BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Re:	FCC Intercarrier Compensation - Workshop and Solicitation of Comments on the Missoula Plan	)))	Docket No. M-00061972

<u>REPLY COMMENTS OF VERIZON AND VERIZON WIRELESS</u>

INTRODUCTION

In response to the invitation issued at the close of the Commission-sponsored September 11, 2006 workshop concerning the Missoula Plan**,** Verizon[1] and Verizon Wireless (hereinafter "Verizon") provide the following comments in reply to certain comments and presentations made at the Workshop.

As Verizon's initial comments and its presentation at the Workshop made clear, if this Commission chooses to file comments with the Federal Communications Commission ("FCC") on the Missoula Plan, then it should oppose that Plan, which is merely a minority-supported and flawed starting point in an evolving proceeding at the FCC. The Plan's proponents may suggest tweaks to the Plan in a feigned effort to address the concerns raised at the Workshop, but these minor changes cannot remedy the fundamental defects in this proposal. The Commission should not be led astray. It was quite clear at the Workshop that the majority of the industry opposes the Missoula Plan. The Commission heard about the Missoula Plan's myriad flaws not only from Verizon, but from the Office of Consumer Advocate, numerous CLECs, and the cable industry. Verizon cannot recall the last time it stood united with these varied segments of the industry on any issue – which is perhaps the most compelling evidence that the Missoula Plan is not the right

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[1] "Verizon" includes ILECs Verizon Pennsylvania Inc. and Verizon North Inc., CLEC MCImetro Access Transmission Services, LLC d/b/a Verizon Access Transmission Services, and IXCs MCI Communications Services Inc., and Verizon Select Services Inc.

answer and that its fundamental problems cannot be fixed with mere adjustments around the edges.

Among the numerous concerns raised with the Missoula Plan, Verizon emphasizes the following points as the principal reasons why any comments this Commission files with the FCC should oppose the adoption of the Missoula Plan and why the Plan should not be relied upon in Pennsylvania for any purpose.

1) The Plan is not competitively neutral, because it unduly favors rural carriers at the expense of the rest of the industry.

2) The Plan is complex: it creates different rules for different groups of carriers; it establishes a series of option elections that could potentially drive further disparities among carriers, even those within the same Track; it would gut the terms of virtually all of Verizon's interconnection agreements with other carriers in Pennsylvania; and it would act as a disincentive for the continuation of existing EAS arrangements.

3) The Plan reduces rates (and revenues) for large companies. Yet rates for mid-sized and small carriers (Tracks 2 and 3) remain significantly higher for years. For large companies, this means that Track 1 carriers give up their own revenue, yet continue to pay substantial amounts in access charges and reciprocal compensation to smaller carriers, and then presumably pay even more to the newly-created Restructure Mechanism("RM"), thus leaving their customers to subsidize to even more heavily service to customers of small carriers.

4) The Plan would actually allow rate disparities to *increase* over time. While the Plan sets specific rate targets for carriers in Tracks 1 and 2, it does not do so for Track 3. It would continue to set interstate access rates for Track 3 based on their interstate revenue requirement. In most cases, these rates would be automatically retargeted to achieve that rate of return each year by NECA when it makes its annual filing with the FCC. The plan would also link intrastate access charges to interstate rates, and hence to this rate-setting mechanism. The default rates for local traffic terminated to Track 3 carriers would also be tied to these rates. In future years, as the interstate revenue requirement increases, and interstate access minutes decline, it is reasonable to expect that the interstate access rates of Track 3 carriers will increase – and with it the other rates in the system that are tied to the interstate rates. There is nothing in the Missoula Plan to check these increases. Thus, while other players are reducing their rates under Missoula, Track 3 carriers would actually be raising their rates over time.

5) The Plan ignores competitive reality. Large companies in Track 1 are expected to raise their subscriber line charges ("SLCs") by $3.50, which they likely will be unable to do in the competitive markets they serve. Yet Track 2 and 3 companies, many of whom operate in less competitive markets, are only asked to raise their SLCs by $2.25. The

resulting shortfall will then be paid for by Track 1 customers, through their contributions to the RM.

6) The Plan reduces the ability of Track 1 carriers to invest in infrastructure for their customers. Because the SLC increases in Track 1 areas are not likely to be sustainable in the market, the plan does not provide an adequate opportunity for Track 1 carriers to recover the revenue given up in access. It is one thing if market forces take revenue away from a particular carrier – for example, Verizon is losing lines and minutes in its ordinary wireline telephone business, and is working hard to develop new networks and new services to replace those revenues. But the Commission should not endorse a regulatory policy – the Missoula Plan – that artificially reduces revenues without any reasonable prospect for recovering them. By interfering in the natural development of the marketplace through this abrupt and artificial elimination of capital, this plan could undermine the market transition to new networks and services that will be the real source of benefits for consumers in Pennsylvania in the years ahead.

7) The Plan balloons the universal service fund with no indication of increased need. The RM would add at least $2.2 billion dollars to the federal universal service mechanisms, even according to the estimates provided by the Missoula proponents. Proposals to "retarget" the existing high cost fund account for hundreds of millions of dollars, and yet are completely unrelated to the rate rebalancing in the Missoula Plan. Those proposals are included only to satisfy certain ILECs among the Plan's supporters. As recently noted by Commissioner Boyle of Nebraska, the proposed "early adopter" fund will clearly be larger than the $200 million estimated by the Missoula Plan supporters. If her estimates are correct, the total new funding would be $4 billion, and the total funding for all federal mechanisms would be $11 billion. Increases of this magnitude would threaten the sustainability of the fund. And, since Pennsylvania is already one of the largest net contributors to the federal USF, it is reasonable to expect that adoption of these new mechanisms under Missoula would further add to the drain of resources from ratepayers in Pennsylvania.

8) The Plan's effects on state jurisdiction are unclear. The Plan provisions designating what aspects of state participation are optional and what are mandatory appear to combine the worst of both worlds. Part of the Plan is preemptive, so the FCC will likely be forced to defend the Plan in court. Part of the Plan is optional, which means some risk that not all states will join, thereby undermining the goal of uniformity in intercarrier compensation reform.

9) The Plan incents wasteful network re-arrangements. By moving the "edge" from the end office to the tandem, the Plan creates incentives for large scale network rearrangements. Carriers that already have direct trunking to the end office will be given an incentive to drop those arrangements and go to the tandem instead. While the Plan discusses possible compensation from the edge owner to parties who keep direct trunking in place, either party can decide to rearrange the facilities instead. Verizon would then face either a significant new compensation expense (for those trunks that were retained) or significant rearrangement cost (if they are rearranged). Moreover, the network architecture rules in the Plan are likely to create additional arbitrage opportunities.

10) The Plan complicates existing ILEC to ILEC arrangements. Most local traffic between ILECs is exchanged today on a bill-and-keep basis, and is not measured. The Plan would allow Track 2 carriers to charge reciprocal compensation, even on traffic that is EAS today. It also would create an incentive for Track 3 carriers not to renew EAS agreements, since they would then be able to charge their interstate access rates for that traffic. This could create a major new reciprocal compensation expense, undermine EAS arrangements that benefit customers today, and require Track 1 carriers to measure large amounts of traffic that are not measured now.

11) The Plan preserves and expands existing inefficiencies. Because the Plan does not unify rates, carriers will still require some mechanism for distinguishing between local and long distance calls. The mechanism proposed in the Plan is based entirely on the telephone numbers of the calling and called parties, and the assignment of those numbers to ILEC wire centers. This proposal raises major concerns:

- It effectively endorses virtual NXX, which will allow carriers using virtual NXX to evade paying the appropriate level of intercarrier compensation.

- It would require large investments in system changes, especially for wireless carriers. Today, whether a wireless call is considered local or long distance depends on the physical location of the customer, and the systems of wireless networks are designed on that basis. Changing to a system where physical location does not matter, and the numbers alone determine the classification of the call, would require new recording and billing systems to be developed.

CONCLUSION

For the reasons stated in Verizon's Comments, in its oral Workshop presentation and in these Reply Comments, the Commission should not endorse the Missoula Plan. To the extent the Commission wants to focus on access charge reform, it should address rural ILEC access charges, which are far in excess of those charged by Verizon and other Track 1 carriers, and should otherwise await the outcome of the FCC's intercarrier compensation proceeding before taking any additional actions.

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