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May 13, 2010

**VIA FEDERAL EXPRESS**
Rosemary Chiavetta, Secretary
Pennsylvania Public Utility Commission
Commonwealth Keystone Building
400 North Street, 2nd Floor
Harrisburg, PA 17120

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

and

AT&T Communications of Pennsylvania, LLC, TCG New Jersey, Inc. and TCG Pittsburgh, Inc. v. Armstrong Telephone Company-Pennsylvania, et al.
Docket No. C-2009-2098380, et al

Dear Secretary Chiavetta:

Enclosed please find the original and nine copies of the Main Brief of the Verizon Companies, as well as the appended Proposed Findings of Facts, Conclusions of Law and Ordering Pararagraphs, filed on behalf of Verizon Pennsylvania Inc., Verizon North Inc., Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance, MCImetro Access Transmission Services, LLC d/b/a Verizon Access Transmission Services, and MCI Communications Services, Inc., in the above captioned consolidated matter. Because the Main Brief includes certain Proprietary information, a Public Version also is being provided for the public record.

Please do not hesitate to contact me if you have any questions.

Very truly yours,

Suzan D. Paiva

SDP/slb
Enc.

**Via E-Mail and First Class Mail**
cc: The Honorable Kandace F. Melillo
Certificate of Service

**PENNSYLVANIA**
**PUBLIC UTILITY COMMISSION**

| | | |
|---|---|---|
| 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<br>Complainant<br><br>v.<br><br>Armstrong Telephone Company - Pennsylvania, et al.<br>Respondents | : | Docket No. C-2009-2098380, et al. |

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**MAIN BRIEF OF VERIZON**

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Dated: May 13, 2010

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*Buffalo Valley Tel. Co. v. Pa. PUC*, 990 A.2d 67, 2009 Pa. Commw LEXIS 1728 (Pa. Commw. Ct. 2009)

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*Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund*, No. I-00040105, Recommended Decision Issued July 23, 2009

*Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund*, No. I-00040105 (Opinion and Order entered August 5, 2009)

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66 Pa. C.S. § 3015(a)(3)

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66 Pa. C.S. § 3017(c)

66 Pa. C.S. § 3019(b)(3)

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26 Delaware Code § 707(e)

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# I. STATEMENT OF QUESTIONS AND SUMMARY OF POSITIONS

## A. Summary

The Commission opened this investigation to consider "whether there should be further intrastate access charge reductions . . . . in the service territories of rural incumbent local exchange carriers ["RLECs"]."[1] The evidentiary record that the Commission has now assembled demonstrates that the answer to that question is a resounding "yes."

The record shows that there are serious anti-consumer consequences from permitting the RLECs to continue to charge outdated carrier access rates that average over five cents a minute, and in some cases exceed ten cents a minute, while most other carriers in Pennsylvania charge no more than 1.7 cents for the same service.[2] The RLECs use these high access rates as a means to obtain too much of their operating revenue from other carriers – and ultimately at the expense of those carriers' customers – when they should be obtaining more of that revenue from their own end-users. Because the RLECs' access rates are so excessive in comparison to those of other carriers, this irrational and inefficient rate structure harms the customers of the carriers that must divert revenue to pay these rates and also harms consumers in the RLECs' territory by diminishing competitive options.

Chapter 30 provides the Commission with a statutory tool to bring the RLECs' rates back in line with the rest of the industry. That statute empowers the Commission to rebalance revenue from access to retail rates consistent with 66 Pa. C.S. § 3017(a), which the Commonwealth Court has recognized allows the Commission to decrease access rates

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1 *Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund*, Order Instituting Investigation, Docket No. I-00040105 entered December 20, 2004 at 1 (available on Commission website).

2 Verizon St. 1.0 (Price Direct) at 19; Verizon St. 1.1 (Price Rebuttal) Tables One and Two.

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by "making revenue neutral increases to other noncompetitive rates."[3] The question is not whether the RLECs may continue to recover this revenue, but simply how they should collect it, and the record conclusively demonstrates that they should be collecting more revenue from their own end-users and less from other carriers. Chapter 30 also endorses the concept of using Verizon's switched access rates as an industry benchmark, by requiring all competitive carriers operating in Verizon's territory to charge rates no higher than Verizon's access rates. 66 Pa. C.S. § 3017(c).

The RLECs and the OCA concoct various obstacles to a valid and fully effective rate rebalancing. They would allow for only the most minimal rate rebalancing, and argue that the Commission has no option but to require other carriers to keep sending a disproportionate amount of revenue to the RLECs, either by maintaining high RLEC access rates or by replacing the access revenue with huge, new dollar-for-dollar subsidies from the state universal service fund ("USF"). But the evidence and the law refute these arguments. The RLECs and OCA fail to establish any basis in law or in fact that that would require the Commission to cap RLEC retail rates at the low levels they advocate – particularly where they contend that other carriers must foot the bill for avoiding those rate increases. It is evident that what the RLECs are really asking is for the Commission to protect them from competition by allowing them to charge lower rates and to claim operating subsidies from other carriers, an unsupportable argument that is contrary to the very premise of Chapter 30. In short, the record evidence shows that a thoughtfully crafted rebalancing of revenue from access to retail rates as contemplated by Chapter 30 is possible for each of the RLECs to reduce their dependence on revenues from other carriers.

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[3] *Buffalo Valley Tel. Co. v. Pa. PUC*, 990 A.2d 67, 2009 Pa. Commw LEXIS 1728 (Pa. Commw. Ct. 2009), slip op. at 22.

The record also shows that it is *not* an easy or cost-free solution to the problem of high RLEC access rates to replace that revenue with huge new subsidies from the carrier-funded state USF – the very same fund that ALJ Colwell recently concluded was hopelessly flawed and in need of a complete overhaul. As an initial matter, the current Chapter 30 provides no express statutory authorization to use other carriers' revenue to rebalance RLEC access rates and the entire proposition is antithetical to the legislative policies set forth in that statute to encourage competition and reduce regulatory burdens. Indeed the term "universal service fund" is a misnomer, because there is no evidence that this fund is or will be used to help customers who cannot obtain affordable service, as opposed to simply providing unexamined operating subsidies to the RLECs, as ALJ Colwell recognized. Moreover, shifting the revenue burden from one carrier-funded source (access rates) to another (the USF) does nothing to solve the fundamental problem with the RLECs' access charges, which is that the RLECs are collecting too large a portion of their operating revenues from other carriers instead of their own retail end-users. Creating this carrier-funded insurance policy in the form of more USF money for the RLECs would simply recreate the same anti-consumer, anti-competitive problem under a different name. Worse yet, the companies that would be forced to fund this revenue guarantee for the RLECs are subject to their own regulatory burdens and are experiencing their own line loss and market pressures in today's highly competitive market, and cannot afford to divert tens of millions of new dollars each year from their own operations to the RLECs. This "tax" to support RLEC operations would be harmful to customers of the contributing carriers and would discourage telecommunications investment in Pennsylvania.

The record shows that the RLECs can and should be expected to rebalance access revenue to retail rates (or to voluntarily forego that revenue if they so choose), but a compliance stage will be necessary to establish the precise details of the rebalancing for each individual RLEC. Each RLEC should be required to submit a rebalancing plan in the form of a compliance filing that eliminates the unfounded retail rate limitations and reduces their access rates to a uniform level, with the opportunity to rebalance that revenue to retail rates. The Commission can then address whether any transition is needed, but in no event should these compliance filings cause the USF to increase.

### B. Questions

1. Should the RLECs' intrastate switched access rates be reduced?

   **Answer:** Yes

2. To what level should the RLECs' intrastate switched access rates be reduced?

   **Answer:** To a uniform benchmark level set at the rate of the largest ILEC, Verizon PA, consistent with Chapter 30's requirement for competitive carriers under 66 Pa. C.S. § 3017(c)

3. How should the revenue be rebalanced to comply with 66 Pa. C.S. § 3017(a)?

   **Answer:** By providing the opportunity for offsetting increases to regulated rates for noncompetitive services

4. What compliance action is required?

   **Answer:** The RLECs should provide compliance filings proposing changes as ordered by the Commission, subject to comment by the parties

## II. FACTUAL AND LEGAL BACKGROUND

The RLECs comprise all of the incumbent local exchange carriers ("ILECs") in Pennsylvania except for the two Verizon ILECs – Verizon PA and Verizon North. Taken together, the RLECs serve approximately one million access lines in Pennsylvania (based on

year-end 2007 data as reported to the Commission). While referred to collectively as "the RLECs," each RLEC is a separate company with its own individual tariffs and rates. They vary in size and in corporate affiliation. (Verizon St. 1.0 (Price Direct) at 4-5).

Most of the RLECs have chosen alternative regulation under Chapter 30 of the Public Utility Code. (Verizon St 1.1 (Price Rebuttal) at 6). Therefore, the rebalancing of revenue away from intrastate switched access rates in order to reduce those rates is governed in the first instance by Chapter 30 and by the alternative regulation plans adopted under that statute. Under alternative regulation, the Commission no longer reviews or sets rates based on rate-of-return or underlying costs and the Commission is no longer privy to the RLEC's costs or profits. For an alternatively regulated RLEC, rates are generally divided into two categories – rates for "competitive" services and rates for "noncompetitive" services. The Commission's regulation of rates differs for each category.

For services declared or deemed "competitive," the RLEC operating under alternative regulation has full pricing flexibility. The Commission does not regulate these rates and the RLEC is free to increase them or decrease them. This regulatory mechanism is predicated on the notion that the rates for "competitive" services are constrained by competition. For services that continue to be categorized as "non-competitive," rates may be increased each year only if the inflation-based formula in the company's price stability mechanism allows for an overall increase to noncompetitive revenue. The RLEC has discretion to decide which noncompetitive service rates to increase, or whether to exercise or bank its opportunity to increase rates, subject to Commission review. The Commission retains the authority to ensure that rates for individual noncompetitive services remain just and reasonable and that the RLEC's pricing actions are consistent with its alternative

regulation plan.[4] Revenue may also be rebalanced among rates for noncompetitive services on a neutral basis so that rates for one service are reduced and rates for another service or services increased, which is the option that is relevant to this proceeding. Generally for all alternative regulation RLECs in Pennsylvania, switched access and basic stand-alone residential and business dial tone services *remain* categorized as "noncompetitive" services. Other services may also remain as noncompetitive for an individual ILEC, and those may vary among the carriers. (Verizon St 1.1 (Price Rebuttal) at 7-8).

In its various operational capacities Verizon[5] is, among other things, both a competitor and customer of the RLECs in Pennsylvania. Verizon is a customer of the RLECs each time it pays switched access rates to them. Indeed, it has no choice but to be the RLECs' customer because Verizon is required to pick up and deliver calls its own customers make to RLECs' local subscribers. At the same time, Verizon and the RLECs are competitors. For instance, MCImetro, Verizon's competitive local exchange carrier ("CLEC") affiliate, provides competing service in the territories of the RLECs CenturyLink and Consolidated/North Pittsburgh in the provision of retail services to enterprise (large business) customers. And Verizon's interexchange carrier ("IXC") affiliates compete with RLECs to provide long-distance services to Pennsylvania residents. (Verizon St. 1.0 (Price Direct) at 5). In these various capacities, Verizon is harmed by the RLECs' excessive access rates and urges the Commission to undertake a reasonable rebalancing reducing these rates.

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[4] *Buffalo Valley*, 990 A.2d 67, slip op. at 21.

[5] This brief is filed on behalf of Verizon Pennsylvania Inc., Verizon North Inc., Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance, MCImetro Access Transmission Services, LLC d/b/a Verizon Access Transmission Services, and MCI Communications Services Inc. (collectively "Verizon").

This proceeding had its origins in the Commission's 1999 *Global Order*, in which the Commission reduced the access charges of all ILECs and adopted a settlement establishing an interim USF to provide replacement revenue for a specific set of RLEC access reductions, while ensuring that their basic residential rates did not exceed $16.[6] The *Global Order* called for an investigation to be initiated "on or about January 2, 2001, to further refine a solution to the question of how the Carrier Charge (CC) pool can be reduced," and directed that at the conclusion of this investigation "the pool will be reduced."[7]

On July 15, 2003, the Commission approved a settlement that provided for additional rebalancing of revenue from RLEC access rates to retail rates and increased the rate benchmark from $16 to $18.[8] In accepting the Joint Proposal, the Commission cautioned the RLECs that it expected their access rates to continue to decrease, stating "we do not intend to declare the access rates established by this Order as the final word on access reform. Rather, this is the next step in implementing continued access reform in Pennsylvania in an efficient and productive manner."[9]

The Commission opened this present investigation on December 20, 2004 to try to decrease the flow of revenue from other carriers to the RLECs by "consider[ing] whether [RLEC] intrastate access charges and intraLATA toll rates . . . should be decreased" and "any and all rate issues and rate changes that should or would result in the event that

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6 *Joint Petition of Nextlink Pennsylvania, Inc.*, Docket Nos. P-00991648; P-00991649, 196 P.U.R.4th 172 (Opinion and Order entered September 30, 1999) ("*Global Order*"), slip op at 25 (available on Commission website at telecommunications\issues\global order).

7 *Global Order* at 56.

8 *Access Charge Investigation per Global Order of September 30, 1999*, Docket Nos. M-00021596, etc., (Opinion and Order entered July 15, 2003) ("*7/13/03 RLEC Access Order*") (available on Commission website).

9 *Id.* at 12.

disbursements from the Pennsylvania Universal Service Fund are reduced and/or eliminated."[10] Over the objections of the RLECs' access customers, including Verizon, this investigation was stayed several times to await developments in the Federal Communications Commission's ("FCC") intercarrier compensation investigation, and in the interim RLECs have continued to charge their excessive switched access rates and also to collect over $30 million each year from the USF.

By order entered April 24, 2008, the Commission granted "in part" a third stay of the investigation, again staying its consideration of reducing RLEC access rates. However, based on developments in a parallel case in which three of the RLECs had attempted to increase their access rates, the Commission determined that certain issues could no longer be deferred and must be addressed immediately. The Commission's April 24, 2008 order reopened this investigation on a limited basis to address two general issues: (1) the existence and potential alteration of any "caps" on RLEC residential and business monthly service rates; and (2) potential increases or decreases in funding provided to RLECs from the USF.[11] On July 23, 2009 Administrative Law Judge ("ALJ") Susan D. Colwell issued a recommended decision that among other things rejected the RLECs' arguments that the USF should be expanded to fund their annual inflation-based revenue increases while allowing them to avoid increasing retail rates, and recommending that the Commission convene a rulemaking to "reform[]" the current USF "to provide monetary assistance only

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10 *Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund*, Order Instituting Investigation, Docket No. I-00040105, entered December 20, 2004 at Ordering ¶ 1 (available on Commission website).

11 *Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund,* No. I-00040105 (Opinion and Order entered April 24, 2008) (available on Commission website).

to those RLECs for service in high-cost service areas and for assistance to low-income customers."[12]

Meanwhile, on March 19, 2009, AT&T Communications of Pennsylvania, LLC and its affiliates ("AT&T") filed individual formal complaints asking the Commission to reduce the access rates of each RLEC. With two separate orders adopted at its July 23, 2009 public meeting the Commission consolidated the AT&T complaints with the pre-existing RLEC access rate investigation and lifted the stay of the access charge portion of the investigation, sending the cases to the Office of Administrative Law Judge for development of an evidentiary record and issuance of a recommended decision by August 5, 2010.[13]

## III. BURDEN OF PROOF

The burden of proof in a Commission proceeding involving rates is governed by the Public Utility Code. Where a formal complaint challenges an existing rate, the burden of proof rests with the complainant,[14] but "[i]n any proceeding upon the motion of the Commission involving any proposed or existing rate of any public utility . . . the burden of proof to show that the rate involved is just and reasonable shall be upon the public utility."[15]

This proceeding is a consolidation of the Commission's ongoing investigation of the RLECs' access rates that commenced in 2004, together with a series of formal complaints brought by AT&T in 2009 against the RLECs' access rates. This Commission has already

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12 *Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund*, No. I-00040105, Recommended Decision Issued July 23, 2009 ("Colwell 7/23/09 RD") at 66 (available on Commission website).

13 *Investigation Regarding Intrastate Access Charges and IntraLATA Toll Rates of Rural Carriers and the Pennsylvania Universal Service Fund*, No. I-00040105 (Opinion and Order entered August 5, 2009) (available on Commission website); *AT&T Communications of Pennsylvania, LLC v. Armstrong Telephone Co., etc.*, No. C-2009-2098380 (Opinion and Order entered July 29, 2009) (available on Commission website).

14 66 Pa. C.S. § 332(a) ("the proponent of a rule or order has the burden of proof.")

15 66 Pa. C.S. § 315(a).

addressed the burden of proof where a pre-existing access rate investigation is consolidated with a subsequent complaint against the same company's access rates. In the Verizon access investigation the Commission overruled ALJ Fordham's conclusion that the IXC complainants bore the burden pursuant to 66 Pa. C.S. § 332(a) and instead concluded that the "public utility" bears the burden of proof pursuant to 66 Pa. C.S. § 315(a).[16] The Commission's reasoning applies equally to this case and requires the RLECs to bear the burden of proof.

Accordingly, the RLECs bear the burden of proof in this case, and they have failed to establish that their current high access rates are "just and reasonable" as required by 66 Pa. C.S. § 315(a). To the contrary, PTA's witness admitted at the hearing that it is not PTA's position that the Commission should refrain from reducing the RLECs' intrastate access rates, (Tr. at 585), and that there is "a perception" by the Commission and the industry that "high access rates were detrimental to competition." (Tr. at 670). In fact, the PTA companies "remain supportive of intrastate access reductions that balance the various affected public interests" and "do not oppose further intrastate access reform."[17] OCA also agrees that the RLECs' currently high access rates are anti-competitive and must be reduced to eliminate "unfair discrimination" and "arbitrage incentives."[18] The RLECs submitted no cost studies attempting to justify the high level of their access rates, and as discussed below, the undisputed record shows that those rates should be reduced.

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16 *AT&T Communications of Pennsylvania, Inc. v. Verizon North Inc.*, C-20027195 (Opinion and Order entered January 8, 2006) at 20-21 (available on Commission website) (due to the existence of a preexisting investigation into the access rates, the filing of a formal complaint does not shift the burden of proof to the complainant).

17 PTA St. 1 (Zingaretti Direct) at 3, 55.

18 OCA St. 1 (Loube Direct) at 48.

## IV. THE RLECS' INTRASTATE SWITCHED ACCESS RATES SHOULD BE REDUCED

### A. The RLECs' Access Rates Are Higher Than The Rates Other Carriers Charge For The Same Service

The record shows that, with a few limited exceptions,[19] the RLECs' intrastate switched access rates are extremely high in comparison to what Verizon and other carriers charge for the exact same intrastate switched access service. As depicted in tables one and two from Verizon's rebuttal testimony, the RLECs' weighted average rate per minute for intrastate access is over 5 cents – which is more than 300% higher than the 1.7 cents per minute charged by Verizon PA for the same service. Some of the RLECs are charging more than 10 cents a minute for the same service. (Verizon St. 1.1 (Price Rebuttal) at 10-11; Verizon St. 1.0 (Price Direct) at 19). Competitive carriers operating in Verizon territory are prohibited by statute from charging rates higher than Verizon's rates and therefore generally charge 1.7 cents per minute or less. *See* 66 Pa. C.S. § 3017(c). There is no doubt that the RLECs' access rates are disproportionately higher than those of most of the other local exchange carriers operating in Pennsylvania.

Much of the disparity between the RLECs' rates and those of other carriers on an average rate per-minute basis is driven by the fact that many of them still impose a huge monthly carrier charge or "CCLC" on other carriers on a per-access line basis. The average PTA company CCLC is $5.87 per line, per month, and a number of them charge over $10 per line per month. CenturyLink's CCLC is $7.19 per line, per month. (Verizon St. 1.1. (Price Rebuttal) at 11). In contrast, Verizon's current CCLC is 58 cents per line per month.

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[19] The RLECs' discovery responses, as depicted on table one of Verizon's Statement 1.1, show that the following carriers' average intrastate switched access rate per minute is already approximately equal to or below Verizon PA's current rates: Armstrong North, Frontier Breezewood, Frontier Canton, Frontier Lakewood and Frontier PA.

(*Id.*) The RLECs' outdated and excessive CCLCs illustrate the stark difference between the switched access rates of the RLECs and Verizon's rates for the same service, as well as the considerable variation even among the RLECs themselves.[20]

The CCLC is an access rate element created when intrastate access rates were first developed in the mid-1980s and was originally designed to recover a portion of the fixed costs of providing local loops to the ILEC's own end users, in order to keep end user rates artificially low. Because these fixed costs are not related to the switching and transport functions used to provide long-distance carriers with access to a LEC's network, an excessively high CCLC serves as a vehicle to transfer to the LEC's access customers the LEC's fixed costs of providing local exchange service to its own retail customers. For this reason, the CCLC has been a primary focus of regulators seeking to rationalize intrastate switched access rates, including this Commission. For example, in the 1999 *Global Order*, this Commission recognized that the CCLC "is the largest contributor to local service rates not directly related to cost" and looked to reduce the revenue collected from the CCLC as a way to both reduce implicit subsidies built into access rates and to benefit competition in Pennsylvania.[21] Similarly, when the FCC removed the CCLC from rural carriers' interstate switched access rates in 2001, it observed that its action would "reduce the cost of long distance service and encourage a more efficient level of consumption. It will move per-minute switched access rates towards cost-based levels and promote efficient competition in

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20 Interestingly, a few of the RLECs, particularly those noted in the previous footnote, have nominal or zero-rated carrier charges, demonstrating that it is certainly possible for an RLEC to provide service in rural territory without charging a huge carrier charge to its carrier access customers. (Verizon St. 1.0 (Price Direct) at 14).

21 *Global Order*, slip op. at 13.

the exchange access market by permitting both incumbent and competitive carriers to compete for all services based on price."[22]

The result of federal and state regulators' efforts to move toward more rational access pricing has been a pronounced decline in typical access charge rates in the interstate jurisdiction, with the FCC reporting that interstate switched access charges declined from more than 17 cents per minute in 1984 to 1.71 cents per minute in 2008.[23] Clearly the RLECs' intrastate access rates – currently averaging around 5 cents per minute with some exceeding 10 cents – have not kept up with this pace of reform.

The record therefore establishes that the majority of the RLECs continue to charge extremely high access rates in comparison to Verizon and other Pennsylvania carriers, both on a per-minute basis and in terms of the traditional subsidy rate element of the CCLC.[24] The fact that these rates are so much higher than the rates charged for the same service by other carriers in the industry indicates that the RLECs' rates are unjust, unreasonable and not cost justified.[25]

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22 *Multi-Association (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Second Report & Order and Further Notice of Proposed Rulemaking, CC Docket No. 00-256, Fifteenth Report & Order in CC Docket No. 96-45, and Report & Order in CC Docket Nos. 98-77 and 98-166, 16 FCC Rcd 19613, 2001 FCC LEXIS 6052 (Rel. Nov. 8, 2001) ("*MAG Order*") ¶ 63. In addition to their large carrier charges, some of the RLECs continue to charge other outdated subsidy rate elements, such as the "Transport Interconnection Charge" or "TIC," which Verizon does not charge. (Verizon St. 1.0 (Price Direct) at 14-15).

23 *See* "Trends in Telephone Service," Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, August 2008, Table 1.2. (Verizon St. 1.1, Exhibit Price Rebuttal 1).

24 The tariff pages containing each RLEC's current access rate elements, including the CCLC, are attached to Verizon's direct testimony as Exhibit 3. (Verizon St. 1.0 (Price Direct) Exhibit 3). A depiction of each RLEC's access rates on a per-minute-of-use basis appears in Verizon's rebuttal testimony at tables one and two. (Verizon St. 1.1 (Price Rebuttal) at 10-11). The per-minute calculations are taken from the RLECs' own discovery responses, dividing revenues by minutes. (*Id.*)

25 *See Mobilfone of Northeastern Pennsylvania, Inc. v. PUC*, 78 Pa. Commw. 336, 467 A.2d 902 (1983) (affirming the Commission's consideration of the rates charged by other carriers for the same service as an indicia of reasonability).

### B. Permitting The RLECs To Continue To Charge Excessive Access Rates Is Harmful To Consumers And Competition

The record clearly shows that continuing to permit the RLECs to charge access rates so far in excess of what other Pennsylvania carriers charge for the exact same switched access service is harmful to consumers and to competition. Reducing those rates to be more in line with the rates of Verizon and other carriers will have substantial public benefits.

First, the RLECs' high access charges are harmful to consumers because of their impact on the customers of carriers that must pay those excessive access rates. The RLECs charge these rates not only to IXCs but also to every other local exchange carrier (ILEC or CLEC) that must terminate intraLATA toll traffic to RLEC customers. For example, the Verizon ILECs, which provide wireline local service to many customers in Pennsylvania, themselves pay a substantial amount of money each year to the RLECs for switched access.[26] These carriers – both LECs and IXCs -- have no competitive choice for access service and therefore must terminate traffic to the RLECs and must pay their access rates. Because these rates are higher than they should be, the result is to require other carriers to divert large sums of revenue away from their own operations to fund the RLECs' operations, depriving these carriers of revenues that could be used to improve products, services, or networks, or even to reduce rates — to the ultimate detriment of their customers.

As the FCC explained, when one group of carriers is permitted to charge higher access rates than other carriers, "the higher [access] . . . rates may shift an inappropriate share of the carriers' costs onto" the carriers paying those rates and, through them, to the

[26] In 2008 Verizon PA and Verizon North, the Verizon ILEC entities, paid **[BEGIN PROPRIETARY] [END PROPRIETARY]** in switched access charges to the RLECs. (Verizon St. 1.1 (Price Rebuttal) at 19.

market in general.[27] Similarly here, the RLECs are shifting an inappropriate share of their own operating costs onto the IXCs and other LECs operating in Pennsylvania. The FCC repeatedly has observed that economically efficient competition and the consumer benefits such competition yields cannot be fully achieved as long as carriers seek to recover a disproportionate share of their costs from other carriers, rather than from their own end users.[28] Such irrational access rate structures lead to what the FCC has termed "inefficient and undesirable economic behavior,"[29] and, ultimately, to higher prices for consumers. As the FCC has observed, this also suppresses demand for the services of those carriers that must pay the excessive access charges and reduces incentives for local entry by firms that might be able to provide service more efficiently than the other LEC if they were not required to subsidize the less efficient operations.[30] (Verizon St. 1.0 (Price Direct) at 9-10).

Second, the RLECs' high access charges harm consumers in the RLECs' own territories because they diminish competitive options. Where excessive access charges provide a mechanism for subsidizing local exchange services to a disproportionate degree, this distortion artificially slows the emergence of local exchange competition, a fact that this Commission itself recognized in 2003 by finding that RLEC access rates must be reduced so that "competitors are better able to compete for local and long distance customers in an ILEC's service territory because IXCs are not hindered by paying ILECs excessive access

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[27] *In the Matter of Access Charge Reform; Reform of Access Charges Imposed by Competitive Local Exchange Carriers,* Seventh Report And Order And Further Notice Of Proposed Rulemaking, CC Docket No. 96-262, 16 FCC Rcd 9923; 2001 FCC LEXIS 2336, ¶22 (FCC Rel. April 27, 2001).

[28] *See generally Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long Distance Users; Federal-State Joint Board on Universal Service,* 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, 15 FCC Rcd 12962, 2000 FCC LEXIS 2801 (May 31, 2000) ("*CALLS Order*"); *MAG Order; CLEC Rate Cap Order.*

[29] *CALLS Order*, at ¶ 129.

[30] *Id.* at ¶ 114.

charges in providing competitive toll services and CLECs are better able to compete with ILEC local service rates that have been kept artificially low as a result of the access charge subsidies."[31] The FCC similarly noted that rural carriers' "higher rates and implicit subsidies may discourage efficient local and long distance competition in rural areas and limit consumer choice."[32] Simply put, if the prices of the RLEC's services are artificially depressed because the RLEC recovers a disproportionate amount of its revenues through access charges, then potential entrants simply will not enter to compete for consumers' business or they may be forced to compete less effectively. With specific regard to relatively small rural carriers like some of the RLECs, the FCC has found that rationalizing their switched access rates will enhance incentives for long distance carriers to originate service in rural areas and will foster facilities-based competition for residential subscribers in those areas.[33]

The RLECs effectively concede that their higher access rates – which permit them to charge lower retail rates – enable them to stave off competitors in their territory. PTA's witness, for example, asserted that if RLECs reduce their access rates and must rebalance that revenue by increasing retail rates they will face "massive customer attraction campaigns" from competitors and "massive migrations" by customers pursuing "attractive

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[31] *7/13/03 RLEC Access Order,* at 10. *See also PUC v. North Pittsburgh Telephone Company,* No. R-00038087 (Opinion and Order entered April 10, 2003) (available on Commission website) (dismissing customer complaints against a proposed rebalancing of revenue from access to retail rates because "we are of the opinion that the residential Complainants may misunderstand the purpose of a revenue neutral rate rebalancing filing, which is to bring rates in line with costs. Historically, the Company's local exchange service rates have been set below the cost to provide that service, while its access rates have been set above the cost of service. *The new competitive market place requires telecommunications providers to move their rates closer to the cost of providing service.* The instant filing continues the process of eliminating the subsidization of local exchange service rates that has been provided by inflated access rates.") (emphasis added).

[32] *MAG Order* at ¶ 6.

[33] *MAG Order* at ¶ 11.

offers" from competitors.[34] Similarly, CenturyLink's witness admitted at the hearing that "it's a safe summary of CenturyLink's position in this case that [it] cannot raise rates because customers will leave and go to a competitor," and that CenturyLink fears a rate rebalancing could "move market share to competitive carriers." (Tr. at 394, 422). But the Commission should not be maintaining high access rates to protect the RLECs from competition. If competitors stand ready to serve customers in the RLECs' territory at "attractive" rates, as the PTA asserts, then this Commission should not stop them – which is what the RLECs are really asking by opposing access reductions and rate rebalancing. In fact, permitting the RLECs to use excessive rates for the protected service of switched access as a means to suppress competition is directly contrary to the Legislature's directive in Chapter 30 to "provide diversity in the supply of existing and future telecommunications services and products in telecommunications markets throughout this commonwealth by ensuring that rates, terms and conditions for protected services are reasonable and *do not impede the development of competition."* 66 Pa. C.S. § 3011(5) (emphasis added).

And of course requiring carriers to pay excessive rates for switched access is harmful to the carrier ratepayers, such as Verizon, that are the RLECs' customers for switched access service. As the Commonwealth Court recently recognized, Chapter 30 "expressly preserves the Commission's authority and responsibility to protect all ratepayers," and "[t]his protection extends to services provided to other telephone carriers, i.e., 'ratepayers,' for Petitioners' switched access service."[35]

The parties that advocate maintaining the "status quo," thus leaving the RLECs' access rates at their current excessive levels, deny that there are consumer benefits to be had

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34 See PTA St 1-SR (Zingaretti Surrebuttal) at 49.

35 *Buffalo Valley*, 990 A.2d 67, slip op. at 20.

from reducing RLEC rates and contend that the money saved from doing so will only be used to increase the "profits" of the carriers that pay access rates.[36] These parties simply ignore the workings of the competitive market. It is irrational to suggest that companies like Verizon have extra money that they are obligated to use to support the RLECs' operations, and that otherwise would go into "corporate coffers" or excess "profit" if Verizon were no longer required to pay the RLECs' excessive rates. In a competitive market, companies must invest in their networks and their customers if they wish to remain competitive and stay in business – and they cannot afford merely to profit-take savings from access charge reductions. The simple truth is that in a competitive market, carriers that refuse to pass along the benefits of cost savings will lose customers to those who do. Cost savings may be reflected in reduced rates, or rates that stay the same because the savings have offset other cost increases, or a smaller rate increase than would have otherwise been implemented. Also, competitors in the long distance market may choose to invest the savings in advanced technology, improved service quality or customer service, or they could introduce new services or features, thereby bringing tangible benefits to consumers in other ways. Competition will ensure that such benefits are passed along to consumers in one way or another. (Verizon St. 1.1 (Price Rebuttal) at 18).

The RLECs proceed from the assumption that they have some entitlement to take money from the customers and networks of other carriers to support their own operations, but they do not. While CenturyLink accuses Verizon and its other carrier access customers of "placing their profit seeking motives above consumers' interests,"[37] in fact it is in the best interests of *all* consumers to move to a more efficient rate structure for RLEC rates in

[36] CenturyLink St. 1.0 (Lindsey and Harper Direct) at 14; OSBA St. 1 (Wilson Direct) at 14.

[37] CenturyLink St. 1.0 (Harper and Lindsey Direct) at 14.

Pennsylvania. While the carriers pay the RLECs' high access rates in the first instance, it is ultimately the customers that shoulder the burden in the form of higher toll rates, less innovation and diminished competition. (Verizon St. 1.1 (Price Rebuttal) at 17).

Indeed, the Commission has already determined that the RLECs' access rates should be reduced, for these precise reasons. Beginning with the *Global Order* over ten years ago, the Commission's stated goal has been to reduce RLEC access charges as "necessary steps to strive to replace the system of implicit subsidies with 'explicit and sufficient' support mechanisms to attain the goal of universal service *in a competitive environment*."[38] As the Commission explained in 2003, when it approved a previous RLEC rate rebalancing that resulted in some access rate decreases, its policy to gradually reduce RLEC access rates is essential to furthering the Commission's goal of bringing opportunities for competition in the RLECs' territories, noting that the RLECs' high access charges "impede competition in the telecommunications market" and that if those rates were reduced "competitors are better able to compete for local and long distance customers in an ILEC's service territory" and "CLECs are better able to compete with ILEC local service rates that have been kept artificially low as a result of the access charge subsidies."[39] In its August 5, 2009 order reopening this investigation and consolidating it with the AT&T complaints, the Commission made quite clear that "[i]t has been, and continues to be the intention of this Commission, since the *Global Order* of 1999, to gradually lower intrastate access charges *so as to allow for greater competition in the intrastate and interexchange toll markets*."[40]

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38 *Global Order*, slip op at 25 (emphasis added).

39 *7/13/03 RLEC Access Order* at 10.

40 8/5/09 Order at 20 (emphasis added).

It should be noted, moreover, that no party is advocating in this proceeding that the RLECs' access rates should be reduced to incremental cost or that intrastate access rates should be priced in a manner that would provide no contribution to operating (or loop) costs.[41] To the contrary, as discussed below, Verizon advocates a benchmark rate based on its own access rates. Verizon's current access rates are above the incremental cost of providing access service, thus providing a reasonable contribution to overall operating costs (or loop costs, if that terminology is preferred). Therefore, the RLECs would continue to receive a contribution to operating costs from access rates, albeit a smaller one, even if they reduce their access rates as Verizon recommends. The RLECs' access rates should be reduced below their currently excessive levels and the RLECs instead should recover more of their operating costs – not *all* of their costs – from their own retail end users. Verizon is not asking for a "free ride," nor is it arguing that "basic local exchange rate[s] [should] recover all network costs." (OCA St. 1-S (Loube Surrebuttal) at 5, 8). Verizon is simply arguing that the Commission should move the RLECs to a more efficient rate structure where they recover *more* of their operating costs from retail end users – which will benefit consumers in the RLECs' territory and throughout the state.

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[41] As CenturyLink's witnesses admitted, the functionality used to provide switched access is essentially the same, regardless of what carrier is providing it. (CenturyLink St. 1 (Harper and Lindsey Direct) at 34). This argument about higher "costs" is simply another way for the RLECs to argue that they should be provided greater contribution to operating costs through access rates than Verizon is provided through its own access rates. (Verizon St. 1.1 (Price Rebuttal) at 30).

## V. IF THE RLECS' INTRASTATE SWITCHED ACCESS RATES SHOULD BE REDUCED, TO WHAT LEVEL SHOULD THEY BE REDUCED AND WHEN?

### A. Rate Levels: The RLECs' Access Rates Should Be Reduced To A Uniform Benchmark Level At Verizon's Lower Access Rate

Until comprehensive access reform can be achieved at the national level (or until carriers can negotiate their own intercarrier compensation agreements), the Commission should benchmark all RLECs' intrastate switched access rates to the lower Verizon PA's intrastate switched access rate. A benchmark at the level of Verizon PA's rates would be a simple and effective means to quickly move excessive switched access rates in Pennsylvania to more efficient levels. This benchmark will promote equity and competitive parity and reduce market distortions by prompting carriers with the highest access rates to recover more of their network costs from their own customers, rather than from other carriers and their customers through access rates. The concept of moving all access rates to a uniform industry benchmark is consistent with Chapter 30's legislative policy, as demonstrated by the benchmark requirement for competitive carriers set forth in 66 Pa. C.S. § 3017(c).

Benchmarking is a common approach used by regulators and policymakers to establish just and reasonable rates. The approach of benchmarking to the largest ILEC's rate is commonly used by the FCC and state policymakers around the country to determine appropriate levels for switched access rates.[42] For this reason, LECs operating in Verizon

[42] *See, e.g.*, the **FCC**'s *CLEC Rate Cap Order*; *Order Instituting Rulemaking to Review Policies Concerning Intrastate Carrier Access Charges*, **California** D. 07-12-020 in Rulemaking 03-08-018, Final Opinion Modifying Intrastate Access Charges 2007 Cal PUC LEXIS 609 ( Dec. 6, 2007) (capping CLEC rates at no higher than the rates of the two largest carriers, Verizon and SBC, plus 10%); *DPUC Investigation of Intrastate Carrier Access Charges*, Decision, **Connecticut** D.P.U. Docket No. 02-05-17 (2004), 2004 Conn. PUC Lexis 15, at *45 (capping CLEC rates at SBC's then-current rate); **Delaware** Code, Title 26, § 707(e) (capping all service providers' switched access rates at the level of the largest ILEC in the state); *TDS Metrocom, Inc., Petition for Arbitration*, Arbitration Decision, **Illinois** Comm. Comm'n Docket No. 01-0338, at 48-50, 2001 Ill PUC LEXIS 829 (Aug. 8, 2001) (a CLEC may not charge an ILEC more for terminating intrastate switched access than the ILEC charges the CLEC); 199 **Iowa** Admin. Code

PA territory are already required by statute to benchmark to Verizon PA's switched access rates, which is the rate that Verizon proposes as the benchmark for all carriers through this proceeding. *See* 66 Pa. C.S. § 3017(c). (Verizon St. 1.0 (Price Direct) at 4).

The intrastate switched access rates of the largest ILEC in the state — in this case, Verizon PA — are the most appropriate benchmark. As the largest ILEC in the state, Verizon PA's access rates have historically been subject to the greatest regulatory scrutiny – as demonstrated by the fact that they are so much lower than the RLECs' rates -- and are the prevailing rates. Because the market will not set a "competitive" rate for the RLECs, the benchmark rate should serve as a proxy for the "competitive" rate that the RLECs, like other market participants, should be required to accept. In a competitive market, carriers would

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22.14(2)(d)(1)(2) (prohibiting CLECs from charging a carrier common line charge if it would render the CLEC's rate higher than the competing ILEC's rate); **Louisiana** PSC General Order No. U-17949-TT, App. B, Section 301 (k)(4), 1996 La. PUC LEXIS 62 (May 3, 1996) (CLECs must charge non-discriminatory switched access rates that do not exceed the competing ILEC's rates); Code of **Maryland** Regulations § 20.45.09.03(b) (capping CLECs' switched access rates at the level of the largest LEC in Maryland); *Petition of Verizon New England Inc. et al. for Investigation Under Chapter 159, Section 14, of the Intrastate Access Rates of Competitive Local Exchange Carriers*, Final Order, **Massachusetts** D.T.C. 07-9 (June 22, 2009) (available at http://www.mass.gov/Eoca/docs/dtc/dockets/07-9/079finalorder.pdf) (capping CLEC switched access rates at Verizon's level); *Access Rates to Be Charged by Competitive Local Exchange Telecommunications Companies in the State of Missouri*, Report and Order, **Missouri** P.S.C. Case No. TO-99-596, 2000 Mo. PSC Lexis 996, at *28-31 (June 1, 2001) (capping CLEC access rates at the competing ILEC's level); **New Hampshire** PUC § 431.07 (CLECs cannot charge higher rates for access than the ILEC does); **New York** P.U.C. Case 94-C-0095, Order, at 16-17 (Sept. 27, 1995), N.Y. P.U.C. Opinion 96-13, at 26-27 ( May 22, 1996), and N.Y. P.S.C. Opinion 98-10, 1998 N.Y. PUC Lexis 325, at 26-27 (June 2, 1998) (benchmarking CLEC access charges to the level of the largest carrier in the LATA); *Establishment of Carrier-to-Carrier Rules*, Entry on Rehearing, **Ohio** P.U.C. Case No. 06-1344-TP-ORD, at 16-18, 2007 Ohio PUC LEXIS 693 (Oct. 17, 2007) (capping CLECs' switched access rates at the level of the competing ILEC); **Texas** P.U.C. Subst. Rule § 26.223 (a CLEC may not charge a higher rate for intrastate switched access than the ILEC in the area served or the statewide average composite rates published by the Texas P.U.C. and updated every two years); *Amendment of Rules Governing the Certification and Regulation of CLECs*, Final Order, **Virginia** State Corp. Comm. Case No. PUC-2007-00033, 2007 VA PUC LEXIS 763 (Sept. 28, 2007) (a CLEC's switched access rate cannot exceed the higher of its interstate rate or the rate of the competing ILEC); *Petition by Verizon West Virginia Inc. Requesting that Commission Initiate a General Investigation of the Intrastate Switched Access Charges of Competitive Local Exchange Carriers Operating in WV*, **West Virginia** Public Service Commission Order, Case No. 08-0656-T-PC, 2009 W VA PUC LEXIS 3012 (Nov. 23, 2009) (capping CLEC switched access rates at the competing ILEC's level).

not be able to charge rates significantly above the prevailing rate, as the RLECs do today for switched access. (Verizon St. 1.0 (Price Direct) at 17-18). As depicted in Verizon's direct testimony, Verizon's average rate per minute is approximately 1.7 cents. (*Id.* at 19).[43] On May 11, 2010 the Commission entered an order resuming the Verizon access investigation effective when the recommended decision is issued in this case.[44] Given the large disparity between Verizon's access rates and the much higher rates most RLECs are charging for the same service, the Commission should promptly reduce the RLEC access rates to the Verizon level so that it may consider any future actions on an industry-wide basis.[45]

Verizon's recommendation for a benchmark at the Verizon PA rate level is shared by Qwest, but differs from the recommendation advanced by AT&T and others. AT&T recommends that each RLEC's intrastate switched access rates should be reduced to mirror that RLEC's own interstate switched access rates (which, like the intrastate rates, vary among the RLECs). The primary reason that the Verizon/Qwest proposal for a uniform rate is superior to the proposal to match interstate rates is because of the variation among the RLECs' interstate rates. As AT&T's own witnesses concede, some RLECs are still charging in the range of 4 cents a minute for interstate access,[46] and thus their intrastate rates would remain comparatively high if they simply matched their still high interstate rates.

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43 As explained in Verizon's direct testimony, the benchmark rate should be determined by calculating the composite of the Verizon PA intrastate switched access rate elements for the functions that the RLEC actually performs in providing its switched access service. Therefore, the particular rates charged will vary depending upon the specific switched access functions the RLEC performs and the miles of transport provided by the RLEC, where applicable. (Verizon St. 1.0 (Price Direct) at 21).

44 *AT&T Communications of Pennsylvania LLC v. Verizon North Inc*, No. C-20027195 (Opinion and Order entered May 11, 2010) (available on Commission website).

45 Verizon's benchmarking proposal would not dictate any particular rate structure or reductions of particular rate elements—although Verizon expects that if RLECs are ordered to benchmark their rates to Verizon's rates, they would look first to reducing elements, like the CCLC and TIC, that are most clearly driving excessive access rates. The RLECs would be required to meet the benchmark on an aggregate, per-minute basis.

46 AT&T St. 1.3 (Panel Surrebuttal) at 16.

Conversely, mirroring interstate rates would cause some carriers, such as CenturyLink and Windstream, to charge lower access rates than Verizon, a result Verizon is not advocating.[47] A much more fair result is to require all carriers to meet a uniform rate level, which the Commission can then address on an equitable industry-wide basis in the future. Moreover, Qwest's Mr. Easton explained very clearly how a uniform intrastate rate level among the various carriers would be more effective at deterring "traffic pumping" than allowing some RLECs to match interstate rates that are still considerably higher than the rates charged by Verizon and other carriers for intrastate access.[48]

Verizon is not insensitive to the fact that it may be difficult for some of the smaller carriers to match Verizon's access rates and rebalance the revenue to retail rates all at once. Verizon therefore also suggests that if the Commission is reluctant immediately to move those particular carriers all the way down to Verizon's benchmark rate, it could, as an interim measure, move them to their own higher interstate rates as AT&T has recommended. (Verizon St. 1.0 (Price Direct) at 22). Verizon also suggested that for some RLECs the Commission might determine that a phased-in reduction is appropriate. (Verizon St. 1.2 (Price Surrebuttal) at 20-21). But the longer term objective should be a common benchmark rate that puts all carriers on equal competitive footing.

The PTA companies contend that to reduce all of the PTA companies' rates to interstate levels would require them to rebalance a total of **[BEGIN PROPRIETARY]** **[END PROPRIETARY]** in revenue, while matching Verizon PA's rates would require them to rebalance a total of **[BEGIN PROPRIETARY]** **[END**

47 Verizon St. 1.3 (Price Rejoinder) at 7.

48 Qwest St. 1-SR (Easton Surrebuttal) at 4.

**PROPRIETARY**].[49] These exhibits provide a break-down of the RLECs' calculated revenue effect for each company under both scenarios. A comparison of GMZ-10 and GMZ-12 at the individual carrier level shows that for some carriers it would require more revenue to reduce their rates to interstate levels than it would to match Verizon PA's rates (*i.e.,* Windstream), while for others the result is the opposite. In other words, for some carriers their interstate rates are higher than Verizon's proposed benchmark, while for others their interstate rates are lower than Verizon's proposed benchmark. CenturyLink is an example of the latter category, reporting that it would have to rebalance **[BEGIN PROPRIETARY]** **[END PROPRIETARY]** to match interstate rates, versus **[BEGIN PROPRIETARY]** **[END PROPRIETARY]** to match Verizon PA's rates.[50] The total revenue to be rebalanced under their calculations for each scenario would be the sum of the PTA and CenturyLink totals.

### B. Timing: A Reasonable But Not Excessive Phase-In Can Be Considered For Some RLECs In The Compliance Stage

While Verizon does not oppose a reasonable transition or phasing-in of the rebalancing, the RLECs have not proposed any plan for rebalancing access revenues to retail rates, much less a reasonable transition period. The record (discussed in more detail below) shows that many of the RLECs are able to rebalance the excess access revenue to retail rates without a transition, but that for others the Commission may choose to phase down the access decreases in steps to avoid large retail increases. This detail can be finalized in the

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[49] PTA St. 1 (Zingaretti Direct), Exhibits GMZ-10 and 12.

[50] OCA's witness, Dr. Loube, also provided an estimate of the revenue impact to the RLECs of reducing their rates to interstate levels, but his estimates are generally lower than the estimates provided by the RLECs themselves. He estimates that the PTA companies would have to rebalance **[BEGIN PROPRIETARY]** **[END PROPRIETARY]** to reduce their rates to interstate levels and that CenturyLink would have to rebalance **[BEGIN PROPRIETARY]** **[END PROPRIETARY]** to reduce its rates to interstate levels. (*See* OCA St. 1, (Loube Direct) Exhibit RL-4).

compliance stage, once the Commission has provided specific direction on the details of the required rebalancing.

## VI. IF THE RLECS' INTRASTATE SWITCHED ACCESS RATES SHOULD BE REDUCED, HOW SHOULD ANY REVENUE REDUCTIONS BE RECOVERED IN COMPLIANCE WITH 66 Pa.C.S.A. 3017?

### A. Meaning Of The Revenue Neutrality Requirement Under 3017

Switched access is categorized as a "noncompetitive" service for all alternative regulation RLECs in Pennsylvania. (Verizon St. 1.1 (Price Rebuttal) at 7). This classification means that the Commission retains the authority to ensure that rates for switched access service remain just and reasonable and that the RLEC's pricing actions are consistent with its alternative regulation plan.[51] The Commission also may rebalance revenue among noncompetitive services on a neutral basis so that rates for one service are reduced and rates for another service or services increased. As the Commonwealth Court recently recognized, "[u]nder 66 Pa. C.S. § 3017 the Commission has specific authority to rebalance revenue among noncompetitive services by reducing access rates *and making revenue neutral increases to other noncompetitive rates.*"[52]

Therefore, to reduce the RLECs' access rates on a revenue-neutral basis as required by the statute, the Commission should provide the RLECs with the option to increase rates for other noncompetitive services in a manner calculated to increase the revenue from those rates to recapture the revenue removed from access rates. The Commission should allow each RLEC leeway to design its own increases, subject to Commission review. While for the most part the other noncompetitive services subject to rate increases are likely to be

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[51] *Buffalo Valley Tel. Co. v. PUC*, 990 A.2d 67 (Pa. Commw. Ct. 2009), slip op. at 21 (upholding Commission's decision to reverse D&E access rate increases).

[52] *Id.* (emphasis added).

basic residential and business dial tone line service, the RLECs should not limit themselves to those services and should be free to propose increases to any noncompetitive service rate, and also should be free to choose to forego some or all of the rate increases, or bank them for future use.

Contrary to the arguments of some parties to this proceeding, Section 3017(a)'s revenue neutrality requirement cannot be satisfied by requiring the RLECs to recover the lost revenue from competitive or unregulated services. This argument is contrary to the Commonwealth Court's finding, discussed above, that the offsetting increases should be made "to other noncompetitive rates."[53] The only reasonable reading of Section 3017(a) in the context of Chapter 30's scheme of alternative regulation is that the RLEC must be given the opportunity to rebalance revenue to other regulated rates within the noncompetitive basket of services, as this would keep the rate changes revenue neutral within the set of those services for which the Commission has authority to regulate rates. The Commission has no authority to direct the RLECs to increase rates for competitive or deregulated services.[54] Further, in a competitive market a company cannot be expected to maintain competitive service prices at levels designed to generate contribution for rate regulated services. (Verizon St. 1.1 (Price Rebuttal) at 32).

Additionally, revenue neutrality cannot be satisfied by requiring other carriers to divert revenue from their own operations to subsidize the RLECs through an expanded USF. Notably, neither 66 Pa. C.S. § 3017(a) nor any other portion of Chapter 30 provides for decreases to noncompetitive revenue to be offset by a carrier-funded state USF. Had the Legislature wished to provide for a state USF as a means to provide revenue neutrality, it

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53 *Buffalo Valley Tel. Co. v. Pa. PUC*, 990 A.2d 67 (Pa. Commw. Ct. 2009) (emphasis added).

54 *See* 66 Pa. C.S. § 3019(g) (Commission has no authority to regulate rates for competitive services).

could have and would have said so. For the reasons discussed in the "USF" section below, it is neither lawful nor good policy to attempt to secure revenue neutrality for the RLECs by assessing the intrastate revenue of other Pennsylvania telephone carriers to transfer revenue to the RLECs.

### B. Rate Increases Are The Appropriate Means To Rebalance The RLECs' Access Revenue

#### 1. The Retail Rate Limitations Advocated By The Other Parties Are Not Supported By The Record

If the Commission determines that the evidentiary record supports the exercise of its statutory authority under 66 Pa. C.S. § 3017 to direct the RLECs to reduce access rates in a revenue neutral manner – which it does – then as both a matter of law and of policy the only way to do so is by "making revenue neutral increases to other noncompetitive rates," as the Commonwealth Court recognized.[55]

The parties have submitted various tables depicting the total monthly, per-line increase to each RLEC's residential rates if its access rates were reduced to match interstate rates, assuming that the revenue would be rebalanced with equal increases to stand-alone basic residential and business service rates. For example, OCA's Exhibit RL-4, under the column "Residential Rates if Access Rates in Parity," depicts resulting residential rates ranging from $9.31 to $30.33. (OCA St. 1 (Loube Direct) Exhibit RL-4). PTA's Exhibit GMZ-13 shows resulting residential rates ranging from $13.50 to $32.91. (PTA St. 1 (Zingaretti Direct) Exhibit GMZ-13). AT&T's Attachment 5 show resulting residential rates ranging from $13.50 to $25. (AT&T St. 1.2 (Panel Rebuttal) Attachment 5 (Revised)). While the line count and access revenue estimates in these tables would have to be updated

[55] *Buffalo Valley*, 990 A.2d 67.

in a compliance filing, these tables provide an evidentiary foundation for the order of magnitude of required rate increases for each carrier.[56]

These tables show that – contrary to the RLECs' and OCA's arguments – it is entirely possible to design a rate rebalancing that will make substantial reductions to the RLECs' access rates and leave their retail rate at a level that is still just and reasonable, in light of the record evidence. In short, the record does not support the proposition that the RLECs cannot increase retail rates to rebalance the revenue.

The RLECs and the OCA concoct various impediments to retail rate increases, largely advanced as part of their arguments that there should be a "benchmark" RLEC residential rate level that should mark the point at which the RLEC cannot be required to increase rates further, but rather should be permitted to take any remaining revenue from other carriers through increased USF subsidies. These arguments are not supported by the law or the evidence, as explained in detail below.

The OCA contends that the RLECs should not be permitted to increase their residential standalone basic service rates above $17.09, even though its concedes that nine of the RLECs already have rates above this level and despite the fact that the Commission already permitted the RLECs in 2003 to raise their rates to $18, with the OCA's agreement. (OCA St. 1 (Loube Direct) at 13 and Exhibit RL-4). OCA did not submit any new evidence in support of this benchmark, but rather, as Dr. Loube explained at the hearing, it simply

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[56] The record contains the information to calculate the per-line increase required to meet the 1.7 cent Verizon benchmark as well. For example, Exhibit GMZ-12 shows the revenue impact of matching Verizon's rate on a per-carrier basis. These amounts could be replaced in the first column of GMZ-13 to calculate the per-line increase required to rebalance that amount of revenue. PTA St. 1 (Zingaretti Direct) Exhibits GMZ-12 and 13. Similarly, the record contains the information to calculate the impact if a larger per-line increase were made to business rates than to residential rates. *See* OCA St. 1 (Loube Direct) Exhibit RL-4 (showing residential and business lines separately by carrier). Again, however, any such calculations would have to be provided in the compliance stage.

relied on the arguments advanced in the first phase of this investigation before ALJ Colwell. (Tr. at 505). The basis advanced to support this benchmark, therefore, is the contention that RLEC rates must be suppressed to keep them "comparable" to Verizon PA's statewide average rates. (*Id.*)

Having never made any specific rebalancing proposal in written testimony, PTA's witness Mr. Zingaretti explained for the first time at the hearing that PTA was relying on the benchmark that it advanced in the first phase of the proceeding, which he explained was $18.94. (Tr. at 585). He conceded that rates could be rebalanced at least up to that point and stated that the PTA would claim the remaining revenue from the USF. (Tr. at 679). In the first phase, PTA's witness Mr. Laffey had argued for a benchmark that was 115% of the average basic residential rate in Verizon's urban Density Cells 1 and 2. (Verizon Phase I Main Br. at 17; Verizon Phase I Reply Br. at 13).[57] This level is also based on limiting the RLECs' rates to keep them "comparable" to Verizon's rates.[58] Like OCA, the PTA did not submit any new evidence in support of its proposal.

CenturyLink's written testimony argued that it cannot increase its residential rates above their current $18 level, but at hearing, CenturyLink's witness conceded that a "reasonable benchmark" "could be something above $18," although he did not explain what that benchmark would be or how it would be calculated. (Tr. at 425-426). The basis for CenturyLink's limitation is to protect CenturyLink from losing lines to competitors. (Tr. at

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57 Although this was never explained in written testimony, Mr. Zingaretti appears to have updated the phase one calculations to account for subsequent Verizon rate increases. As depicted in Verizon's rebuttal testimony in this phase, the current average of Verizon's urban Density Cell 1 and 2 rates is $16.47 (25 cents higher than the average during phase one), and so 115% of that average would be $18.94. (Verizon St. 1.1 (Price Rebuttal) at 37).

58 Tr. at 678 (admitting that this "was simply a comparability number" and "not an affordability number.")

394-95) (conceding that increasing rates above $18 "would be a much easier question if competitive factors weren't at play").

Finally, AT&T, in the course of suggesting a phased-in approach to increasing the RLECs' residential rates, suggested a benchmark starting at $22 and increasing by $1 per year until it reaches $25. AT&T explained that this level was calculated by starting with the $18 rate level from 2003 and "[a]djusting that rate for the inflation that has occurred since then." (AT&T St. 1.2 (Panel Rebuttal) at 5). The seven-year-old $18 rate level that forms the starting point of AT&T's calculations was the product of a settlement and was not based on any analysis of a reasonable level for basic residential rates. (Verizon St 1.2 (Price Surrebuttal) at 8).

**2. There Is No Legal Or Evidentiary Basis To Suppress The RLECs' Residential Rates To Keep Them "Comparable" To Verizon's Rates**

OCA and the PTA concede that their arguments for a $17.09 (from OCA) and $18.94 (from PTA) limit on RLEC residential retail rates are based solely on the concept that RLEC rates must be kept "comparable" to the Verizon ILECs' rates, and they both rely on their arguments from phase one of this case without providing any new evidence. But there is no legal basis to impose a "comparability" restriction on the RLECs' rates – particularly where the purpose of the limit is to argue for an entitlement to USF subsidies funded by other carriers.

These parties argued in the first phase of this case for a "comparability" component to the RLEC rate benchmark based on a federal statute listing governing "principles" for the FCC and the Federal-State Joint Board on Universal Service that rates in rural areas should be "reasonably comparable to rates charged for similar services in urban areas." 47 U.S.C. § 254(b)(3). But the Public Utility Code does not mandate that RLEC rates must be

"reasonably comparable" to any other carrier's rates, and the Commonwealth Court recently held – agreeing with the arguments of this Commission's Law Bureau -- that Section 254(b)(3) is not a mandate to ***state*** commissions constraining the level of intrastate retail rates.[59] In short, there is no legal basis to depress RLEC rates to keep them "comparable" to Verizon's. (Verizon St. 1.2 (Price Rebuttal) at 34).

But even if there were some legal basis that would permit this Commission to limit the RLECs' rates to a level "reasonably comparable" to some other carrier's rates – notwithstanding that the undisputed record shows that customers can afford to pay higher rates, as discussed below – OCA's and PTA's arguments are factually flawed. First, it is unreasonable to use Verizon's basic rates as the standard upon which to limit the RLECs from increasing their own residential rates because Verizon's own rates have been kept artificially low by regulation and there has been no determination either that Verizon's current regulated basic residential local service rates define the level of "affordability" today, or that RLEC customers could not afford to pay rates higher than Verizon's residential rates.[60] Second, OCA deliberately depresses the results of its "comparability" calculation because Dr. Loube does not look to Verizon's "urban" rates – which is the only possible point of reference under 47 U.S.C. § 254(b)(3) (referring to rates that are "reasonably comparable to rates charged for similar services in *urban* areas.") (emphasis added). Rather, Dr. Loube artificially depresses the Verizon rate by purporting to calculate a statewide average, which skews the result downward since Verizon's rural rates are lower. Verizon's "urban" rates are those in Density Cells 1 and 2 only, which are currently $16.32

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[59] *Buffalo Valley*990 A.2d 67, slip op. at 34 (accepting this Commission's argument that Section 254(b) pertains to federal universal service and is not a mandate to state commissions).

[60] Verizon St. 1.1 (Price Rebuttal) at 35.

and $16.62, respectively. (Verizon St. 1.1 (Price Rebuttal) at 37). A rate 120% of the highest Verizon urban rate (i.e., the margin Dr. Loube suggests) is nearly $20 – not the $17.09 that forms the basis of all of OCA's calculations.

PTA's comparability calculations in the first phase, which its witness relies upon here, were also flawed. While PTA used an average of Verizon's urban Density Cell 1 and 2 rates, it used a very low 115% margin. (Phase One, PTA St. 1SR (Laffey Surrebuttal) at 4; Tr. at 484). The record in the first phase demonstrated that both PTA's 115% margin and OCA's 120% margin were purely arbitrary, and even Dr. Loube admitted that other states that tie rates to other carrier rates in the state look to higher percentages, such as 130% in Wyoming and 150% in California. (Phase One, OCA St. 1 (Loube Direct) at 11-12; Phase One, Verizon St. 1.1 (Price Rebuttal) at 34-35). Using a 150% comparability range and Verizon's highest urban rate would yield a "reasonably comparable" rate of $24.93 – a level that would be expected to increase each year with Verizon's exercise of its own price change opportunities.

In sum, while OCA and PTA rely primarily on the evidence from the first phase to support their very low rate cap assertions, neither the law nor the record supports their arguments. Even if comparability to Verizon's rates were a relevant concept, correcting for the factual flaws in their arguments shows that the RLECs could increase their rates as high as nearly $25 and still charge rates reasonably comparable to Verizon's urban rates.

### 3. The Evidence Regarding "Affordability" Does Not Support Suppressing The RLECs' Rates As Some Parties Advocate

While there is no legal basis for a "comparability" restriction on RLEC rates, the Commission has recognized that "the mandates of Chapter 30 require that local service rates be reasonable and *affordable* in all areas of this Commonwealth." (8/5/09 Order at 20)

(emphasis added). But OCA concedes that its affordability analysis does not support the very low $17.09 rate cap that it advocates. Nor does that evidence support the PTA's $18.94 rate level.

As Dr. Loube explained at the hearing, OCA did not submit any new evidence in this phase on affordability for residential telephone rates, but rather Dr. Loube relied on the testimony submitted by OCA's witness Roger Colton in phase one, in which that witness asserted that the affordable rate was $32. (Tr. at 504-505). No other party submitted evidence on "affordability." As Dr. Loube explained in his direct testimony, in order to equate a $32 total bill affordability level to the residential rate benchmarks that have been discussed in this case, it is necessary to subtract from the $32 level the taxes and fees that the customer would pay, such as the subscriber line charge, E-911 fees and the like. (OCA St. 1 (Loube Direct) at 19-20). Dr. Loube agreed under cross-examination that subtracting the relevant taxes and fees, a $32 affordable bill would equate to an affordable benchmark rate of $23. (Tr. at 508-509).[61] Therefore, if OCA did not depress its result with its flawed "comparability" arguments discussed above, then its evidence on affordability could not support a benchmark any lower than $23 – which is $6 higher than the proposed $17.09 benchmark that OCA uses in its calculations and $4 higher than the proposed benchmark mentioned by the PTA witness at the hearing.

Moreover, in concluding that the affordable level is $32, OCA is relying on the most conservative reading of the evidence submitted by Mr. Colton in phase one. Verizon demonstrated that with a few simple and well-supported changes to Mr. Colton's

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[61] Dr. Loube conceded that his assertion at page 20, line 5 of his direct testimony that the $32 affordable bill equated to a benchmark of $20.15 was an error and that number should have been $23. (Tr. at 508). The relevant taxes and fees are depicted on exhibit RL-6 to Dr. Loube's direct testimony and add up to approximately $9.00.

assumptions, his resulting affordable rate would be much higher.[62] Mr. Colton noted that the $32 affordability level he presumed was generated by making the very conservative assumption that the average customer would spend only 0.75% of his income on basic local service, an assumption that Mr. Price explained in his own phase one testimony was not reasonable in light of the facts known about consumer spending.[63] Mr. Colton admitted that if that assumption were adjusted upward only slightly, to 1% of income, the resulting affordability level would be almost $43 – with the subtraction of the $9 in taxes and fees this would equate to a benchmark of $34. (Phase One, Tr. 132-133). The evidence submitted in this phase also demonstrates that the $32 affordability level based on how much the typical household would be expected to spend on local telephone service is conservatively low – as demonstrated by CenturyLink's admission that its average revenue per household is much higher at $45, which is more in line with Mr. Price's adjustments to Mr. Colton's affordability analysis. (Tr. at 436)

#### 4. The Record Does Not Support The Cap The Other Parties Apply To RLEC Business Rates

Another significant flaw in the calculations submitted by the other parties is their assumption that in any rate rebalancing the RLECs' business rates cannot be increased more than the dollar-per-line increase on their residential rates. But nothing in Chapter 30 prohibits a carrier from making a higher per-line increase on business rates. In fact, for

[62] Phase I, Tr. at 132; Phase I, OCA St. 2 (Colton Direct) at Schedule RDC-5; Phase I, Verizon St. 1.1 (Price Rebuttal) at 24.

[63] Mr. Colton's analysis is conservative in assuming that customers can "afford" to spend just 0.75% of a family's income on basic local telephone service. Mr. Price demonstrated that according to the FCC's own data, households in the lowest quintile of household income in 2006 spent on average 3.11% of their total household expenditures on telephone services and that the average household expenditure for telephone services for rural households was 2.62% of total household expenditures. (Phase I, Verizon St. 1.1 (Price Rebuttal) at 25-26 and Exhibit 3). If only half of the average rural household expenditure were for basic local service it would still be 1.3% of total expenditures, or $43.25 per month. This data suggests that Mr. Colton's affordability estimate is conservative and too low. (*Id.* at 25-26).

Verizon, Chapter 30 limits the revenue it may allocate to residential rates when it implements its annual inflation-based rate increases, and so Verizon's business rates routinely receive a higher per-line increase than its residential rates.[64]

There is no record support for the proposition that the RLECs should not be permitted to increase their business rates beyond the same dollar amount by which residential rates are increased. None of the witnesses attempted to explain why basic business rates could not increase more than residential rates if necessary to absorb an access rate rebalancing before turning to claim USF subsidies– even if one accepted their flawed premise that residential rate increases should be limited. This was the same flaw with the RLEC/OCA position in the first phase, and although Verizon pointed out several times the lack of evidentiary foundation to limit RLEC business rate increases, no one ever produced any actual evidence in support of the proposition, nor did anyone attempt to rebut Verizon's evidence that showed that the RLECs' business rates are relatively low and could be increased without any constraint. The record simply does not contain the evidence to support imposing a business rate cap at all, much less to restrict the RLECs from increasing their business rates and instead requiring other carriers – including their direct competitors – to reimburse them so that they may ***avoid*** raising their business rates.

The PTA's witness in the first phase, Mr. Laffey, conceded that the national average single line business rate was $36.59 in 2007.[65] This 2007 national average is ***$10 higher than*** CenturyLink's business rate of $26.23 and higher than many of the other RLECs'

[64] 66 Pa. C.S. § 3015(a)(3).

[65] Phase I, PTA St. 1R (Laffey Rebuttal) at 22. *See also* FCC Trends in Telephone Service, August 2008, Table 13.2. (Price Rebuttal Exhibit 1).

business rates.[66] It would be an absurd result to require other carriers, including direct competitors, to reimburse the RLECs through an expanded USF to allow them to avoid increasing business rates that are presently about $10 or more below the national average. In this phase, OCA and the RLECs, and even AT&T, presume that business rate increases would be no higher, on a dollar per line basis, than the residential increases. But this presumption is not supported by the record.

### 5. The Record Shows That RLECs Can Rebalance More Revenue To Retail Rates Than Is Depicted In The Other Parties' Tables.

The other parties' rate rebalancing calculations are flawed because of their incorrect assumptions that RLEC residential rates must be capped at unsupportably low levels and that business rate increases must be kept equal to residential increases. With a more flexible rate design, the individual RLECs can be expected to rebalance more revenue to retail rates then they, the OCA or AT&T have depicted in the worksheets attached to their testimony. AT&T's own calculations, for example, show that if the RLECs increase their residential rates to $23 instead of $22 in the first step (even with the unsupported limitation on business rate increases that AT&T assumes), then the revenue left unrecovered from retail rate increases under AT&T's scenario would be cut by more than half. (AT&T St. 1.2 (Panel Rebutal) Attachment 5). In that case (AT&T's Step 2), 19 of the RLECs would be able to rebalance their access rates to match their interstate rates if they increased their residential rates to $23 and made an equal increase to business rates.

Neither the RLECs nor the OCA has made any effort to design a rebalancing that would minimize residential rate increases, for instance by allocating more revenue to

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66 Each RLEC's current business rate is depicted in AT&T's Attachment 5 to the Panel Rebuttal Testimony.

business rates and/or allocating some of the revenue to other noncompetitive service rates. Because their goal is to argue for expanded USF subsidies, their motive is to make the prospective residential rate increases look as large as possible. But even with that bias in mind, the charts provided by the PTA (PTA St. 1 (Zingaretti Direct), Exhibit GMZ-13) and the OCA (OCA St. 1 (Loube Direct), Exhibit RL-4) reveal that many of the RLECs could rebalance the necessary access revenue while still keeping residential rates below the most conservative $23 affordability level. With more thought given to rate design, they might be able to keep the residential increases even smaller. The RLECs and OCA are deliberately creating obstacles to a reasonable rebalancing to support their claim for risk-free, carrier-funded USF subsidies (debunked below).

Given these facts, each RLEC should be required to submit a rebalancing plan in the form of a compliance filing that assumes a $23 residential rate and reasonably maximizes the revenue allocated to other rates for noncompetitive services, and reduces their access rates uniformly to the Verizon PA level. (Verizon St. 1.1 (Price Rebuttal) at 39). The Commission can then address whether it is reasonable for any RLEC to implement a transition plan reducing their access rates in steps and/or to establish rates higher than $23. But in no event should these compliance filings create new "entitlements" to other carriers' revenues from the flawed USF.

And of course this is not an "all or nothing" proposition. While the best result is for all RLECs to match Verizon's benchmark rates, the Commission should look at the rebalancing on a carrier-by-carrier basis. It is unquestionable that each and every RLEC has room for some access rebalancing if the matter is approached with an open mind to the optimum rate design. In short, Verizon is not asking for any of the RLECs to be left without

the opportunity to collect this revenue from their end users -- but it is ultimately up to them if they want to use the opportunity or not. In fact, this is the model that the Legislature established via Chapter 30.

### 6. The Contention That RLEC Rates Should Be Capped To Protect The RLECs From Losing Lines To Competition Is Unsupportable

The least valid reason advanced for capping RLEC rates is the notion that the RLECs must be protected from increasing their rates to avoid competitive losses – particularly since the cost of protecting the RLECs from competition is to require other carriers to subsidize their operations, either through excessive access rates or through the USF.

It is evident that the real reason the RLECs do not wish to increase their rates is not because customers could not afford to pay higher rates, and is not because there is some legal requirement to keep rates "comparable" to Verizon's rates. Rather, PTA and CenturyLink argue that they cannot be required to increase basic dial tone rates beyond current levels because of competition from other telecommunications providers. For example, PTA's Mr. Zingaretti suggests that the only thing holding back an onslaught of competition and customer alternatives is the fact that the RLECs are allowed to charge relatively low retail rates because of the revenue support provided by high access rates. (PTA St. 1-SR (Zingaretti Surrebuttal) at 49) (asserting that if RLECs increase their retail rates they will face "massive customer attraction campaigns" from competitors and "massive migrations" by customers pursuing "attractive offers" from competitors). As CenturyLink's witnesses conceded at the hearing, "it's a safe summary of CenturyLink's position in this case that [it] cannot raise rates because customers will leave and go to a competitor," and that CenturyLink fears a rate rebalancing "could . . . artificially move

market share to competitive carriers." (Tr. at 394, 422).[67] Indeed, CenturyLink submitted a study purporting to show that customers would depart for a competitor if it increased its basic service rates over $18. (CenturyLink St. 2.0 (Staihr Direct, Adopted by Harper)).

But the notion that some customers might defect to competitors of CenturyLink or the other RLECs actually *confirms* that universal service would not be jeopardized by an increase in basic exchange rates. If it is true that some customers would switch to RLEC competitors, affordability and universal service concerns do not apply because by definition affordable service is available. In fact, some switching to competitors is to be expected in a free market when an RLEC's artificial competitive advantage (the ability to charge local rates well below the market rate because of subsidies) is reduced. When competition has taken hold, it is time to reduce or eliminate the costs imposed by outdated regulatory burdens that prevent the RLECs from meeting the competitive price in the market. Because the RLECs concede that their customers have competitive alternatives, the competitive market is already ensuring universal service at affordable rates in RLEC territory and there is no reason to allow the RLECs to continue to depend unduly on other carriers for their revenue through high access rates or the state USF. And using excessive access rates or the USF as a means for the RLECs to fend off competitors is directly contrary to the pro-competitive goals of Chapter 30, including the obligation to "ensur[e] that rates, terms and conditions for protected services are reasonable and *do not impede the development of competition.*" 66 Pa. C.S. § 3011(5) (emphasis added). Instead, the Commission should move the RLECs to a more efficient rate structure that secures more revenue from their own end users and should focus on reducing the RLECs' costs by alleviating any regulatory

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[67] CenturyLink's witness has it backward, of course. Competition is not "artificial." What is "artificial" is subsidizing the RLECs' operations to diminish competition.

burdens that are no longer needed in a competitive market. The Commission should look to effectuate the legislative policy of "recogniz[ing] that the regulatory obligations imposed upon the incumbent local exchange telecommunications companies should be reduced to levels more consistent with those imposed upon competing alternative service providers." 66 Pa. C.S. § 3011(13). To the extent such a lightening of outdated regulatory burdens would allow the RLECs to operate more efficiently and reduce their own underlying costs, that result would be beneficial for the RLECs, for consumers and for the competitive market.

While protecting the RLECs from competition is not a valid basis either to cap their rates or to force other carriers to continue with anti-competitive subsidies, Verizon is not suggesting that any company should be forced by regulation to operate its business at a loss. If an RLEC came forward with specific evidence to show that it is indeed operating at a loss – which no RLEC has done here – the Commission would have to take appropriate action. This, however, is a theoretical question because no such evidence has been presented and the record here shows that the Commission can address the rebalancing of the RLECs' access rates within the parameters of Chapter 30.

### C. The Pennsylvania USF Should Not Be Used To Fund This Rate Rebalancing

The RLECs, OCA, and to a lesser degree AT&T, propose to replace access revenue dollar-for-dollar with funds from the USF, as if it were an easy and cost-free solution to the problem of reforming the RLECs' access rates – but that suggestion could not be farther from the truth. This forced revenue transfer is not authorized by current law, but even it were, imposing a huge "hidden tax" increase on the revenue of other regulated carriers

would be the worst thing the Commission could do from a policy perspective in today's hyper-competitive communications market.

The parties urging the expansion of the USF appear to have lost sight of the fact that, as ALJ Colwell recently explained, the USF "is not 'free money' to be plundered at will and without concern for its origins or for whether it is the best use of the money." (Colwell 7/23/09 RD at 87). In fact, "[t]he PA USF is a fund which exists because the ratepayers of other telecommunications providers have paid the money, unwittingly, as a hidden tax." (*Id.*) It is unsupportable from both a policy and a legal basis to expand and make permanent the very same state USF that ALJ Colwell recently concluded was hopelessly flawed and in need of a complete overhaul.

The parties' proposals in this regard are astoundingly brazen. By its own estimation, OCA's plan would permanently increase the USF by $63 million per year — which when combined with the current fund would force other regulated carriers to transfer nearly $100 million of their intrastate revenues to the RLECs every year.[68] But the Commission made quite clear in its order setting the scope of this investigation that it was not presuming or guaranteeing that it would replace any of the access revenues with USF subsidies, noting that "we would like to remind the Parties who rely on the PaUSF that access charge reform in Pennsylvania may or may not depend upon the continuation of the PaUSF" and "we are not constrained by the PaUSF for access charge reform." (12/10/09 Order at 23). For the

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[68] While the RLECs have not made a straightforward proposal, both the PTA and CenturyLink make clear that they believe they are entitled to replace some or all the access revenue with money from the USF to avoid raising their retail rates, which would expand the USF by as much or more than the OCA proposal. As Mr. Zingaretti explained at the hearing, it would require $91.7 million in revenue to be rebalanced for all the RLECs to mirror their interstate rates. (Tr. at 588). The PTA agrees that some unspecified portion of this revenue could be rebalanced to retail rates, with an unspecified but likely substantial portion being subsidized by the USF. (Tr. at 676-77).

reasons below, the Commission should reject any proposal to expand the USF to fund RLEC access reductions.

#### 1. Expansion Of The USF Is Not Authorized By Current Law

The existence of the current USF – which was created in 1999 under the now-expired version of Chapter 30 – does not mean that the Commission has the statutory authority now to create a new USF to fund new access decreases in light of today's different Chapter 30 statute and under today's very different market conditions, especially where contributing carriers do not agree to it.

The *Global Order* USF was a temporary measure, proposed through a settlement under which other regulated carriers would make payments to the RLECs to reimburse them for the access and toll rate decreases agreed to in the same settlement. The fund collects its money from all telecommunications providers (excluding wireless carriers) based on their intrastate end-user telecommunications revenues, but only the RLECs receive support from the fund. As the Commission explained, "[a]lthough it is referred to as a fund, it is actually a passthrough mechanism *to facilitate the transition from a monopoly environment to a competitive environment* – an exchange of revenue between telephone companies."[69] This arrangement was clearly intended to be temporary, as the Commission explained: "[t]he interim funding mechanism that we create through this order will function until December 31, 2003, or until the subsequent ... investigation develops a new process, *whichever occurs first*."[70] ALJ Colwell therefore rightly concluded in phase one of this investigation that, "[l]ooking back over the Commission's Orders leading up to this Investigation, it is clear that there was no expectation by the Commission that the PA USF

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[69] *Global Order*, slip op. at 135 (emphasis added).

[70] *Global Order*, slip op. at 146 (emphasis added).

would be institutionalized in its present form," and that "[t]he parties to [the *Global Order*] litigation, as well as the parties to the Access Charge Investigation were agreeable to settlement because they believed that the Commission would institute *and litigate* an investigation which would address and handle the PA USF and access charge issues in a timely manner." (Colwell 7/23/09 RD at 88).

The Commonwealth Court affirmed the Commission's creation of the *Global Order's* temporary USF primarily because it found that Verizon's predecessor, Bell of Pennsylvania, was estopped from challenging the Commission's legal authority to establish the USF, having conceded that authority by agreeing to prior USF proposals under the governing statute at that time.[71] But that same reasoning cannot be used here because Verizon has consistently opposed expansion of the USF to fund future RLEC access reductions under the current Chapter 30.

The Commonwealth Court also accepted the Commission's argument that the old Chapter 30 provided sufficient state law authority to establish the USF because of its declaration of policy to maintain telecommunication services "at affordable rates," and to ensure that "customers pay only reasonable charges for local exchange telecommunications services," and the retention of power to the Commission to "establish such additional requirements and regulations as it determines to be necessary to insure the protection of consumers." (*Id.*) The Commission had argued that its authority is "not limited to the mere letter of the law, but must look to the underlying purpose of the statute and its reasonable effect," and it contended that the interim USF served those underlying purposes. (*Id.*)

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[71] *Bell Atlantic-Pennsylvania, Inc. v. PUC*, 763 A.2d 440, 496, 2000 Pa Commw LEXIS 592 (Commnw. Ct. 2000), *rev'd on other grounds, MCI WorldCom Inc. v. PUC*, 572 Pa. 294, 844 A.2d 1239 (2004)..

But the governing law and the operative facts today are not the same as they were when the Commission adopted, and the Commonwealth Court approved, the interim transitional USF ten years ago. Since that time, "Act 183" has replaced the old Chapter 30, which expired by its own terms at the end of 2003. When Act 183 became law at the end of 2004, it contained a provision permitting the Commission to rebalance access rates in a revenue neutral manner. 66 Pa. C.S. § 3017(a). But it made no reference at all to a state USF being used as a source for that revenue. Had the Legislature wished to authorize such a mechanism or to endorse the expansion of the current USF for future access reductions, it could have and would have said so. The new Chapter 30 also now limits its preservation of the Commission's authority "to ensure the protection of customers" by specifying that any "such additional requirements" must be "*consistent with this chapter.*" 66 Pa. C.S. § 3019(b)(3) (emphasis added). The new Chapter 30's policy objectives include promoting competition and reducing regulatory burdens on regulated carriers. 66 Pa. C.S. § 3011(8), (9) and (13). Where the Legislature omitted any mention of a USF and did not expressly authorize its use to rebalance access rates, the Commission cannot reasonably conclude that forcing other carriers to transfer their own revenues to the RLECs as proposed is "necessary to ensure the protection of customers" or that it is "consistent with this chapter." As discussed below, forcing regulated carriers to transfer their own revenue to the RLECs will impede competition and harm consumers, is not necessary to ensure "universal service" and will exacerbate the regulatory burdens on the Verizon ILECs and other regulated carriers, all the exact opposite of the policies Chapter 30 seeks to advance.

But even if the Commission had the statutory authority to increase the size of the fund, the current USF regulations make no provision for increasing the fund size to account

for future RLEC access reductions. The regulations determine the size of the fund each year based on the "[p]rior year's size of fund minus the estimated surplus from the prior year or plus any shortfall from the prior year." 52 Pa. Code § 63.165(b). The only provision to increase the fund size is "due to growth in access lines of recipient carriers," (*Id.*), but the RLECs indicate that the recipient carrier lines are declining. Accordingly even if the contributing base and methodology remained the same, the size of the fund could not be increased without a rulemaking to alter the existing regulations, and therefore could not be accomplished through this proceeding.

Accordingly, the Commission should conclude that current law does not authorize the use of other carriers' revenues through the USF to fund the RLECs' access reductions, and should not consider expanding the USF as an option when designing the rate rebalancing here.

#### 2. Expanding The USF Will Impose Huge New Regulatory Burdens On Other Regulated Carriers, Which Are Not Tenable In Today's Competitive Market

In light of Chapter 30's directive to reduce burdens on incumbent local exchange carriers and promote competition, the Commission must consider the huge regulatory burden that the USF advocates seek to impose on the Verizon ILECs and other regulated carriers, and the adverse consequences to those companies and their customers.

The undisputed record evidence shows that replacing revenue from the RLECs' access rates with revenue from the USF would dramatically increase the funding burden on the Verizon ILECs. For example OCA proposes to transfer $63 million in revenue from access rates to the USF. Today the Verizon ILECs would pay about $5.4 million of this

amount through access rates, and other carriers, primarily IXCs, would pay the remainder.[72] But if the $63 million were instead to be paid out by increasing the current USF, where the share to be paid by carriers is based on their intrastate revenue rather than by the extent to which they use the RLECs' networks, the Verizon ILECs' share of the burden would be an additional $32 million each year (on top of the $17.2 million that they already pay to the USF).[73] In other words, the Verizon ILECs would save $5.4 million in access payments due to the reduction of the RLECs' access rates, but would gain $32 million in new USF costs, for a net increase in their funding burden to the RLECs of nearly $27 million. There has been no evidence presented to the Commission that even attempts to justify such a massive transfer of wealth from Verizon to other carriers.

It is difficult to fathom how the OCA could view a $27 million per year additional revenue drain on the Verizon ILECs to be a pro-consumer outcome. While the RLECs lament their own line losses and pressures from competition in an attempt to argue that their own revenue cannot be reduced to any degree and that they must be subsidized by other carriers, their competitive pressures pale in comparison to the erosion in Verizon's business over the same time period. The Verizon ILECs operate in markets that are far more competitive than the RLECs' territory. Since 1999, through 2009, the Verizon ILECs have experienced line loss of **[BEGIN PROPRIETARY]** **[END PROPRIETARY].**

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[72] If all of the Verizon companies are considered, Verizon would pay $13.2 million of the $63 million in access charges. This calculation is based on data produced in discovery on the volume of interexchange traffic originated and terminated to the RLECs' networks. The Verizon companies as a group (IXCs, ILECs and CLECs) pay approximately 21% of the total RLECs' intrastate access revenue. The remaining 79% is paid by other carriers. The Verizon ILECs alone pay about 8.6% of that total. (Verizon St. 1.2 (Price Surrebuttal) at 11-12).

[73] The share of all Verizon companies taken together would be $36 million. This calculation is based on the fact that the Verizon companies as a group currently pay about 57% of the assessments to the USF each year. The Verizon ILECs pay 51%. This calculation is based on the 2009 assessments. The total USF assessment was $33.8. The sum of the Verizon companies' share was $19.4 million. The Verizon ILECs' share was $17.2 million. Verizon St 1.2 (Price Surrebuttal) at 12.

(Verizon St. 1.1 (Price Rebuttal) at 19). Because of such losses, Verizon's contributions to the USF are now supported by only a fraction of the access lines that it served in 2000. For every Verizon access line in 2000, there was only **[BEGIN PROPRIETARY]**

**[END PROPRIETARY]** access lines in 2009. On a per-access line basis, that means for every line paying $1 to fund the USF in 2000, that line in 2009 must pay **[BEGIN PROPRIETARY]** **[END PROPRIETARY]** in 2009 to satisfy the same contribution burden. And the RLECs and OCA now propose to expand the USF burden. It is no longer supportable in today's market to expect Verizon and its customers to fund the RLECs' operations through access charges and/or through the state USF.

The Verizon ILECs cannot be expected to absorb the costs of operating their regulated business in today's highly competitive market and at the same time be forced to turn the revenues that they earn over to the RLECs. At the very least, the Commission would first have to examine whether this forced revenue transfer, together with the other regulatory burdens imposed on the Verizon ILECs and the loss of revenues due to competition, would cause them to operate their regulated business in Pennsylvania at a loss. *Brooks-Scanlon v. Railroad Comm'n of La.*, 251 U.S. 396, 399 (1920) (a carrier cannot be compelled to carry on its regulated business at a loss).

Depriving the Verizon ILECs of revenues needed to operate their own business is not only harmful to the companies but also to customers. The Verizon ILECs provide a broad array of services throughout their territories, including service to a larger number of rural access lines than all of the RLECs put together, and they continue to meet and/or exceed their own broadband availability commitments. All of these obligations come with costs, and the Verizon ILECs receive no state USF subsidies and charge much lower access

rates than the RLECs. Further, many of their services are competitive and subject to pricing constraints by the market, and their rates for noncompetitive services are capped by the inflation-based Chapter 30 formula. If the Verizon ILECs are required to increase their already substantial transfer of revenue to the RLECs through the state USF, this new unfunded revenue drain would divert revenue from Verizon's operations that would otherwise be used to serve Verizon's customers and support its own business, such as by investing in the network, maintaining or improving products and services or through meeting competition on rates. It would be a disservice to the consumers in Verizon's territory to force Verizon to bear a larger burden of subsidizing the RLECs' operations. The purpose of this case is to decrease the burden Verizon and other carriers have borne over the years through a combination of USF contributions and excessive access rates, and to have the RLECs secure more of their revenue from their own end-users.

Although the RLECs are quick to insist on revenue neutrality for themselves – even demanding that the Commission protect their revenue stream from losses due to competition – the huge amount of revenue they propose to take from Verizon through an expanded USF is decidedly *not* revenue neutral.[74] But the Verizon ILECs operate under the same form of alternative regulation authorized by Chapter 30, under which, as Mr. Kubas explained, "[t]he concept behind the . . . price cap regulation is that [I]LECs are free to make as much profit (or absorb as much loss) as they can as long as the [I]LEC follows its Chapter 30 (now Act 183) Plan." (OTS St. 1 (Kubas Direct) at 20). This construct does not work if the Commission can step in and force Verizon to send tens of millions of dollars each year to the RLECs.

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[74] *See, e,g,* 52 Pa. Code § 63.170 ("A telecommunications service provider may not implement a customer or end-user surcharge or any other direct or indirect charge to recover any contributions to the Fund.")

The other parties downplay the magnitude of the burden they are trying to impose on the other regulated telephone companies that currently must contribute to the USF by arguing that the Commission can increase the contributing base to the USF by requiring additional carriers such as wireless and voice over internet protocol ("VoIP") providers to contribute.[75] But again this is something that cannot be accomplished in this phase of the proceeding, if at all. The Commission has ruled that "[e]xamination of whether wireless carriers and VoIP service providers should be contributors to the PaUSF" is not a proper issue to be raised in this phase of the investigation. (12/10/09 Order at 24). Therefore, it certainly is not proper to presume that the funding base of the USF will be increased in making the decisions required in this phase of the proceeding. But even if the point came where the Commission were to entertain arguments to force wireless and VoIP carriers also to transfer their revenues to the RLECs, these carriers are likely to raise various additional legal challenges to the authority of this Commission to force them to contribute to the USF, and the outcome of any such attempt is far from certain. And simply as a policy matter, imposing such burdens on the more innovative services would greatly discourage investment in new technologies in Pennsylvania – the very opposite of the outcome Chapter 30 seeks to encourage.

### 3. Increasing The USF Does Not Remedy The Anti-Consumer Effect Of Excessive Carrier-Funded Subsidies To The RLECs

In light of Chapter 30's directives to encourage competition and protect customers, the Commission must consider the fact that the anti-competitive and anti-consumer problem that is presented by allowing the RLECs to collect too much revenue from other carriers through their high switched access rates is not remedied by allowing them to collect the

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[75] *See* PTA St. 1 (Zingaretti Direct) at 56; Tr. at 513 (Dr. Loube).

same revenue from other carriers in a different way through the USF. As Sprint's Mr. Appleby explained, "[a]ny suggestion of a half-measure, such as merely shifting the carrier charge subsidy into the PA USF, fails to address the problem and will merely perpetuate 'inefficient, uneconomical and unfair' loop recovery." (Sprint St. 1.2 (Appleby Rebuttal) at 10; *see also id* at 19 (recognizing that replacing RLEC access revenue with USF would still constitute a "hidden tax.")). Shifting the revenue to the USF would only change "the way these overcharges are collected from competitors' customers." (*Id.* at 47). According to OSBA's Mr. Wilson, "there is no justifiable economic reason to provide a general PAUSF subsidy to all RLECs" and "indiscriminate PAUSF funding could be having the unintended consequence of keeping lower cost competitors out of subsidized rural markets rather than promoting competition." (OSBA St. 2 (Wilson Rebuttal) at 17). Comcast's Dr. Pelcovits explains that "[i]t would be counterproductive . . . to offset reductions in access revenue with a dollar-for-dollar increase in the Pennsylvania USF. This would constitute corporate welfare and would obviate the public policy benefit from targeting subsidies to the highest cost geographic area and limiting the size of the subsidy to the minimum necessary to achieve social objectives." (Comcast St. 1.2 (Pelcovits Rebuttal) at 23). The AT&T witnesses acknowledge that the USF "is not a free lunch; while it may look like local service rates are lower, the money is just coming from somewhere else," and that "responsibility for RLEC cost recovery" belongs with the RLECs' own retail customers. (AT&T St. x (Panel Rebuttal) at 13).

More than tripling the size of the USF to provide further subsidies to the RLECs' operations would be detrimental to both consumers and carriers, because it would encourage the RLECs to continue relying on artificial subsidies rather than becoming more efficient

and/or innovative in their operations. This is the exact opposite of the incentive that alternative regulation is intended to provide. Expanding the USF in this manner would simply perpetuate the anticompetitive *status quo* under which one set of providers (the RLECs) recovers network costs from other providers. Such a result is incompatible with and harmful to the workings of a competitive market for communications services. Indeed, it would recreate the exact same problem that is inherent in the RLECs' excessive access rates, albeit through a slightly different mechanism. Just as with the current excessive access rates, customers of the carriers forced to contribute to the USF would be denied the benefits of revenue that otherwise could have been used to improve the companies' products, services, or networks, or even to reduce rates. Customers in the RLEC territory will also suffer. Although they will theoretically have access to stand-alone basic service from the RLECs at rates lower than what otherwise might have been charged, their opportunities for competitive alternatives will be diminished because any carriers that wish to come in and compete with the RLEC will have to compete with heavily subsidized operations and either may choose not to do so or may not compete as effectively. These RLEC customers might also be deprived of service, product and network innovation by the RLEC itself, because an RLEC that is guaranteed a constant and risk-free stream of revenue from a source other than its customers, and that also faces a diminished competitive threat, will naturally have less incentive or need to deploy innovative products and services to retain and attract customers. In fact because the USF contributions are calculated based on the carriers' intrastate revenue, communications companies that might otherwise have chosen to invest in Pennsylvania could choose to take their business elsewhere, leaving Pennsylvanians in general with fewer competitive options at a time when attracting

technological innovation is even more critical to Pennsylvania's future. (Verizon St. 1.1 (Price Rebuttal) at 48-49).

The only way actually to solve the anti-competitive and anti-consumer problem of excessive RLEC access rates is to have the RLECs reduce their dependence on revenue provided by other carriers and recover that revenue instead from their own end users.

#### 4. "Universal Service" In RLEC Territory Is Not In Jeopardy

To the extent the other parties rely on Chapter 30's directives regarding the protection of universal service as support for increasing the USF, the Commission must consider the record evidence that shows that universal service is not in jeopardy in RLEC territory and that forcing other carriers to prop up the RLECs' businesses financially is not necessary to advance universal service.

The RLECs themselves concede that customers in their territories enjoy access to affordable services from a number of different competitive options. As CenturyLink's Mr. Bonsick explained, "CenturyLink continues to see robust inter-modal competition for residential consumers, including wireless, voice and data services, cable voice and data services, and VoIP services (e.g., Vonage, Magic Jack). And on the business customer side, IP and data service providers are targeting all classes of business customer." (CenturyLink St. 3.1 (Bonsick Surrebuttal) at 11). It is clear that an expansion of the fund is not needed to spur universal service, and in fact may well have a negative effect. When consumers have access to quality services that are being provided by a number of competing carriers and technologies, at affordable rates (as the RLECs' testimony asserts is the case in Pennsylvania today), the goals of universal service are achieved through the workings of competitive markets, and artificial subsidies – particularly new ones based only on anecdotal evidence – are unnecessary.

When the Commission created the present USF over 10 years ago, it recognized that it was a temporary or interim measure that was only intended *"to facilitate the transition from a monopoly environment to a competitive environment."*[76] As ALJ Colwell pointed out, eventually "the market is meant to rely on competition to keep rates affordable" rather than continuing to "provide subsidies to companies who do not have to prove need," which she observed "will not assist the market in reaching its goals and will, instead, provide barriers to entry for new carriers." (Colwell 7/23/09 RD at 87). The record shows that the "competitive environment" the Commission foresaw back in 1999 has now arrived. There is no need to force other carriers to subsidize the RLECs' operations to ensure universal service.

The RLECs attempt to have it both ways – they argue on the one hand that competition extends to every single exchange in their territories and threatens the viability of their business from all fronts, but on the other hand, they then attempt to claim that some unspecified customers in undisclosed locations have no alternative to the RLECs for service and need their basic service rates to be maintained at artificially low levels. As CenturyLink's witness explained its position at the hearing, "in every exchange, there's likely at least one customer who has a competitive option, but in all exchanges there are customers without competitive options," and one would have to go "street by street and house by house" to find, for example, cell phone "dead spots" to determine where competition is absent. (Tr. at 392). But this transparently self-serving attempt to evoke "universal service" concerns does not survive scrutiny. Moreover, to the extent there is a universal service concern for isolated individuals based on unique circumstances, this can be

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[76] *Global Order*, slip op. at 135 (emphasis added).

addressed with Lifeline service and/or through the rulemaking recommended by ALJ Colwell.

### 5. To The Extent A Transition Mechanism Is Needed, It Would Be Simpler And Less Controversial To Step Down The RLECs' Access Rates Over Time Rather Than To Transfer Revenue To The USF

While OCA and the RLECs envision a permanent entrenchment of the USF sending nearly $100 million in revenue to the RLECs each year in perpetuity, AT&T proposes a variation on the use of the USF, arguing that the USF could be temporarily expanded so that the RLECs could reduce their access rates immediately but increase their retail rates over several years to rebalance the revenue.

But there is no need to implicate the USF in this scenario. If a transition period is needed at all, then considerable litigation and debate can be avoided simply by reducing the RLECs' rates, phased-in over a few steps. The Commission should prefer the simpler answer in this instance over the more complicated one. As a practical matter, increasing the assessments to the state USF will bring in unnecessary administrative complexity to this case and the potential for continued litigation, appeals and delay, particularly if the Commission attempts to expand the contributing base. It would also require a rulemaking since the current regulations do not provide a process to increase the size of the fund in this manner even on a temporary basis, as discussed above. Further, increasing USF assessments may provide a shock to smaller carriers who are not participating in this case and who do not realize that their USF assessments could substantially increase under AT&T's plan. Moreover, shifting the revenue away from access rates to the USF unfairly skews the burden away from the IXCs and toward other LECs, as discussed above, which

would be harmful to consumers.[77] By far the simpler approach, if it is concluded that a transition period is needed, is to leave the revenue in access rates and take those rates down in defined steps over a period of time. There is no reason to add the complexity and extra step of first expanding the state USF.

As a substantive matter, moreover, there is no benefit to be gained by shifting this revenue to the USF to secure a larger immediate access reduction, as opposed to the more administratively simple stepping down of the RLECs' access rates over time, if a transition is found to be necessary. As discussed above, the RLECs should be reducing their dependence on revenue from other carriers, not simply shifting that burden from access rates to another carrier-funded source such as the state USF. Shifting the revenue to another carrier-funded source does nothing to ameliorate the adverse impact on customers both of the contributing carriers (because those carriers have less money to spend serving their own customers) and of the RLEC (because their customers still face diminished opportunities for competitive alternatives and the RLECs will continue to have diminished incentives to engage in service, product and network innovation). (Verizon St. 1.1 (Price Rebuttal) at 48-49).

Increasing the state USF – even on a purportedly "temporary" basis – is not good policy and is bad for consumers. Pennsylvania's telephone carriers already provide over $33 million each year in a direct revenue transfer to the RLECs through the current USF, which as discussed in Verizon's rebuttal testimony provides a windfall to the RLECs: they have been guaranteed a constant amount of revenue since 2000 notwithstanding declines in

[77] Verizon St. 1.2 (Price Surrebuttal) at 11-12 (explaining how a transfer of revenue from access rates to the USF as currently constituted transfers a substantial portion of the funding burden from the IXCs to the Verizon ILECs).

access lines and access minutes. (Verizon St 1.1 (Price Rebuttal) at 47). The Verizon family of companies alone provides nearly $20 million to the RLECs each year through their USF assessments, without even considering the additional revenue they are forced to contribute by paying the RLECs' excessive intrastate access rates. ALJ Colwell concluded that this current fund is a "hidden tax" that should be revisited and reconstituted. The Commission should not exacerbate this "hidden tax" by increasing the USF, even on a temporary basis.

But because AT&T and OCA offered proposals in the spirit of compromise, Verizon offered an alteration to AT&T's proposal that would allow excess funds in the *current* USF to be used for a short transition period without requiring any carrier to increase its current state USF contribution (and therefore not requiring any change to the current USF regulations). Specifically, the current USF contains approximately $8.4 million in excess funds that are today providing a windfall to the RLECs and that should be removed from the current USF immediately. (Verizon St. 1.1 (Price Rebuttal) at 47).[78] The Commission could redirect those excess USF funds toward the specific RLECs that require a longer transition for the new access reductions for a short period of time (while the rulemaking to

[78] Verizon's Mr. Price explained that the current ten-year-old USF is providing a windfall to the RLECs. If the RLECs had rebalanced the revenue to local service rates or left it in access and toll rates back in 1999-2000, those revenues would have diminished rather than being a constant annual stream of revenue of over $30 million a year for nearly 10 years, as they have been with the USF. If the RLECs had rebalanced their access and toll reductions with basic local service rate increases in 1999-2000, the over $30 million in annual revenue from 1999-2000 would have decreased by at least 20%, to $24 million, due to the line loss they describe. CenturyLink's share of $6 million would have declined by 28% to $4.3 million. Even if the RLECs had not rebalanced the revenue at all and left the toll and access rates the same, given industry trends the RLECs' access and toll minutes-of-use over this time have decreased, which would have reduced the resulting revenue. Using information recently released by the FCC, the volume of intrastate access minutes dropped by at least 22% on an industry-wide basis from 1999 through 2006. Extrapolating the annual average decline through the end of 2009, the decline would be 31.6%. Yet because they are receiving the replacement revenue from other carriers who cannot choose to stop paying, the RLECs are still receiving over $30 million a year nearly ten years later, even though they would not be receiving that level of revenue in the absence of the USF. Reducing the current USF by 25% would reduce the present $33.6 million contribution to $25.2 million. The difference is $8.4 million. (Verizon St. 1.2 (Price Surrebuttal) at 14-16.

alter the fund is being litigated), to help phase in revenue neutral rate increases. Under no circumstances, however, should the current state USF be increased, even on a temporary basis as proposed by AT&T.

## VII. GENERAL LEGAL ISSUES

### A. Retroactivity Of Any Access Rate Reductions

Verizon is not seeking retroactive access refunds from the RLECs. Some parties have argued that 66 Pa. C.S. § 1309(b) requires that AT&T's complaints against the RLECs be decided within nine months of the date the complaint is filed, or alternatively any rate reductions must be retroactive to that nine-month deadline The nine-month deadline and retroactivity provisions of 66 Pa. C.S. § 1309(b) apply "only when 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(b). Because the Commission cannot mandate net reductions in gross intrastate operating revenue as a result of AT&T's complaint due to the application of Section 3017(a), but may only order access reductions on a revenue-neutral basis, "the requested reduction in rates" does not "amount[] to in excess of 3% of the total gross annual intrastate operating revenues of" any of the RLEC defendants. As a result, the nine-month deadline and retroactivity provisions of Section 1309(b) do not apply.

However, given the serious consumer harms from allowing the RLECs to maintain access rates so far above the level charged by other carriers, the Commission should act promptly to reduce the RLECs' access rates and rebalance that revenue on a going forward basis.

## B. Compliance

This Commission must decide the general parameters of the rate rebalancing based on the record assembled. However, by the time the Commission's decision is ready to be implemented, the line counts and access minute volume information assumed in the parties' testimony will have changed. Therefore, the Commission should require each RLEC to submit a compliance filing within a specified time after the Commission's order, subject to comment, under the following assumptions:

1. Assume that access rates must be reduced to a benchmark equivalent to the Verizon PA access rate on a per-minute-of-use basis, which is currently about 1.7 cents.

2. Assume that the revenue from the reduced access rates will be rebalanced to retail rates for noncompetitive services. Each RLEC should have the flexibility to distribute the revenue among rates so long as the total amount of revenue needed to rebalance the access decrease is either accounted for in retail rates or the revenue is voluntarily foregone by the RLEC or banked for future use consistent with the terms of its alternative regulation plan.

3. If it is not possible to rebalance all of the particular RLEC's revenues by allocating the increases evenly to residential and business rates without having the residential rates exceed $23, then business rates must be increased in a greater proportion to residential rates until they reach the national average of $36.59, and reasonable consideration must also be given to additional increases to other noncompetitive rates, before the RLEC may proceed to step 4 below.[79]

4. If the RLEC is not able to rebalance all of the necessary revenue following steps 1 through 3 above, then the RLEC may complete the rebalancing by phasing in the additional access decreases and rate increases with a $1 per year increase to monthly basic residential and business rates, with corresponding decreases to access rates over time.[80]

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[79] If a particular RLEC's current retail rates are very low the Commission certainly has the discretion to phase-in the access decreases and rate increases even before the residential rates reach $23 to avoid rate shock to end users. However, the phase-in period should be made as expeditious as possible.

[80] Alternatively, some additional access reductions could be made immediately and the $8.4 million in excess funds in the current USF redirected to these specific RLECs on an interim basis to replace the revenue while they increase their retail rates by $1 per year over time as described in step 4, above. Distributions from the $8.4 million are reduced as retail rates are increased, until there are no more USF distributions.

5. Under no circumstances will the current USF be increased to serve as a source of revenue to off-set RLEC access rate decreases.

6. Each RLEC must submit compliance filings complying with the above parameters within 30 days of order entry (including all work-papers in their native format and all underlying assumptions, filed on a proprietary basis as needed).

7. The Commission will establish a comments and reply comments period, which may include the opportunity for an informal meeting to discuss the compliance filings prior to the submission of written comments. However, the comment cycle must be closed within 45 days of the compliance filing.

## VIII. CONCLUSION

For the foregoing reasons, the Commission should reduce the RLECs' intrastate access rate and rebalance the revenue to retail rates, as described above, but should reject any proposals to increase the current USF for purposes of funding the rebalancing.

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Dated: May 13, 2010


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**Appendix A**
**To Main Brief of**
**Verizon Companies**

**PENNSYLVANIA**
**PUBLIC UTILITY COMMISSION**

| | | |
|---|---|---|
| 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<br>Complainant<br><br>v.<br><br>Armstrong Telephone Company - Pennsylvania, et al.<br>Respondents | : | Docket No. C-2009-2098380, et al. |

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**VERIZON'S PROPOSED FINDINGS OF FACT,**
**CONCLUSIONS OF LAW AND ORDERING PARAGRAPHS**

Verizon Pennsylvania Inc., Verizon North Inc., Bell Atlantic Communications, Inc. d/b/a Verizon Long Distance, MCImetro Access Transmission Services, LLC d/b/a Verizon Access Transmission Services and MCI Communications Services Inc. (collectively "Verizon") propose the following findings of fact, conclusions of law and ordering paragraphs in the above-captioned proceeding.

**Findings of Fact**

1. The Rural Incumbent Local Exchange Carriers ("RLECs") whose switched access rates are the subject of this proceeding are (1) The United Telephone Company of Pennsylvania LLC d/b/a CenturyLink ("CenturyLink"), and the following companies represented by the Pennsylvania Telephone Association ("PTA"): (2) Armstrong Telephone Company – Pennsylvania, (3) Armstrong Telephone Company -- North, (4) Bentleyville Telephone Company, (5) Buffalo Valley Telephone Company, (6) Citizens Telephone

Company of Kecksburg, (7) Frontier Communications Commonwealth Telephone Company, LLC (d/b/a Frontier Commonwealth), (8) Frontier Communications of Breezewood, LLC, (9) Frontier Communications of Canton, LLC, (10) Frontier Communications of Canton, LLC, (11) Frontier Communications – Lakewood, LLC, (12) Frontier Communications – Oswayo River, LLC,(13) Frontier Communications of PA, LLC, (14) Conestoga Telephone & Telegraph Company, (15) D&E Telephone Company, (16) Hickory Telephone Company, (17) Ironton Telephone Company, (18) Lackawaxen Telecommunications Services, (19) Laurel Highland Telephone Company, (20) Mahanoy & Mahantango Telephone Company, (21) Marianna & Scenery Hill Telephone Company, (22) The North-Eastern Pennsylvania Telephone Company, (23) North Penn Telephone Company, (24) Consolidated Communications of Pennsylvania Company (f/k/a North Pittsburgh Telephone Company), (25) Palmerton Telephone Company, (26) Pennsylvania Telephone Company, (27) Pymatuning Independent Telephone Company, (28) South Canaan Telephone Company, (29) Sugar Valley Telephone Company, (30) Venus Telephone Corporation, (31) Windstream Pennsylvania, LLC f/k/a ALLTEL Pennsylvania, Inc., and (32) Yukon-Waltz Telephone Company.

2. Each of the RLECs is an "incumbent local exchange telecommunications company" as defined by 66 Pa. C.S. §§ 3012 and 3017.

3. Taken together, the RLECs serve approximately one million access lines in Pennsylvania (based on year-end 2007 data as reported to the Commission). Each individual RLEC is a separate company with its own individual tariffs and rates. They vary in size and in corporate affiliation. (Verizon St. 1.0 (Price Direct) at 4-5).

4. The majority of the RLECs, including all the larger ones, have chosen to be governed under the alternative form of regulation authorized by Chapter 30 of the Public Utility Code. Some of the RLECs operate under a Simplified Ratemaking Plan, where their allowable rates are determined by their return on common equity. (Verizon St. 1.1 (Price Rebuttal) at 6) (citing Phase I, Laffey Direct, 12/10/08, at 18).

5. Switched access is a protected service and a non-competitive service within the meaning of Chapter 30. (Verizon St. 1.1 (Price Rebuttal) at 7-8).

6. Switched access is a service provided by local exchange carriers to other carriers for originating or terminating interexchange or "toll" calls. Interstate access charges apply to calls that originate and terminate in different states, and intrastate access charges apply to calls that originate and terminate in different local calling areas within the same state. The Federal Communications Commission oversees interstate access rates, and the states oversee intrastate access rates. (Verizon St. 1.0 (Price Direct) at 6).

7. The average-rate-per-minute that each RLEC charges for intrastate switched access is depicted in tables one and two from Verizon's rebuttal testimony. The RLECs' weighted average rate per minute for intrastate switched access is over 5 cents – which is more than 300% higher than the 1.7 cents per minute charged by Verizon PA for the same service. Some of the RLECs are charging more than 10 cents a minute for the same service. (Verizon St. 1.1 (Price Rebuttal) at 10-11; Verizon St. 1.0 (Price Direct) at 19).

8. The following carriers' average intrastate switched access rate per minute is already approximately equal to or below Verizon PA's current rates: Armstrong North, Frontier Breezewood, Frontier Canton, Frontier Lakewood and Frontier PA. (Verizon St. 1.1 (Price Rebuttal) at 10).

9. Competitive carriers operating in Verizon territory are prohibited by statute from charging rates higher than Verizon's rates and therefore generally charge 1.7 cents per minute or less. *See* 66 Pa. C.S. § 3017(c). (Verizon St. 1.0 (Price Direct) at 4).

10. With the exception of the five companies listed in paragraph 8, above, the RLECs' intrastate switched access rates are disproportionately higher than those of most of the other local exchange carriers operating in Pennsylvania. (Verizon St. 1.1 (Price Rebuttal) at 10-11).

11. Much of the disparity between the RLECs' switched access rates and those of other carriers on an average rate per minute basis is driven by the fact that many of them still impose a large monthly carrier charge or "CCLC" on a per-access line basis, ranging from $4.04 to as high as $17.99 per line, per month. (Verizon St. 1.0 (Price Direct) at 14). The average PTA company CCLC is $5.87 per line. CenturyLink's CCLC is $7.19 per line, per month. (Verizon St. 1.1. (Price Rebuttal) at 11). These specific carrier charges for each RLEC can be found in the individual carriers' tariff sheets attached as Exhibit 3 to Verizon's Statement 1.0. Verizon's current CCLC is 58 cents per line per month. (*Id.*)

12. The CCLC is an access rate element created when intrastate switched access rates were first developed in the mid-1980s and was originally designed to recover a portion of the fixed costs of providing local loops to the ILEC's own end users, in order to keep end user rates artificially low. Because these fixed costs are not related to the switching and transport functions used to provide long-distance carriers with access to a LEC's network, an excessively high CCLC serves as a vehicle to transfer to the LEC's access customers the LEC's fixed costs of providing local exchange service to its own retail customers. (Verizon St. 1.0. (Price Direct) at 13).

13. Some of the RLECs still charge a "transport interconnection charge" or "TIC," also sometimes called the "residual interconnection charge" or "RIC," which is another per-minute rate element that is not directly related to providing switched access services and instead was created in the past to subsidize overall operating costs. The Verizon ILECs do not charge a TIC or RIC, and the majority of the RLECs have set these rate elements at $0 in their tariffs. (Verizon St. 1.0. (Price Direct) at 14-15). The specific TIC or RIC rates can be found in the individual carriers' tariff sheets attached as Exhibit 3 to Verizon's Statement 1.0.

14. Although they had the opportunity to do so in this proceeding, none of the RLECs submitted a cost study to justify their current access rates.

15. Continuing to permit the RLECs to charge access rates so far in excess of what other Pennsylvania carriers charge for the same switched access service is harmful to consumers and to competition. The RLECs' high access charges are harmful to consumers because of their impact on the customers of carriers that must pay those excessive access rates. The RLECs' high access charges harm consumers in the RLECs' territories because they diminish competitive options. (Verizon St. 1.1 (Price Rebuttal) at 13-16).

16. Requiring carriers to pay the RLECs' high rates for switched access is harmful to the carrier ratepayers that are the RLECs' customers for switched access service. (Verizon St. 1.1 (Price Rebuttal) at 13-16).

17. Reducing RLEC intrastate switched access rates to be more in line with the rates of Verizon and other carriers will have substantial public benefits. (Verizon St. 1.1 (Price Rebuttal) at 13-16).

18. Having all RLECs reduce their intrastate switched access rates to the benchmark at the level of 1.7 cents per minute, based on Verizon PA's rates for the same service, will promote equity and competitive parity and reduce market distortions by prompting carriers with the highest access rates to recover more of their network costs from their own customers, rather than from other carriers and their customers through access rates. (Verizon St. 1.0 (Price Direct) at 17-19).

19. To reduce the RLECs' access rates on a revenue-neutral basis, the RLECs may increase rates for other noncompetitive services in a manner calculated to increase the revenue from those rates to recapture the revenue removed from access rates, or the RLECs may choose voluntarily to forego those increases.

20. While there is no legal basis to impose a "comparability" restriction on the RLECs' rates for stand alone basic residential service (see conclusions of law, below), even if there were some legal basis to do so the record shows that the RLECs could increase their rates as high as $25 and still charge rates reasonably comparable to Verizon's urban rates. (Verizon Main Br. at 32; Phase I, Verizon St. 1.1 (Price Rebuttal) at 34-35).

21. The record shows that an affordable RLEC rate would range from $23 to $34. There is no record evidence regarding affordability to support limiting RLEC rates below $23. (Verizon Main Br. at 32-34; Tr. at 508).

22. The record does not support limiting RLEC residential rates (exclusive of taxes and fees) to $17.09, as advocated by the OCA or to $18.94, as advocated by the PTA. (Verizon Main Br. at 32-34; Tr. at 508).

23. The record does not support any limitation on RLEC business rate increases. (Verizon Main Br. at 34-36).

24. The national average single line business rate was $36.59 in 2007. This 2007 national average is $10 higher than CenturyLink's business rate of $26.23 and higher than many of the other RLECs' business rates. (Verizon St. 1.1 (Price Rebuttal) at 38). Each RLEC's current business rate is depicted in AT&T's Attachment 5 to the Panel Rebuttal Testimony.

25. Because of their flawed assumptions that RLEC residential rates must be capped at insupportably low levels, and their presumption that business rate increases must be kept equal to residential increases, the other parties' rate rebalancing calculations are flawed. With a more flexible rate design, the individual RLECs can be expected to rebalance more revenue to retail rates then the RLECs, the OCA or AT&T have depicted in the worksheets attached to their testimony.

26. Replacing revenue from the RLECs' switched access rates with revenue from other carriers through an expansion of the USF would dramatically increase the funding burden on the Verizon ILECs. (Verizon St. 1.2 (Price Surrebuttal) at 11-12).

27. OCA's proposal to transfer $63 million in revenue from switched access rates to the USF would result in a net increase in the Verizon ILECs' funding burden to the RLECs of nearly $27 million. (Verizon Main Br. at 47).

28. The Verizon ILECs operate in markets that are even more competitive than the RLECs' territory. Since 1999, through 2009, the Verizon ILECs have experienced significant line losses. The proprietary percentages are set forth in Verizon St. 1.1 (Price Rebuttal) at 19.

29. It is no longer supportable in today's market to expect Verizon and its customers to support the RLECs' operations through switched access charges and/or

through the state USF. Depriving the Verizon ILECs of revenues needed to operate their own business is not only harmful to the companies but also to customers. (Verizon Main Br. at 47-51).

30. Replacing the RLECs' switched access revenue with funds from an expanded USF would recreate the exact same problems with adverse customer impacts and harm to competition that is inherent in the RLECs' excessive switched access rates, albeit through a slightly different mechanism. Also because the USF contributions are calculated based on the carriers' intrastate revenue, communications companies that might otherwise have chosen to invest in Pennsylvania could choose to take their business elsewhere, leaving Pennsylvanians in general with fewer competitive options. (Verizon St. 1.1 (Price Rebuttal) at 48-49).

31. There is no benefit to be gained by expanding the USF on a temporary basis for purposes of transitioning the RLECs rates. If a transition period is needed, then the RLECs' rate rebalancing can be phased-in over time. (Verizon St. 1.2 (Price Surrebuttal) at 9-10).

32. The current USF contains approximately $8.4 million in excess funds that are today providing a windfall to the RLECs. (Verizon St. 1.1 (Price Rebuttal) at 47; Verizon St. 1.2 (Price Surrebuttal) at 15).

**Conclusions of Law**

33. The RLECs' have the burden of proof in this proceeding. 66 Pa. C.S. § 315(a); *AT&T Communications of Pennsylvania, Inc. v. Verizon North Inc.*, C-20027195 (Opinion and Order entered January 8, 2006) at 20-21.

34. The RLECs have failed to meet their burden of proving that their intrastate switched access rates are just and reasonable.

35. The Commission retains the authority to ensure that rates for individual noncompetitive services remain just and reasonable. *Buffalo Valley Tel. Co. v. PUC*, 990 A.2d 67, slip op. at 21; 66 Pa. C.S. §§ 1301, 3015(g).

36. Chapter 30 "expressly preserves the Commission's authority and responsibility to protect all ratepayers," and "[t]his protection extends to services provided to other telephone carriers, i.e., 'ratepayers,' for Petitioners' switched access service." *Buffalo Valley Tel. Co. v. Pa. PUC*, 990 A.2d 67 (Pa. Commw. Ct. 2009), slip op. at 20.

37. The Commission may consider the fact that the RLECs' switched access rates are higher than the rates charged by many other carriers in the industry for the exact same service as a basis to conclude that the rates are not just and reasonable. *Mobilfone of Northeastern Pennsylvania, Inc. v. PUC*, 78 Pa. Commw. 336, 467 A.2d 902 (1983).

38. The current switched access rates of the RLECs other than those listed in paragraph 8, above, are not just and reasonable and must be reduced.

39. Under 66 Pa. C.S. § 3017(a) the Commission has the authority to rebalance revenue by decreasing switched access rates and "making revenue neutral increases to other noncompetitive rates." *Buffalo Valley Tel. Co. v. Pa. PUC*, 990 A.2d 67 (Pa. Commw. Ct. 2009), slip op. at 20.

40. The revenue neutrality requirement of 66 Pa. C.S. § 3017(a) cannot be satisfied by requiring the RLECs to recover the lost revenue from competitive or unregulated services. The only reasonable reading of Section 3017(a) in the context of Chapter 30's scheme of alternative regulation is that the RLEC must be given the

opportunity to rebalance revenue to other regulated rates within the noncompetitive basket of services, as this would keep the rate changes revenue neutral within the set of those services for which the Commission has authority to regulate rates.

41. The revenue neutrality requirement of 66 Pa. C.S. § 3017(a) cannot be satisfied by requiring other carriers to divert revenue from their own operations to subsidize the RLECs through an expanded USF.

42. There is no legal basis to impose a "comparability" restriction on the RLECs' rates.

43. Federal law regarding universal service appears at 47 U.S.C. § 254. Section 254(b)(3) is not a mandate to state commissions constraining the level of intrastate retail rates. *Buffalo Valley Tel. Co. v. PUC*, No. 847 C.D. 2008 (Commw. Ct., December 15, 2009), slip op. at 34.

44. Preservation or protection of the RLECs' revenues and profits should not be confused with achievement of universal service goals. Universal service refers to the ability of end-users to obtain reasonably-priced telecommunications services. ILECs can be protected in many ways that will not benefit consumers, and conversely consumers can be helped in many ways that will not benefit carriers. (Colwell 7/23/09 RD, Conclusion of Law #7).

45. Chapter 30 does not expressly authorize the use of revenues from other carriers through a state USF to rebalance access revenue.

46. Chapter 30 preserves the Commission's authority "to ensure the protection of customers" but any "such additional requirements" must be "consistent with this chapter." 66 Pa. C.S. § 3019(b)(3) (emphasis added). Requiring other carriers to transfer

their own revenues to the RLECs to fund switched access rate reductions is not "necessary to ensure the protection of customers" and is not "consistent with this chapter."

47. The Commission promulgated regulations regarding the administration of the PA USF. 52 Pa. Code §§ 63.161-171. The current USF cannot be expanded in terms of the size of the fund or the contributing base without a rulemaking to alter these regulations.

48. The Commission has ruled that "[e]xamination of whether wireless carriers and VoIP service providers should be contributors to the PaUSF" is not a proper issue to be raised in this phase of the investigation. (12/10/09 Order at 24).

49. The nine-month deadline and retroactivity provisions of Section 1309(b) do not apply in this case.

**Ordering Paragraphs**

50. AT&T's complaints are granted in part, consistent with this order and the following ordering paragraphs.

51. Each RLEC must reduce its intrastate switched access rates and may rebalance that revenue to rates for other noncompetitive services as set forth in this opinion and order.

52. Within thirty (30) days of the effective date of the Commission's order, each of the RLECs must submit to the Commission and serve on all parties a separate compliance filing (including all work-papers in their native format and all underlying assumptions) under the following assumptions:

a. Access rates must be reduced to a benchmark equivalent to the Verizon PA switched access rate on a per-minute-of-use basis, which is currently about 1.7 cents.

b. The revenue from the reduced access rates may be rebalanced to retail rates for other noncompetitive services. The revenue may be allocated among noncompetitive rates at the RLEC's discretion, so long as the total amount of revenue needed to rebalance the access decrease is either accounted for in retail rates or the revenue is voluntarily foregone by the RLEC. The RLEC may also propose to bank the potential increase for future use in retail rate increases, consistent with its alternative regulation plan.

c. If it is not possible to rebalance all of the particular RLEC's revenues by allocating the increases evenly to residential and business rates without having the residential rates exceed $23, then business rates must be increased in a greater proportion to residential rates until they reach the national average of $36.59, and reasonable consideration must also be given to additional increases to other noncompetitive rates, before the RLEC may proceed to step "d" below.

d. If the RLEC is not able to rebalance all of the necessary revenue following steps "a" through "c" above, then the RLEC may complete the rebalancing by phasing in the additional access decreases and rate increases with a $1 per year increase to monthly basic residential and business rates, with corresponding decreases to access rates over time. Alternatively, the RLECs may propose to redirect the $8.4 million in excess funds in the current USF to the specific RLECs that need additional time to complete rebalancing, on an interim basis to replace the revenue while they increase their retail rates by $1 per year over time as described above. Distributions from the $8.4 million will be reduced as retail rates are increased, until there are no more USF distributions.

49. The USF will not be increased to serve as a source of revenue to off-set RLEC switched access rate decreases.

50. The Commission will establish a comment and reply comment period following the compliance filings, which may include the opportunity for an informal meeting to discuss the compliance filings prior to the submission of written comments. However, the comment cycle must be closed within 45 days of the compliance filing.

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**CERTIFICATE OF SERVICE**

I hereby certify that I have this day served a copy of the Verizon companies' Main Brief, upon the participants listed below in accordance with the requirements of 52 Pa. Code Section 1.54 (related to service by a participant) and 1.55 (related to service upon attorneys).

Dated at Philadelphia, Pennsylvania, this 13th day of May, 2010.

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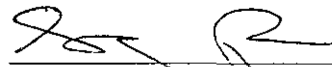

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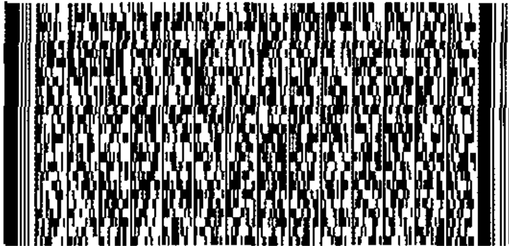

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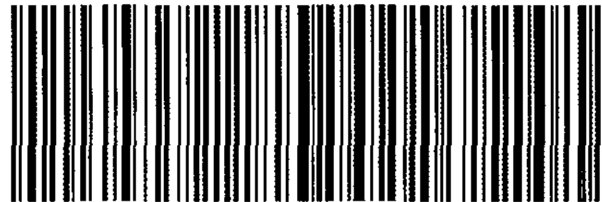

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