RLECs, all of which comprise the PTA Companies, share significant service similarities. PTA Direct at 27.

126. The PTA Companies have many regulatory burdens associated with their traditional (and continuing) role as providers of last resort. PTA Direct at 29.

127. The RLECs have an obligation to serve which has never been diminished or moderated by the Commission. PTA Surrebuttal at 29-30.

128. Unregulated carriers, cable voice and wireless have no obligation to serve. PTA Surrebuttal at 26-30.

129. Regulated CLECs have no GLR obligation. PTA Surrebuttal at 28.

130. The cost of the COLR obligation has never been identified by any type of cost study and it is unknown how to do one without separate account tracking and special accounting systems, which do not exist. PTA Surrebuttal at 30.

131. The task is made more difficult, not just because the areas of competition are imprecisely undefined, but also because the "costs" themselves are undefined and an appropriate methodology has never been set. PTA Direct at 29.

132. Just because the cost of providing COLR service may be difficult to calculate does not mean it does not exist or that it is not substantial. PTA Direct at 29.

133. COLR requirements impose substantial costs upon the RLECs. PTA Direct at 29.

134. If the IXCs' revenue reductions are assigned entirely to the RLECs' end use customers, to a local rate increase of \$7.32 per line on average, or a 47% rate increase would result. PTA Ex. GMZ-13; PTA Direct at 18.

135. These rates will far exceed Verizon's own rural rates (Density Cells 3 and 4), which currently range from \$11.95 to \$15.40. Verizon Rebuttal at 37.

136. All customers in RLEC rural areas will be charged more than in Verizon's rural area if the IXCs have their way. PTA Surrebuttal at 47-48.

137. The rates will also exceed that national average by a considerable margin. PTA Ex. JLL-3 (Colwell Benchmark/USF Proceeding).

138. The RLECs have declined to use the allowable revenue increases calculated under their Chapter 30 plans to increase rates to generate higher revenues and income for themselves. As of June 2008, there were approximately \$22 million in "banked" allowable revenue increases (i.e., unused rate relief), and that figure, as of January 2010, has now ballooned to almost \$30 million. During the time frame that these banks were accumulated, only \$18.8 million in rate increases were taken (mostly to ancillary services). PTA Direct at 19.

139. The RLECs have only been able to implement less than two-fifths (2/5) of their regulatorily allowable rate increases. PTA Direct at 19.

140. PTA Companies served 841,981 access lines in 2005. By 2008, this figure dropped to 717,935, a 17% decline over 3 years. PTA Direct at 19.

141. The line losses to the PTA Companies are staggering and reflect the reality of the major shift now occurring in telecommunications. PTA Direct at 19.

142. Increasing local rates will actually result in less revenue, not more. PTA Direct at 20.

143. Based upon already experienced line losses at current local rate levels, further local line losses will accelerate dramatically in response to the final rates set forth in AT&T Attachment 5. PTA Surrebuttal at 49.

144. RLECs will be unable to pass the proposed increases on to their remaining customers, which means the RLECs will have to absorb the revenue reductions and will have to reduce the capital expenditures needed to continue to provide quality service to rural customers in Pennsylvania. PTA Surrebuttal at 49.

145. The opponents of PA USF support all receive support at the federal level and in some states. PTA Direct at 22-24.

146. The availability of federal high cost loop (HCL) support is irrelevant for PA USF support purposes. PTA Direct at 24, 33.

147. Restricting state support only to those PA RLECs receiving HCL support ignores the flaws in the HCL mechanism as well as the other mechanisms the FCC has implemented. PTA Direct at 24.

148. Lack of high cost loop support on the federal level does not mean that a company does not have high loop costs. It merely means that the USAC has limited loop support because of the limited amounts of federal USF loop support available. PTA Direct at 33-35.

149. The federal IAS and ICLS funds are closer proxies to the current PA USF and for the current proposed round of access reductions. PTA Direct at 33-35.

150. The IAS and ICLS funds are more similar to the PA USF than the HCL Fund because they represent the direct explicit support that was created when the implicit support from interstate access rates was reduced. PTA Direct at 34.

151. Interstate access charge reductions that are **not** shifted to the end user through higher Subscriber Line Charges are recovered by carriers via the ICLS or IAS. PTA Direct at 34.

152. The PA USF was never intended to terminate or discontinue. PTA Surrebuttal at 18.

153. The *design* of the PA USF was interim, the *existence* of the Fund was not. PTA Surrebuttal at 18.

154. The PA USF adopted by the Commission clearly provided that, if the PA USF were eliminated and no replacement funding adopted in its place, the access rate reductions and existing PA USF credits on customer bills would be immediately reversed. PTA Surrebuttal at 18.

155. By failing to include it in its complaint, it is clear that AT&T was not seeking retroactive refunds. AT&T did not address retroactive refunds in its direct testimony, and essentially withdrew any claim at the hearing. PTA Direct at 53; Tr. 195.

156. Switched access customers represent only 0.18% of total customers. PTA Ex. GMZ-16.

157. The effect of AT&T's complaint on total gross annual intrastate operating revenues, in the event access charges were reduced, will always be zero because revenue must be raised by an equal amount elsewhere. PTA Direct at 54.

158. The services provided by the RLECs are the same – telecommunications – and are not two or more types of service. This is unlike a situation of a combined services company (for example, the combined water and gas operation of the former PG&W). PTA Direct at 54.

159. The function of the two basic services at issue in this case, local network dial tone and access, both are the provision of the local network to complete or terminate a call. These services comprise the “type of service” the RLECs provide. PTA Direct at 54-55.

160. In lieu of compliance filings subject to fast-track comments and replies, a more efficient manner of implementing any mandated rate changes, including updating rate elements, would be technical conferences involving the parties and Commission staff as were used in both previous rural access reform proceedings. PTA Rejoinder at 11-12.

## II. PROPOSED CONCLUSIONS OF LAW

1. In a proceeding involving a complaint against existing rates, the burden of proof is on the complainant. 66 Pa.C.S. § 332(a).
2. With respect to the investigation issues in this proceeding, the burden of proof is on the RLECs to demonstrate that their existing rates are just and reasonable. 66 Pa. C.S. § 315(a).
3. As tariffed rates approved by the Commission, which today remain in full compliance with all applicable statutes, rules, and orders regarding intrastate access rates, the PTA Companies' have met their burden of proving that their existing intrastate access rates are just and reasonable. 66 Pa. C.S. § 315(a).
4. The PTA Companies' existing intrastate access rates are just and reasonable. 66 Pa.C.S. §§ 1301, 3015(g).
5. Intrastate access rates are not discriminatory. 66 Pa.C.S. §§ 1304, 3011(3).
6. The PTA Companies' existing rates remain in full compliance with existing statutes, Commission orders, their tariffs, and their Chapter 30 Plans. 66 Pa. C.S. §§ 1301, 1303, 1304, 3011-3019.
7. The level of intrastate access charges is not explicitly referenced in the preamble to Act 183 or anywhere else. 66 Pa. C.S. §§ 3011(1)-(13).
8. The original 1993 Chapter 30 contained a specific statement in the text of the statute that access charges should be reduced to a level below \$0.125 cents for companies with more than 250,000 access lines. 66 Pa.C.S. § 3007(1).
9. Act 183 no longer requires intrastate access reductions and mentions access rates only with respect to mandating revenue neutrality to the RLECs if access rates are compelled to be reduced. 66 Pa. C.S. § 3017(a).
10. Current intrastate access rates will remain just and reasonable in compliance with all applicable statutes, regulations, and orders if not reduced further. 66 Pa. C.S. §§ 1301, 3015(g).
11. The Commission may not require a local exchange telecommunications company to reduce access except on a revenue neutral basis. 66 Pa. C.S. § 3017(a).
12. No change to any alternative form of regulation or network modernization plan may be made without the express agreement of both the commission and the local exchange telecommunications company. 66 Pa. C.S. § 3013(b).
13. As the primary law by which the RLECs are regulated, any inconsistent law or regulation must yield. 66 Pa. C.S. § 3019(h).



14. Both the United States and Pennsylvania Constitutions prohibit the government from taking private property without just compensation. PA Const. Article, Section 1; U.S. Const. Amend. IV, XIV.

15. The regulatory body may consider only revenues from the services within its jurisdiction. *Smith v. Ill. Bell Tel. Co.*, 282 U.S. 133, 148-49 (1930).

16. This Commission's regulatory authority is limited to *intrastate regulated* services and confiscation is defined within that jurisdiction. *Smyth v. Ames*, 169 U.S. 466, 541 (1898).

17. Revenues from competitive services reflect the compensation due to the firm for the risks of a competitive business and cannot be treated as "compensation" for below-cost rates set by the regulator. *Barr, et al.*, "The Gild That Is Killing The Lily," 73 Geo. Wash. U.S. Rev. 429, 462-63 (2005).

18. The same principles are reflected in the Public Utility Code, which requires the Commission to set regulated rates at just and reasonable levels. 66 Pa. C.S. § 1301.

19. One clear purpose of Chapter 30 is to provide an alternative to rate base/rate of return rate-setting for judging just and reasonable rates. *PA P.U.C. v. Frontier Communications of Pennsylvania, Inc.*, Docket No. R-00984411 (Order entered February 11, 1999).

20. The local rates being advocated by AT&T, Verizon, Sprint and Comcast are not affordable, just, reasonable or comparable. 66 Pa. C.S. §§ 3011(5), 3011(8); 47 U.S.C. § 254(b).

21. Federal law articulates several universal service mandates, among those being that rates must be affordable; access ... must be provided in all regions of the Nation ... including low-income consumers **and** those in rural, insular, and high cost areas; that services and rates be reasonably comparable to those offered in urban areas; and that [a]ll providers of telecommunications services ... make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service[.] 47 U.S.C. § 254(b) (emphasis added)

22. While not using identical terminology, state law reflects these same federal concerns. 66 Pa. C.S. §§ 3011(3), 3011(8), 3011(12).

23. Universal service must be balanced with, not forsaken for, competition. 66 Pa. C.S. § 3011(8).

24. Current access rates are neither unjust nor unreasonable. 66 Pa. C.S. §§ 1301, 3015(g).

25. By the definitions used in the statute, retroactive relief is not available in this proceeding. 66 Pa. C.S. § 1309(b).

26. The retroactive relief provision in Section 1309(b) applies only where the requested reduction in rates . . . affects more than 5% of the customers and . . . amounts to in excess of 3% of the total gross annual intrastate operating revenues of the public utility[.] 66 Pa. C.S. § 1309(6).

27. Not a single RLEC fails to qualify for this exemption from refunds on the basis of the 5% of customers test. 66 Pa. C.S. § 1309(6).

28. Section 1309(b) retroactive relief can never be applicable to ILEC access reductions because the 3% total operating revenue reduction test can never be met. 66 Pa. C.S. § 3017(a).

29. If the public utility furnishes two or more types of service, the foregoing percentages shall be determined only on the basis of the customers receiving, and the revenues derived from the type of service to which the requested reduction pertains. 66 Pa. C.S. § 1309.

30. Both local and access services are defined as protected services under Chapter 30. 66 Pa. C.S. § 3012.

31. The services provided by the RLECs are the same – telecommunications – and are not two or more types of service. 66 Pa. C.S. § 1309(b).

32. The PTA Companies' intrastate access rates are reasonable charges for protected services which are available on a nondiscriminatory basis. 66 Pa. C.S. § 3011(3).

33. The PTA Companies' intrastate access rates terms and conditions are reasonable and do not impede the development of competition. 66 Pa. C.S. §3011(5).

34. The PTA Companies' intrastate access rates do not discourage the provision of competitive services by service providers on equal terms throughout all geographic areas of this Commonwealth and do not jeopardize the provision of universal telecommunications service at affordable rates. 66 Pa. C.S. §3011(8).

35. The PTA Companies' intrastate access rates do not impede the competitive supply of any service in any region where there is market demand. 66 Pa. C.S. §3011(9).

## CERTIFICATE OF SERVICE

I hereby certify that on this 2<sup>nd</sup> day of September, 2010, I did serve a true and correct copy of the foregoing upon the persons below via electronic mail and first class mail as follows:

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