

STATE OF IOWA
DEPARTMENT OF COMMERCE
UTILITIES BOARD

IN RE: IOWA TELECOMMUNICATIONS ASSOCIATION	DOCKET NOS. TF-07-125 TF-07-139
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FINAL ORDER

(Issued May 30, 2008)

PROCEDURAL HISTORY

On June 29, 2007, the Iowa Telecommunications Association (ITA) filed proposed changes to its Access Service Tariff No. 1 (ITA No. 1), identified as TF-07-125. ITA stated that the proposed changes mirror changes in the National Exchange Carrier Association (NECA) tariff (identified as NECA No. 5), which is the interstate access service tariff used by Iowa local exchange companies that also concur in the intrastate ITA No. 1. One of the proposed changes involved an increase in certain switched access charges by 16.8 percent.

On July 16, 2007, Sprint Communications Company L.P. (Sprint) and MCImetro Access Transmission Services, LLC, d/b/a Verizon Access Transmission Services, and MCI Communications Services, Inc., d/b/a Verizon Business Services (collectively referred to as Verizon), filed separate motions to accept their late-filed resistances to ITA No. 1 and to the proposed tariff changes. In support of their resistances, Sprint and Verizon argued that the Board should not approve the significant increase in access rates without a review of Iowa's access charge regime.

Sprint and Verizon asked the Board to order ITA to set and keep its intrastate switched access rates, specifically the Transport Interconnection Charge (TIC), the Carrier Common Line Charge (CCLC), and the local switching rate, at parity with the interstate switched access rates in NECA No. 5.

On July 30, 2007, the Board issued an order granting Sprint's and Verizon's motions to accept their late-filed resistances. The Board also suspended ITA's proposed tariff changes and requested that ITA file a response to the resistances on or before August 3, 2007.

On August 3, 2007, ITA filed its response. ITA stated that Sprint's and Verizon's objections did not support suspension or investigation of the proposed tariff. ITA asserted that the terms of the tariff mirror the provisions of NECA No. 5 and that when changes are made to NECA No. 5 with the Federal Communications Commission (FCC), the same changes are filed for approval with the Board. ITA stated that the FCC approved the proposed revisions to NECA No. 5 on June 28, 2007.

On August 7, 2007, Sprint and Verizon filed objections to a tariff revision identified as TF-07-139, which was filed by ITA on July 25, 2007. ITA stated that TF-07-139 included revisions that relate to changes made in the NECA interstate access services tariff and the NECA Access Handbook, which was also approved by the FCC. Sprint and Verizon asked that the Board consolidate these objections into the Board's review of TF-07-125 because some of the same issues were in dispute.

ITA filed a resistance to the objections on August 15, 2007, and the Board consolidated the two proceedings by order issued September 14, 2007.

On August 9, 2007, Sprint and Verizon filed replies in support of their objections. Sprint and Verizon asserted that while the FCC approved NECA No. 5 for purposes of interstate traffic, the Board should take different, local considerations into account when reviewing ITA No. 1 for purposes of intrastate traffic.

On August 30, 2007, the Board issued an order allowing ITA's proposed tariff to become effective while the Board further investigated the proposed tariff changes. As part of that order, the Board identified two prior Board rulings that raised questions regarding the extent of the Board's jurisdiction over the appropriateness of intrastate access charges.¹ The Board sought briefs from Sprint, Verizon, ITA, and any other interested persons regarding the extent of the Board's jurisdiction to approve or deny the proposed increase and the reasons the Board may do so.

On September 21, 2007, Sprint, Verizon, and ITA filed initial briefs. All of the parties agreed that the Board has the appropriate jurisdiction to review the proposed rate changes in ITA No. 1, even though they did not rely on the same arguments to reach that conclusion.

¹ See *In re: Fibercomm, L.C., et al. vs. AT&T Communications of the Midwest, Inc.*, "Final Decision and Order," Docket No. FCU-00-3, pp 15-17 (issued October 25, 2001) (hereafter referred to as *Fibercomm*) (The Board determined that it has limited jurisdiction over the access service rates of competitive local exchange carriers (CLECs) to the extent that it finds, after notice and opportunity for hearing, that those CLECs have market power in the relevant markets. This jurisdiction is limited to CLECs pursuant to the terms of Iowa Code § 476.101(1)); See also *In re: Interstate 35 Telephone Company, d/b/a Interstate Communications*, "Declaratory Order," Docket No. DRU-02-4, p. 3 (issued October 18, 2002) (hereafter referred to as *Interstate 35*) (The Board determined that Iowa Code § 476.1 left the Board without jurisdiction over the access rates of incumbent local exchange carriers (ILECs) that are not subject to rate regulation).

On October 5, 2007, Sprint, Verizon, and ITA filed reply briefs generally restating their previous arguments. Also on October 5, 2007, AT&T Communications of the Midwest, Inc., and TCG Omaha (collectively AT&T) filed a response to the initial briefs filed by Sprint, Verizon, and ITA. AT&T stated that it agreed with the analysis provided by Sprint and Verizon advocating the Board's jurisdiction over the access rates of local exchange carriers (LECs) that are not subject to retail rate regulation.²

On November 15, 2007, the Board issued an order setting a procedural schedule for this docket. The Board also determined that it had jurisdiction over written complaints regarding the terms and conditions for the exchange of toll communications, including access charges, pursuant to Iowa Code § 476.11. In addition, the November 15 order reversed the declaratory ruling issued by the Board on October 18, 2002, in the *Interstate 35* docket.

Pursuant to the procedural schedule established and amended in this proceeding, ITA filed its prepared direct testimony, with supporting exhibits and workpapers, on December 21, 2007. Sprint, Verizon, and AT&T filed rebuttal testimony on January 28, 2008, and ITA filed its reply testimony on February 18, 2008.

² The Board notes that on September 21, 2007, the Rural Iowa Independent Telephone Association (RIITA) filed a statement with the Board supporting the questions raised in the August 30, 2007, order, but stating that RIITA could not meaningfully participate by filing a brief pursuant to the established briefing schedule. RIITA did not file a reply brief on the jurisdiction question. RIITA did, however, file a post-hearing brief on April 25, 2008.

A hearing to receive all pre-filed testimony and allow for the cross-examination of all witnesses was held on April 1 and 2, 2008.

Briefs were filed by ITA, Sprint, Verizon, AT&T, RIITA, and the Consumer Advocate Division of the Department of Justice (Consumer Advocate) on April 25, 2008.

DISCUSSION

ITA No. 1 has five basic rate elements that comprise the overall ITA switched access rate that is at issue in this proceeding. These elements are 1) Transport, 2) Local Switching, 3) Information Charge, 4) Transport Interconnection Charge (TIC), and 5) Carrier Common Line Charge (CCLC). The transport charge and the information charge in ITA No. 1 currently mirror the corresponding charges found in NECA No. 5 and are not contested in this proceeding. However, Sprint, Verizon, and AT&T assert that the other three rate elements, the TIC, Local Switching charge, and the CCLC, are in excess of the cost to provide access services and therefore contain subsidies that are equal to the difference between the corresponding rates in NECA No. 5 and ITA No. 1. Sprint, Verizon, and AT&T ask the Board to order ITA to set and keep the TIC, Local Switching charge, and the CCLC at parity with the rates in NECA No. 5. The parties' arguments regarding each of these rate elements will be discussed individually.

1. Transport Interconnection Charge (TIC)

A. Parties' positions

Sprint states that NECA No. 5 reflects a TIC rate value of \$0.000000, whereas in contrast, the TIC rate has been frozen in ITA No. 1 at a value of \$0.015055.

(Sprint Brief, p. 10). AT&T argues that the FCC has previously identified various rate elements in the TIC and moved several of these to different switched access rate elements including SS7 costs, tandem switching costs, multiplexers costs associated with the tandem switch, and actual minutes of use for tandem switched transport costs. (AT&T Brief, p. 13). AT&T points out that in 2001, the FCC concluded that the TIC increased the cost of competitive entry, which had an adverse effect on the development of competition.³ The TIC was removed from NECA No. 5 by the FCC. (AT&T Brief, p. 14).

AT&T and Sprint both assert that several of the LECs that concur in ITA No. 1 charge the interexchange carriers (IXCs) for transport interconnection service even though these LECs do not provide this service. AT&T, Sprint, and Verizon assert that this practice of billing for services not rendered is neither just nor reasonable. (AT&T Brief, pp. 19-20).

ITA argues that the use of surrogate rate elements and procedures, like the NECA process and tariffs, is a reasonable and cost-effective approach for the Board

³ *In the Matter of Multi-Assoc. Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, Federal-State Joint Board on Universal Service, Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers, "Second Report and Order and Further NPRM," FCC-01-304, CC Docket Nos. 00-256, 96-45, 98-77, 96-166, at ¶¶ 24, 73, 99 (Released November 8, 2001) (hereinafter MAG Order).*

to continue. (ITA Brief, p. 18). ITA asserts that the use of the NECA process and interstate access service rates as a surrogate for intrastate access service has enabled a low-cost, cost-based rate process for many years. (ITA Brief, p. 18; Tr. 296). ITA states that this reliance on a surrogate is a principle that has been in place for many years and should continue into the future. (ITA Brief, p. 18). ITA asserts that the measure of reasonableness is not based on the inputs, but rather on the outcome. (Id.) ITA claims that the revenues received from the access charges assessed in Iowa are reasonably comparable to the interstate cost recovery through the NECA No. 5 rates, plus the subscriber line charge (SLC) and universal service contributions, and thereby demonstrates that the current process is just and reasonable. (Tr. 448-49). RIITA supports ITA's position.

ITA acknowledges, however, that the TIC element proved more complicated to discuss in this proceeding because the change in the interstate TIC element was not simply a shift from access charges to other cost recovery methodologies, but rather was the result of a rate design shift by the FCC. (ITA Brief, p. 20). ITA notes that in 1998, ITA froze the intrastate TIC and local switching rates in response to these shifts by the FCC. (ITA Brief, pp. 9-10).

ITA states that the FCC determined that non-traffic sensitive costs should be recovered through fixed-rate SLCs or universal service subsidies. (ITA Brief, p. 22; Tr. 189). As a result, the FCC eliminated the TIC and replaced it with these other interstate cost recovery mechanisms. ITA stated, however, that it maintained a constancy in its intrastate cost recovery mechanism by freezing the TIC and local

switching charges in ITA No. 1, which allowed Iowa companies to recover the same intrastate access charges as they did prior to the FCC's actions.

B. Analysis

Based on the information provided during this proceeding, the Board finds that it is just and reasonable to direct ITA to remove the TIC from ITA No. 1 so that the charge is in parity with NECA No. 5. The TIC is associated with tandem switching services, which are services that are not performed by the majority of ITA members. (Tr. 480). Rather, Iowa Network Services (INS) provides these services on behalf of these LECs and then bills the IXCs for the services provided. (Id.). ITA did not identify any member LECs that offer this service. (Tr. 479-80). The Board finds that it is just and reasonable to eliminate a rate that has no corresponding service.

Moreover, ITA's argument regarding cost recovery is focused on the revenues, rather than the costs, associated with each jurisdiction. ITA did not present any evidence as to the costs of LECs that concur in the ITA tariff; rather, ITA states that no Iowa costs were used in the development of ITA No. 1. (Tr. 307). Therefore, the Board cannot assess the relationship between the costs and the revenues of these companies, nor can the Board determine whether those rates are just and reasonable from a cost standpoint. However, it stands to reason that the costs for a service that is not offered are likely to be zero, meaning that cost-based rates for that unoffered service should also be zero.

2. Local Switching Charge

A. Parties' positions

Sprint states that ITA No. 1 reflects a local switching rate of \$0.040400, whereas NECA No. 5 reflects eight local switching rate bands with the highest rate being \$0.024435. (Sprint Brief, p. 13). According to the FCC, local switching "connects subscriber lines both with other local subscriber lines and with interoffice dedicated and common trunks."⁴ This rate element is addressed to the costs of performing local switching for toll calls. (AT&T Brief, p. 15). In 1998, ITA froze its intrastate local switching service rates when the FCC and NECA reformed the interstate equivalent rates by removing the dial equipment minute (DEM) weighting mechanism from the rates.⁵

The DEM weighting mechanism was devised by the FCC on the premise that small telephone companies typically had higher local switching costs per line, as these companies were unable to realize economies of scale. (AT&T Brief, p. 15). The DEM weighting rules allowed the small companies to recover part of their local switching costs in the interstate jurisdiction. (*Id.*). In 1997, the FCC removed the weighting program from the rates and established the local switching support (LSS) mechanism in the federal Universal Service Fund (USF) to replace the DEM

⁴ *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges, "First Report and Order,"* FCC-97-15, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, at ¶¶ 210-11 (Released May 16, 1997) (hereinafter Access Reform Order).

⁵ *In the Matter of Federal-State Joint Board on Universal Service, Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End-User Common Line Charge, "Fourth Order on Reconsideration" CC Docket No. 96-45, "Report and Order" CC Docket Nos. 96-45, 96-262, 94-1, 91-213, 95-72, at ¶¶ 40-41 (Released December 30, 1997).*

weighting program. Sprint, Verizon, and AT&T claim that the LECs that concur in ITA No.1 are recovering local switching costs through the LSS mechanism, which amounts to approximately \$0.0183 per minute that is recovered through federal USF. (AT&T Brief, p. 15).

ITA asserts that when the DEM weighting mechanism was removed by the FCC in 1997, the FCC reassigned some of the non-traffic sensitive costs to other elements in NECA No. 5, namely flat-rated recovery mechanisms. (Tr. 186, 446). ITA states that three of those elements were reassigned to local switching, one to transport, and one to tandem switching. (ITA Brief, p. 20). ITA states that by freezing the local switching element in ITA No. 1 in 1998, the LECs concurring in ITA No. 1 avoided any intrastate impacts from the FCC's shifts in the interstate arena. (ITA Brief, p. 21). ITA asserts that the FCC reassigned the mechanisms where these costs would be recovered, but the costs to be recovered did not change. (ITA Brief, p. 21). ITA states that Sprint, Verizon, and AT&T have not demonstrated that the LECs concurring in ITA No. 1 are over-recovering their costs. (ITA Brief, p. 21).

B. Analysis

The Board finds that the local switching rate in ITA No. 1 should be unfrozen and set to mirror the corresponding NECA No. 5 rates. The original interstate local switching rate was intentionally increased through DEM weighting to provide additional revenue support to small companies. By freezing ITA No. 1 local switching element at the artificially high level in NECA No. 5 prior to 1997, ITA has perpetuated this subsidy on the intrastate level, even though the FCC has moved the interstate

subsidy to the USF system. There are no Board rules that address the rate for local switching and there are no rules that require the ITA rate be frozen at 1998 levels. (Tr. 48). Further, there is no showing in this record that the pre-1998 interstate subsidy is just and reasonable in the intrastate jurisdiction in 2008. Therefore, it is reasonable to require that ITA reduce its intrastate local switching rates to actually mirror the corresponding rates in NECA No. 5.

3. Carrier Common Line Charge (CCLC)

A. Parties' positions

The common line, or loop, connects a customer's home or business to the LEC's end office. The cost of the loop does not vary by usage.⁶ Sprint states that the Iowa intrastate CCLC is \$0.03 per minute of use, whereas the interstate CCLC is \$0.00. (Sprint Brief, p. 15).

AT&T states that in 1997, the FCC determined that the interstate CCLC should be eliminated because the costs of using an incumbent LEC's common line do not increase with usage and therefore these costs should be recovered through flat, non-traffic sensitive fees. (AT&T Brief, pp. 17-18; *CALLS* Order at ¶ 120).

Verizon states that the FCC removed the remaining interstate CCLC amounts through the *MAG* Order and that in doing so, the FCC reasoned that the cost of long distance service would decrease and encourage a more efficient level of use.

⁶ *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Low-Volume Long Distance Users, Federal-State Joint Board on Universal Service*, Sixth Report and Order, etc., FCC 00-193, CC Docket Nos. 96-262, 94-1, 99-249, 96-45 at ¶ 120 (Released May 31, 2000) (hereinafter *CALLS* Order).

(Verizon Brief, p. 10). Verizon and AT&T say that the FCC predicted that per-minute switched access rates would move towards cost-based levels and promote efficient competition in the exchange access market by permitting both incumbent and competitive carriers to compete based on price. (AT&T Brief, pp. 10-11; Verizon Brief, p. 10; *MAG Order*, ¶ 63).

ITA asserts that the CCLC is set at \$0.03 per minute of use pursuant to the Board's rules. ITA states that 199 IAC 22.14(2)"d" regarding CCLCs has been in place since November 1983 and that ITA is in compliance with that rule. (Tr. 301). ITA states that the rate, while not representative of any particular cost, represents an intrastate access service rate element the Board has found to be acceptable.

B. Analysis

The CCLC has been a topic of discussion on both the federal and state levels. In the *MAG Order*, the FCC reiterated its views on the CCLC that it originally explained in its *Access Reform Order*. The FCC concluded that the CCLC is an inefficient cost-recovery mechanism and an implicit subsidy that is not sustainable in a competitive environment and that the interstate CCLC should be removed from the common line rate structure of rate-of-return carriers.⁷

The Board discussed the CCLC in the recent proceeding, *In Re: South Slope Cooperative Telephone Company*, Docket No. RPU-07-1.⁸ In its final order issued

⁷ See *MAG Order* at ¶ 62; See also *Access Reform Order* at ¶ 69.

⁸ See *In re: South Slope Cooperative Telephone Company*, "Final Order," Docket No. RPU-07-1 (issued February 13, 2008).

February 13, 2008, the Board stated that it is required to consider the effect of intrastate access charges on competition, in accordance with Iowa Code § 476.95(3). The Board concluded that the CCLC runs counter to the state's pro-competition policy if a competitive LEC is permitted to charge the CCLC when competing against an incumbent LEC that is not permitted to include that element as a part of its access charges. Thus, the Board has also expressed concern about the effect of the CCLC on competition in general, if not in the same context as the FCC.

However, 199 IAC 22.14(2)"d" requires the inclusion of a 3 cent per minute of use CCLC. The Board cannot waive its rules on its own motion⁹ and no party has requested a waiver of that rule. Therefore, the Board cannot require the removal of the CCLC from ITA No. 1 in this docket, even if the Board were to find that the CCLC is no longer a viable rate element. While Sprint asserts that the Board did not intend for the CCLC to continue indefinitely without periodic review and that the Board would assess the effect of the CCLC on various local exchange utilities through rate proceedings, there has not been a review of the CCLC since its inception in 1984. (Sprint Brief, p. 16). The Board agrees with Sprint that there have been substantial changes in the telecommunications industry since 1984 and that it would be prudent to review whether this charge continues to perform as it was originally intended or whether the CCLC should be modified or eliminated. Accordingly, the Board will initiate a rule making to review the CCLC. In this docket, however, the Board finds that the CCLC should remain in ITA No. 1 pursuant to 199 IAC 22.14(d)"2."

⁹ AT&T vs. IUB, 687 N.W.2d 554, 559-60 (Iowa 2004).

4. Other concerns

Pursuant to paragraph 22.14(5)"c," the interexchange carriers that resisted the proposed amendments to ITA No. 1 bore the burden of supporting their resistances. They met this burden when they showed that ITA No. 1 was originally based on NECA No. 5 but the intrastate access service rates in ITA No. 1 no longer mirrored the interstate rates in NECA No. 5 in various ways. This left certain elements of ITA No. 1 without any support from NECA No. 5 and shifted the burden to ITA to show alternative support for those elements. Presumably, this could have been done by showing the intrastate rates were based on the reasonable and prudent cost of providing intrastate access service. However, this proceeding did not produce any evidence of the costs that the LECs that concur in ITA No. 1 incur when providing intrastate services. Without this cost data, no relationship was established in this proceeding between the incurred costs and derived revenues.

The Board is sensitive to the potential revenue losses that some LECs that concur in ITA No. 1 may see as a result of the Board's decision in this proceeding. Some of the witnesses during this proceeding discussed the possible establishment of a state universal service fund, which may replace some of the revenue lost by the changes directed by this order. However, the Board cannot determine, based on the record provided, if a reduced revenue level resulting from reduced intrastate access service rates would fail to adequately recover the costs of providing service. In the absence of that evidence, the Board cannot take any steps to consider replacement of those revenues.

Sprint asks the Board to require the LECs that concur in ITA No. 1 to provide a refund to Sprint of the money paid to the LECs that is in excess of any reduced or eliminated rate from ITA No. 1. The Board finds this to be impractical. ITA's proposed tariff changes were filed as an extension of current charges. The Board presumes those tariffed charges to be rational until a complaint is brought before the Board and resolved, as in this case. This is a forward-looking decision and the Board will not reach back prior to this decision for the purpose of ordering refunds.

ORDERING CLAUSES

IT IS THEREFORE ORDERED:

1. The Board directs Iowa Telecommunications Association to remove the Transport Interconnection Charge from ITA No. 1, effective 30 days from the date of this order.
2. The Board directs Iowa Telecommunications Association to reduce the Local Switching Rate in ITA No. 1 to \$0.024435 so as to mirror the NECA interstate tariff rate, effective 30 days from the date of this order.

UTILITIES BOARD

/s/ John R. Norris

/s/ Krista K. Tanner

ATTEST:

/s/ Judi K. Cooper
Executive Secretary

/s/ Darrell Hanson

Dated at Des Moines, Iowa, this 30th day of May, 2008.