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September 25, 1998

BY HAND DELIVERY

Ms. Blanca S. Bayo, Director
Division of Records and Reporting
Florida Public Service Commission
2540 Shumard Oak Boulevard
Tallahassee, Florida 32399-0850

Re: Docket No. 980000A-SP

Dear Ms. Bayo:

Enclosed for filing in the above docket on behalf of Florida's small incumbent local exchange companies are the original and fifteen (15) copies of the comments of Tom McCabe. Copies have been served on participants in accordance with the attached Certificate of Service.

Please acknowledge receipt and filing of the above by stamping the duplicate copy of this letter and returning the same to this writer.

Thank you for your assistance in this matter.

Sincerely,

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Stephane W Redburn, for
J. Jeffrey Wahlen

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**Fair and Reasonable Rates
Comments of the Small LECs
Docket 980000-A**

Chapter 364.025, Section 2, 2(a) requires the Florida Public Service Commission to present its conclusions to the Florida Legislature as to the fair and reasonable Florida basic residential local exchange rate taking into consideration affordability, the value of service, comparable rates in other states, and the cost of providing basic residential local exchange service.

The purpose of these comments is to provide the position of the Small LECs regarding fair and reasonable rates and the impact on rural subscribers and universal service. These comments are filed on behalf of the following companies:

ALLTEL Florida, Inc.
Frontier Communications of the South, Inc.
GTC, Inc.
Vista-United Telecommunications

Northeast Florida Telephone Company
TDS TELECOM/Quincy Telephone
ITS Telecommunications Systems, Inc.

Background

A major challenge faced by Florida as well as other states is opening telecommunications markets to competition while preserving universal service. The Federal Telecommunications Act of 1996 states that:

"Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas."

In the current regulatory framework, universal service has been supported through a complex system of inter-customer and inter-service subsidies. These subsidies were devised by requiring the LECs to charge certain classes of customers (business) higher basic local rates so that other classes of customers (residential) were charged lower basic local rates with the intent of supporting universal service. Additional sources of subsidies have included discretionary services such as vertical services, toll and access which were typically priced at rates above cost in order to maintain lower residential rates. This system of support was made possible in the past because local exchange service was provided through a system of exclusive franchises granted for a specified geographical territory. In return for these exclusive franchises, LECs assumed the responsibility of serving all customers within their service territories.

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In today's changing telecommunications environment, the reliance on implicit subsidies that have traditionally supported universal service can not be sustained in a competitive marketplace. Competitors, who have no obligation to serve all customers in the market, will naturally target high volume, low cost businesses and residential customers. As a result, LECs will need to reduce rates for those services that are priced above cost or risk losing the most profitable customers that typically provide the greatest level of support to universal service.

Although none of the small LECs in Florida has experienced significant and widespread local exchange service competition as provided for under the Telecommunications Act, the small LECs have all encountered competition in one form or another such as bypass, intraLATA presubscription, wireless, and competition from pay telephone service providers. In addition to competition, small LECs have seen revenue erosion from legislative mandates or Commission action, such as access reductions, elimination of interlata and intralata subsidies, and expansion of Extended Area Service (EAS), with no provision to replace these lost revenues. All of these factors are reducing the revenue source used by small LECs to maintain the current basic local exchange rates and to enhance and maintain network infrastructure to ensure that rural customers have access to high quality service(s), advanced telecommunications services and information services. Thus the small LECs believe that a balanced approach to restructuring prices for telecommunications services and universal service funding are *essential* in ensuring the continuation of universal service and the deployment of an advanced telecommunications network as required by the Telecommunications Act of 1996.

The Telecommunications Act of 1996 outlines in Section 254 requirements essential to the preservation of universal service. Under this law, Congress intended that the Federal-State Joint Board and the Federal Communications Commission (FCC) base universal service policies on specific policies outlined in the Act. The small LECs believe the first three principles are intertwined in the issue before the Florida Public Service Commission, which is a determination of fair and reasonable rates. These principles are:

1. Quality services should be available at just, reasonable, and affordable rates,
2. Access to advanced telecommunications and information services should be provided in all regions of the Nation, and
3. Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

The small LECs' positions on affordability, value of service, comparable rates in other states, and the cost of providing basic residential local exchange service are guided by these principles.

What is affordability?

Affordability refers to the financial means of a customer to purchase services. In the context of this proceeding, an affordable rate should be defined as a rate that is representative of value of service, provides access to the maximum number of customers willing and able to purchase basic local telecommunications service and is just and reasonable to encourage infrastructure investment.

In its determination of affordability, we suggest that the Commission should not default to the lowest common denominator. For example, it would not be appropriate to set the rates so low that "every possible subscriber" could afford the service. Rather, the Commission must strive to find a balance between providing quality service at rates that are just, reasonable, and affordable.

Will restructuring basic local exchange rates make telephone service unaffordable in rural areas?

No. The small LECs believe inflation, purchasing power, subscribership and household expenditures are indicators of affordability that the FPSC should consider when addressing fair and reasonable basic local residential exchange rates. In instances where local exchange companies have not had a rate increase in many years, the affordable level, adjusting for inflation, allows companies greater flexibility for restructuring local rates while maintaining affordability. For instance, the purchasing power of \$1.00 in 1984 is equivalent to \$1.54 in 1997.

For the most part, small LEC rates have been the same for more than a decade. If inflation is taken into account, all of the small LECs' rates could increase without changing the relationship subscribers had with their small LECs more than a decade ago.

An analysis of subscribership levels between Florida and other states that have higher average rates (such as Alabama, Georgia, and South Carolina) indicates that increases in basic residential local exchange rates will not adversely affect subscribership levels in Florida.

Finally, in 1995, the annual expenditure for telephone service as a percentage of total household income was 2.2%. The total monthly household expenditure in 1997 was approximately \$62.00 which included an average monthly residential basic local service charge of \$19.49 including taxes and subscriber line charges. Interestingly, toll and other telephone expenditures account for more than twice the total monthly household expenditure for telephone service.

In the determination of affordability, should the impact on low income consumers be of primary importance?

No. Federal and State policies have been implemented to address the needs of low-income subscribers through Lifeline and Link-up programs. Customers qualifying for one of the six programs eligible for Lifeline service receive an interstate credit of \$7.00 and a state credit of \$3.50 for a total assistance of \$10.50. The chart below shows the price of basic residential local exchange service after the Lifeline credit for each of the small LECs based on their average residential basic local rate.

<u>Company</u>	<u>Basic Rate</u>	<u>Lifeline Rate</u>
TDS Telecom/Quincy	\$12.70	\$2.20
ALLTEL	\$9.75	\$0.00
Frontier	\$10.90	\$ 40
GT Comm		
Gulf	\$7.47	\$0.00
St. Joe	\$7.24	\$0.00
Floral	\$7.60	\$0.00
Indiantown	\$8.96	\$0.00
Northeast	\$9.00	\$0.00
Vista-United	\$9.27	\$0.00

Do just and reasonable rates play a role in infrastructure investment?

Yes. In its consideration of just and reasonable basic residential local exchange rates, the Commission should take into consideration how basic residential local rates impact infrastructure investment, whether from incumbent LECs or new entrants. Companies/investors will invest their money if there is a opportunity to earn a reasonable return on their investment. Capital dollars are a scarce resource, especially for small rural LECs, and their investment decisions are often directed to the achievement of the greatest possible return. The continued reliance on implicit subsidies creates uncertainty in the investment decision of incumbent LECs and provides confusing market signals to new entrants. The lack of certainty that incumbent LECs or new entrants will be able to set rates at just and reasonable levels to ensure a reasonable return on its core service, dialtone, will ultimately lead to a situation of "haves" and "have nots" between rural and urban areas.

Regardless of the services residential and business customers purchase, society as a whole benefits from the deployment of a high quality, advanced telecommunications infrastructure. Telecommunications infrastructure is a critical component to economic

development, distance learning, health care, etc. which are all essential to the needs of rural areas. Telecommunications services are a public good that reflects a total societal benefit and cost responsibility.

The Commission should establish rates at levels that provide incentives for companies to continue to invest and maintain infrastructure to ensure that access to advanced telecommunications and information services will be available in all regions of the Nation as set forth in the Act.

Should the determination of affordability be compared to other communications services?

Yes. Generally, people consider basic local exchange service to be a necessity. Thus, basic exchange rates should be set at levels sufficient to ensure affordability. However, the simple fact that local exchange service is considered a necessity should not imply that rates should be subsidized in order to free up disposable income for other services. The small LECs believe that rates charged for other non-essential communications services such as newspapers, cable television service, and Internet access should be considered when reviewing consumers' willingness and ability to pay for telephone service.

For example, in the United States, as of February 1998, there were 65,864,090 basic cable television service subscribers. Approximately 70% of consumers that have access subscribe to cable television service. Based on the FCC's Report on Cable Industry Prices, the average monthly cable rate as of July 1, 1997 ranged from \$27.26 to \$28.83 for competitive and non-competitive areas respectively. Additionally over 11 million consumers are served by non-cable multi-channel video providers. In Florida, nearly 4.3 million Florida consumers subscribe to cable television service.

Internet Access, which is becoming increasingly more popular, is typically priced at rates that exceed the basic residential telecommunications exchange rate of the small LECs. Additionally, consumers who purchase a daily newspaper or other forms of printed news media can spend as much as \$15 - \$20 a month.

Value of Service

Value of service refers to the importance of basic telecommunications service to individual customers and to society as a whole. Historically, the "value of service" has meant the number of subscribers a basic local exchange subscriber can call or be called by for a flat monthly rate and the societal benefit associated with public health and safety. Through the implementation of expanded local calling, residential customers have shown a willingness and ability to pay more for flat-rate basic local exchange service in order to call their community of interest. From a society viewpoint, universal support mechanisms (implicit and explicit) at the federal and state levels are designed to increase subscribership by keeping rates affordable, with the belief that the value of the network is

greater to all users, the greater the number of people on the network. Additionally, society benefits with widespread availability of telephone service to access public safety services such as emergency services. There are few communities today where consumers do not have access to enhanced emergency 911 systems via their local telephone service. The value that consumers perceive in telephone service as a safety device is observed in the willingness of consumers to pay for Cellular service for emergency contact purposes.

Today, however, the value of service concept includes more than just simple voice conversations between subscribers. Residential local service now allows subscribers to reach any other person with a telephone, a pager, a facsimile machine, a cellular unit or a personal computer anywhere in the world. In rural communities, value of service might refer to the isolation that might be relieved by telephone contact with others. In today's highly mobile society, contact with family, friends, doctors, schools, is a core value that converts to actual cost savings to consumers. In addition to avoiding the need to get in the car and travel, thus devouring time and money, through "on-line" access, consumers have access to both educational and shopping services that otherwise may not be available in rural communities. They are able to take advantage of shopping direct services that result in actual dollar savings over the more conventional means of shopping.

Comparable Rates In Other States

TDS Telecom, the parent company of Quincy Telephone Company operates in three southeastern states, Georgia, Alabama, and South Carolina that are in the process of rebalancing local rates. In Alabama, local residential rates are beginning transition over a five year period to a state benchmark of \$16.30. In 1996, the State of Georgia began a five year transition of intrastate access rates to the 1995 interstate level. The lost access revenues are being recovered through increases in residential local exchange rates of up to \$1.00 per year. In South Carolina, residential basic local exchange rates are being rebalanced to the state-wide average rate of \$14.35. Companies whose rates are in excess of the state-wide average are unaffected.

Other states in which TDS operates that have rebalanced local rates are Michigan and Pennsylvania. In Michigan, rural LECs have increased residential basic local rates to \$13.05 with an intrastate subscriber line charge of \$3.50. This equates to a basic residential local exchange rate of \$16.55 compared to Florida's average rural residential basic local exchange rate of \$9.21 (not including the interstate subscriber line charge). In Pennsylvania, TDS Telecom companies have increased local rates to \$18.50 (not including the interstate subscriber line charge.)

Cost of Providing Residential Basic Local Exchange Service

Rural networks are typically high cost regardless of how efficiently they operate. There are many factors that contribute to the high cost to serve rural customers such as density,

cost of capital, length of loops, and economies of scales which are greater for large ILECs for use in obtaining larger discounts for equipment such as switches and cable, as well as other factors.

For the purpose of determining the cost of basic residential local exchange service, the Commission staff requested LECs to provide these costs as Total Service Long-Run Incremental Costs or TSLRIC. These elaborate and detailed cost studies break down the direct, shared and common costs for basic local telecommunications service. Due to time constraints and limited resources, the small LECs were unable to perform such studies. However, the small LECs have provided to the Commission embedded costs of providing basic residential local service to their customers. These costs ranged from a low of \$38.07 for GT Comm's Gulf study area to a high of \$73.07 per line for Indiantown.

In the absence of TSLRIC studies, the small LECs suggest that the costs of the large LECs can serve as a gauge in evaluating the cost of basic local exchange service for small LECs. The small LECs believe that the TSLRIC studies produced by the three large LEC would represent the minimum economic cost the small LECs incur to provide residential basic local exchange service.

The data below highlights some of the differences between small LECs and large LECs which can be attributed to the high cost to serve rural areas.

Company	Lines/Exch	Lines/Sq Mi*	Cbl Inv/Line	Total Inv/Ln	USF Loop Cost /Ln ¹
ALLTEL	2,817	21	\$1,404	\$2,321	\$330
Gulf	4,979	9	747	1,153	391
St. Joe	2,527	12	822	1,387	409
Floral	1,165	8	1,002	1,506	408
TDS/Quincy	4,330	31	1,297	2,143	334
Northeast	4,129	16.5	1,395	2,288	455
BellSouth	31,594	314	850	1,780	288
GTE	25,209	472	916	1,835	289
Sprint/United	20,009	135	883	1,752	272

*Note: Low density equates to higher average cost per loop.

¹ USF Costs obtained from 97-1 USF filing to the FCC. Small Rural LECs costs ranged from \$334 to a high of \$473 per line.

Conclusion

The principle of universal service has guided the development of telecommunications in rural areas, allowing residential customers access to the same features and capabilities as their urban counterparts. Historically, this has been accomplished through the use of implicit and explicit support mechanism at the state and federal level. As the industry moves forward in a competitive environment, justification of the cost and revenue structure becomes more difficult.

The factors under consideration in this proceeding, affordability, value of service, comparable rates in other states and cost, support a balanced restructuring of basic residential local exchange rates. Of particular interest to rural LECs is comparability of rates and services between urban and rural areas. The small LECs believe that restructuring local rates will provide the proper incentives to invest and maintain high quality telecommunications service in rural areas and allow all telecommunications rates to be restructured to comparable rates in urban areas.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true copy of the foregoing has been furnished by U. S. Mail or hand delivery (*) this 25th day of September, 1998, to the following:

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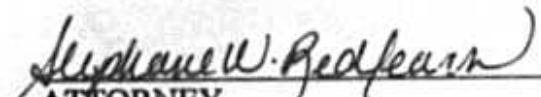
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