

ALASKA LEGISLATURE SPECIAL COMMITTEE/SUBJECT FILES 8672

2250 SCOMM 88: HOUSE TELECOMMUNICATIONS TASK FORCE, 1993

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Table 30
Unrestricted General Fund Revenues of Alaska State Government, 1979-1989
 (millions of dollars)

Fiscal Year	Total Unrestricted General Funds a/	% Change From Previous Year	Petroleum Based Revenue b/	% Change From Previous Year	Nonpetroleum Based Revenue c/	% Change From Previous Year
1980	2,501.2	—	2,256.5	—	244.7	—
1981	3,718.2	48.7	3,304.8	46.5	413.4	68.9
1982	4,108.4	10.5	3,559.1	7.7	549.3	32.9
1983	3,631.0	-11.6	3,001.2	-15.7	629.8	14.7
1984	3,390.1	-6.6	2,852.8	-4.9	537.3	-14.7
1985	3,260.0	-3.8	2,737.0	-4.0	523.0	-2.7
1986	3,075.5	-5.7	2,657.9	-2.9	417.6	-20.2
1987	1,799.4	-41.5	1,394.5	-47.5	404.9	-3.0
1988	2,305.8	28	1,949.6	39.8	356.2	-12.0
1989 d/	1,337.6-2,316.8		1,080.2-2,003.4		257.4-313.4	
1990 d/	1,285.1-2,424.9		1,067.1-2,129.9		218.0-295.0	

a/ Sum of petroleum and nonpetroleum based revenues.

b/ Includes corporate income, severance and property taxes, royalties and rents, and miscellaneous revenues from federal mining rents and royalties, bonus sales and reserve tax.

c/ Includes corporate and other taxes, license and permit fees, State resources revenue (net of petroleum revenues consisting of bonus sales, royalties, and rents), and miscellaneous revenues from federal shared revenues net of federal mining rent, and others.

d/ Projected range.

Source: Alaska Department of Revenue: viva voce (FY 87 and FY 88); Revenue Forecast, March, 1988 (FY 89 and FY 90)



CERTIFICATE OF SERVICE

I, Linda K. Smith, do hereby certify that, on February 27, 1989, I have caused to be sent a copy of the foregoing "Data Response of The State of Alaska to the Supplemental Order Inviting Comments" by United States mail, postage prepaid, to the following:

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Room 814
Washington, DC 20554
 - * Commissioner James H. Quello
Federal Communications Commission
1919 M Street, N.W.
Room 802
Washington, DC 20554
 - * Douglas Slotten
Policy and Programming Division
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* Indicates delivery by hand.

/s/ Linda K. Smith
Linda K. Smith

2-27-89

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February 27, 1989

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Federal Communications Commission
Office of the Secretary

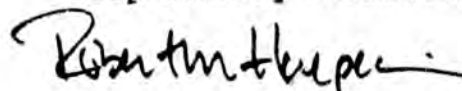
Donna R. Searcy
Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, DC 20554

Dear Ms. Searcy:

This letter is written to report a meeting on February 24, 1989 between representatives of the State of Alaska and Commission staff. This meeting was held to discuss questions the State had concerning the Federal-State Joint Board's Supplemental Order Inviting Comments in CC Docket No. 83-1376, RM 4436 (FCC 88J-4). The meeting was held with Douglas Slotten of the Commission's staff. Attending this meeting on behalf of the State were Linda K. Smith and the undersigned, as counsel for the State, and Karl J. Korsmo and Barry Rubens of Ernst & Whinney, the State's consultants on this matter.

In the event there are any questions concerning this matter, please communicate with this office.

Respectfully submitted,



Robert M. Halperin

cc: Douglas Slotten

3-3-89

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LINDA K. SMITH
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March 3, 1989

HAND DELIVERED

Ms. Donna R. Searcy
Secretary
Federal Communications Commission
Room 222
1919 M Street, N.W.
Washington, D.C. 20554

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MAR - 3 1989

Federal Communications Commission
Office of the Secretary

Re: CC Docket 83-1376, RM 4436

Dear Ms. Searcy:

This letter is written to report meetings between Kay E. Gouwens, Special Assistant Attorney General, and undersigned counsel for the State of Alaska, with William E. Long (March 1, 1989), Nels J. Smith (March 2, 1989) and Bruce Hagen (March 3, 1989). At the meetings, matters reflected in the State's comments, and other filings in the above captioned proceeding, were discussed.

If there are any questions regarding this matter, please communicate with this office.

Very truly yours,

Linda K. Smith

Linda K. Smith

4-13-89

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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APR 13 1989

Federal Communications Commission
Office of the Secretary

In the Matter of)
)
Integration of Rates and Services)
for the Provision of Communications)
by Authorized Common Carriers)
Between the Contiguous States and)
Alaska, Hawaii, Puerto Rico and)
the Virgin Islands)
)

CC Docket No. 83-1376
RM 4436

TO: THE FEDERAL-STATE JOINT BOARD

**COMMENTS OF THE STATE OF ALASKA
IN RESPONSE TO THE SUPPLEMENTAL
ORDER INVITING COMMENTS**

THE STATE OF ALASKA

Douglas B. Baily
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April 13, 1989

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)

Integration of Rates and Services)
for the Provision of Communications)
by Authorized Common Carriers)
Between the Contiguous States and)
Alaska, Hawaii, Puerto Rico and)
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CC Docket No. 83-1376
RM 4436

TO: THE FEDERAL-STATE JOINT BOARD

**COMMENTS OF THE STATE OF ALASKA
IN RESPONSE TO THE SUPPLEMENTAL
ORDER INVITING COMMENTS**

The State of Alaska ("Alaska" or "the State"), by its attorneys, hereby submits its comments in response to the Supplemental Order Inviting Comments, FCC 88J-4, released January 3, 1989 ("Supplemental Order") in the above-captioned proceeding.

In the Supplemental Order, the Joint Board asked the parties to submit data with respect to a variety of matters. It also asked the parties to comment on the appropriate objectives for this proceeding, and on certain alternatives for achieving those objectives. The State of Alaska supplied data in response to the Joint Board's request,^{1/} and now submits these comments which address the Board's objectives and the alternative means of realizing them.

^{1/} Data Response of the State of Alaska to the Supplemental Order Inviting Comments, filed February 27, 1989.

I. SUMMARY.

The State comments on objectives designated by the Joint Board for this proceeding, the data responses and the alternative methods of achieving the Joint Board's objectives.

A. The Objectives.

Universal service is the polestar which should guide resolution of the issues in this proceeding. The national commitment to universal service cannot be compromised, and this is particularly true for Alaska, where there is extraordinary need for and dependence on communications, and where universal service has been difficult to attain. Further, achievement of universal service requires consideration of the impact of national policies on intrastate rates and services, and recognition of the need for a carrier of last resort.

Rate integration, and the national geographic rate averaging on which it is based, are essential to realization of universal service. Attempts to undermine geographic rate averaging, whether in this proceeding or otherwise, should be vigorously resisted. Rate integration should be implemented on all routes, including the Alaska-Hawaii route.

Jurisdictional revenue requirement neutrality is also an important component to promotion of universal service. Accordingly, the State opposes any reassignment of Category 4.23 (previously Category 8.23) equipment costs, and notes one approach to achieving jurisdictional revenue requirement neutrality.

Improved efficiency is a worthwhile goal, but must be measured with respect to both the interstate and intrastate

markets, if it is to be consistent with the Joint Board's "other public interest concerns." With respect to the Joint Board's market based competitive entry objective, it appears that there is now interstate service competition, so that the issue for the Joint Board is not how to create, but how to treat, competition, consistent with promotion and enhancement of universal service and maintenance of rate integration and revenue requirement neutrality.

B. The Data Responses.

The initial data responses do not contain much data on many of the critical issues in this proceeding, and virtually no data at all on other critical issues, including, for example, the impact of either Plan A or Plan B on jurisdictional revenue requirements. Much of the data is inconsistent, for different periods, or otherwise flawed. While supportive of technological innovation and high standards of service quality, the State is concerned about the costs of the proposed Alascom network improvements and the manner in which these costs are recovered. Accordingly, the State believes additional data may be needed to analyze properly the proposed plans.

C. The Plans.

Despite the absence of needed data and the impossibility at present of analyzing the impact on this proceeding of the not yet released Commission price cap order, the State has offered some preliminary comments. In its view, the flaws in the present service arrangements identified by the Joint Board can be remedied. The State suggests a method to improve present

arrangements to increase efficiency and reduce costs. With this improvement, the objectives discussed above can be achieved.

While only briefly described, and lacking data on its impact, Plan A appears more consistent than does Plan B with the objectives the State believes the Joint Board should emphasize, though even Plan A would need to be revised to assure that the universal service and rate integration objectives are satisfied. The State opposes Plan B because it appears inconsistent with universal service and related objectives and because this plan puts the regulatory cart before the horse. The State cannot risk the future of Alaska telecommunications on a plan that would be implemented without any informed understanding of what would eventually occur as a result of it, and which would require, after its adoption, multiple proceedings to determine how it would be implemented and what its effects would be.

II. UNIVERSAL SERVICE AT AFFORDABLE RATES SHOULD AND MUST BE THE PRIMARY OBJECTIVE IN THIS PROCEEDING.

The Joint Board has set forth "the fundamental objectives . . . tentatively selected to apply in developing [its] recommendations" (Supplemental Order at ¶15.) It "tentatively identified . . . five objectives which . . . should guide . . . resolution of the issues in this proceeding -- preservation of universal service, continuation of rate integration, market based competitive entry, increased efficiency, and jurisdictional revenue requirement neutrality." (*Id.* at ¶24.) The Joint Board asked for comment on each of these objectives and a prioritization of them. (*Id.*)

A. The Universal Service Objective.

The State has long stressed the critical and primary importance of universal service. It has also noted the extent to which achievement of universal service is intertwined with continuation of rate integration, geographic rate averaging and jurisdictional revenue requirement neutrality.

Universal service has been particularly difficult to attain in Alaska, as has been previously documented.^{2/} In a June 1986 study, the General Accounting Office noted that the data for Alaska telephones in households for the period between November 1983 and March 1986 showed average penetration levels of below 87 percent.^{3/} Even now, penetration rates remain low. In July 1988 (the period for which the most recent data are available), 92.8 percent of all households in the United States had a telephone.^{4/} Telephone penetration in Alaska was below the national average,^{5/} at 87.3 percent.^{6/} Indeed, for every one of the ten income categories analyzed, the percentage of Alaska households with telephones was below the national average.^{7/} Alaska's telephone

2/ See, e.g., Comments of the State of Alaska, CC Docket Nos. 78-72, 80-286, filed August 29, 1986.

3/ General Accounting Office, Telephone Communications -- The FCC's Monitoring of Residential Telephone Service, at 18-19.

4/ Monitoring Report, CC Docket No. 87-339, December 1988, prepared by the Staff of the Federal-State Joint Board in CC Docket No. 80-286, at Chart 1.1.

5/ Id.

6/ Id. at Table 1.4 (March 1988). The March 1988 penetration percentage is lower than it was in each year since 1984. Id.

7/ Id. at Tables 1.2 and 1.4 (March 1988).

penetration rate in 1988 was among the lowest in the nation, behind all states except Mississippi, Alabama and New Mexico.^{8/} Since such data were collected, Alaska has been one of the four states with the lowest telephone penetration rates.^{9/}

As the State has previously noted, universal service must, therefore, include both creation and preservation of universal telephone service. It must encompass policies that both make it possible for those that do not now have telephone service to attain it, and prevent current telephone subscribers from having to drop service.

Telephone service is particularly important in Alaska. It plays a special role not only "in eliminating the problem of distance and isolation," and in facilitating "citizen participation in education and the political process as well as [in] receiv[ing] basic telephone service, health care and entertainment", but also in "provid[ing] the necessary structure for Alaska's economic development."^{10/} In short, "modern communications are not a convenience in Alaska. Communications are often essential to life itself"^{11/} The extraordinary

8/ Telephone Subscribership in the U.S., Industry Analysis Division, Common Carrier Bureau, January 1989 Report, based on Current Population Survey, Bureau of the Census, Department of Commerce.

9/ See Reply Comments of the State of Alaska, CC Dockets No. 78-72, 80-286, filed October 9, 1986, at 3-4.

10/ State of Alaska House of Representatives, Special Committee on Telecommunications, Interim Report (1986) at 2,8.

11/ United States Senate Committee on Commerce, Science and Transportation and House of Representatives Committee on Energy and Commerce, Joint Hearings, Universal Telephone
(Fn. continued)

reliance in Alaska on telecommunications has been a recurring theme in this proceeding, has been recognized in prior decisions,^{12/} and should continue to be taken into account in determining the importance to be given to the universal service objective.

The State said, in 1984, and continues to believe, that "[t]he public interest of the people of Alaska -- and of the people of the entire United States -- is to further and ensure the availability of affordable universal telephone service. Enhancement of that public interest objective, not private interests, is the goal of this proceeding, and the polestar which . . . must [be] follow[ed] in resolving the questions raised in these dockets."^{13/} The State is, therefore, pleased that the "Joint Board is firmly committed to ensuring universal service for Alaska" and that it recognizes that "[n]ationwide universal service is one of the objectives of the Communications Act." (Supplemental Order at ¶28.) Universal service has, indeed, been

(Fn. continued)

Service Preservation Act of 1983, at 136, testimony of Lisa Rudd, Commissioner, State of Alaska Department of Administration. See also Data Response of the State of Alaska, filed July 15, 1986 and Data Response of the State of Alaska to the Supplemental Order Inviting Comments, filed February 27, 1989.

12/ Integration of Rates and Services, CC Docket No. 83-1376, FCC 84-616 (December 11, 1984) at 2; Integration of Rates and Services, CC Docket No. 83-1376, FCC 84-512 (December 11, 1984) at 7.

13/ Comments of the State of Alaska, filed September 4, 1984, at 2; See also Comments of the State of Alaska, filed November 28, 1986, at 2-12.

"a specific Commission and Joint Board objective in other proceedings" (Id. at 128.)

There can be no question that universal service is a national commitment, mandated by the Congress,^{14/} and endorsed by the courts^{15/} and the Commission.^{16/} Universal service benefits all Americans and draws us together as one nation. All Americans gain from the ability to call any part of the country, or to reach someone who can do so. There can be no compromising this national commitment, in this proceeding or elsewhere.

14/ 47 U.S.C. § 151. See also, e.g., the House Committee on Energy and Commerce Report on H.R. 4102, "The Universal Telephone Service Preservation Act of 1983," which stated:

The 50-year national effort to bring affordable and universally available telephone service to the public has served the nation well. Universal telephone service has contributed to the nation's economic, social and political integration and development. Each telephone subscriber receives a greater benefit and more valuable service when anyone else in the country can be called.

H.R. Rep. No. 479, 98th Cong., 1st Sess. 13 (1983).

15/ See, e.g., NARUC v. FCC, 737 F.2d 1095, 1108 (D.C. Cir. 1984), cert. denied, 469 U.S. 1227 (1985). Citing 47 U.S.C. § 151, the Court of Appeals said "[o]ur case law recognizes the prominence of this universal service objective," and rejected a contention that the Commission has no responsibility to promote universal service.

16/ See Status of Radio and Antenna Equipment Used in the Basic Exchange Telephone Radio Service, DA 89-238, released February 27, 1989, at ¶¶ 17,19 (subscriber unit treated as regulated network equipment to promote universal service); MTS and WATS Market Structure, CC Docket Nos. 78-72 and 80-286. (July 26, 1985) at 1 ("The preservation of universal telephone service has been a major Commission objective . . ."); MTS and WATS Market Structure, 97 F.C.C.2d 682, 683 (1983), aff'd in part, remanded in part, sub nom. NARUC v. FCC, 737 F.2d 1095 (D.C. Cir. 1984), cert. denied, 469 U.S. 1227 (1985). See also Notice, CC Docket No. 78-72, Phase IV, FCC 83-254 (June 8, 1983); MTS and WATS Market Structure, 93 F.C.C. 2d 241, 265-67, 278 (1983).

1. The Relationship of Universal Service to Intrastate Service and the Need for a Carrier of Last Resort.

The Joint Board has identified two important aspects of the national commitment to universal service which deserve special comment. Implementation of universal service (1) involves consideration of the impact of national policies on intrastate rates and service (Supplemental Order at ¶15);^{17/} and (2) requires the availability of interexchange service, if necessary, through "designation of a carrier of last resort." (Supplemental Order at ¶29.)

Universal service includes recognition of the impact of national policies on intrastate rates and services. See NARUC v. FCC, 737 F.2d 1095, 1108, n.6 (D.C. Cir. 1984), cert. denied, 469 U.S. 1227 (1985).^{18/} See also Supplemental Order at n.46.

As the State has previously said, it is of the greatest importance that affordable, universal service be available to all Alaskans, and that the adjectives "affordable" and "universal" apply to

^{17/} See also Supplemental Order at n.46: "This program [in Dockets 78-72 and 80-286] permits an additional interstate assignment of local loop costs in excess of specified levels. It is designed to permit high cost telephone companies to keep local rates lower than they otherwise would be."

^{18/} "MCI contends that the FCC has no responsibility to promote universal service because 'the Commission has no statutory responsibility for local communications', and therefore 'it would be unlawful for it to promulgate a policy designed to . . . benefit local communications.' Brief for Intervenor MCI Telecommunications Corp. at 19 n. 20. We reject MCI's argument. Congress has directed that, 'so far as possible . . . all people of the United States are to have adequate telephone facilities at reasonable prices." NARUC v. FCC, 737 F.2d at 1108, n.6. See also MCI Telecommunications Corp. v. F.C.C., 750 F.2d 135 (D.C. Cir. 1984) (upholding interim SPF freeze).

intrastate, as well as interstate, service.^{19/} While the Joint Board and the Commission do not regulate intrastate communications, the existence of both the mandatory and discretionary Joint Board referral processes are an acknowledgment of the importance to national policies of intrastate rates and service. No Joint Board can blind itself to the impact its actions can have on intrastate rates and services. Prior decisions in this proceeding have recognized the relationship of universal service and intrastate rates,^{20/} and the State urges that it continue to be recognized.

Universal service requires recognizing the need for a carrier of last resort for interstate and intrastate service. The importance to universal service of interexchange service is recognized. (Supplemental Order at ¶29). The State agrees with

^{19/} Comments of the State of Alaska, filed April 5, 1985, at 2-3.

^{20/} The Commission has repeatedly recognized that changes in intrastate rates could adversely affect universal service. See, e.g., Memorandum Opinion and Order, FCC 84-616 at ¶4 (expressing the Commission's desire to avoid "churning of intrastate rates" and putting "at risk the intrastate communications that are essential to many subscribers in remote areas of Alaska") (released December 11, 1986); Memorandum Opinion and Order, FCC 84-512 at ¶20 (expressing concern for "adverse effects on Alaskan ratepayers") (released December 11, 1984); Notice of Proposed Rulemaking, FCC 85-520 at ¶19 ("[The Joint Board] should also consider the impact on intrastate rates for Alaska as a consequence of changes in traffic patterns associated with the structure under consideration") (released September 27, 1986); Memorandum Opinion and Order, FCC 86-602 at ¶26 (permitting implementation of the final step of rate integration, in part to "prevent the separations procedures from increasing the allocation of costs to the intrastate jurisdiction, thereby reducing upward intrastate rate pressures . . . which might result in intrastate rate increases") (released January 1, 1987).

the Joint Board's tentative conclusion that a carrier of last resort be designated, and that it be responsible for building necessary facilities and providing service in accordance with the measures adopted in this proceeding. (Id. at ¶30.) In connection with consideration of carrier of last resort responsibilities, it should be noted that any changes to the Alaska market structure should be carefully crafted to avoid creating stranded investment or other problems which would undermine jurisdictional revenue requirement neutrality and universal service.

2. The Relationship of Universal Service to Other National Policies.

The statutory mandate of universal service requires continuation of the concomitant policy of rate integration and the national geographic rate averaging pattern on which it is based. Jurisdictional revenue requirement neutrality is also interwoven into achievement of universal service. Accordingly, the State considers rate integration and jurisdictional revenue requirement neutrality part of the universal service objective and inseparable from it. It is pleased that the Joint Board has recognized the interrelationship and primacy of these objectives. (Supplemental Order at ¶¶31-32.)

B. The Rate Integration Objective.

Realization of universal service requires that the seventeen year national policy of rate integration^{21/} be maintained. The State agrees, therefore, with the tentative conclusions of the

^{21/} See Domestic Communications Satellite Facilities, 35 F.C.C. 2d 844 (1972), aff'd on recon., 38 F.C.C. 2d 665 (1972), aff'd sub nom. Network Project v. FCC, 511 F.2d. 786 (D.C. Cir. 1975).

Joint Board that (1) "continued integration of interstate MTS and WATS rates is necessary to ensure that all Alaska residents are able to participate fully in the social, economic and political life of our nation"; and (2) "a rate structure which averages interstate toll rates for states other than Alaska, while imposing de-averaged rates for service to and from Alaska could raise questions concerning an unjust and unreasonable discrimination pursuant to Section 202 of the [Communications] Act".

(Supplemental Order at ¶25.) The State, therefore, supports the Joint Board's efforts to develop a recommendation that continues rate integration (*id.*) and believes the Joint Board correctly rejected AT&T's attacks on rate integration (Supplemental Order at n.39).^{22/}

Certain aspects of the rate integration policy require special comment.

1. National Geographic Rate Averaging.

Rate integration means that offshore points are integrated into the national geographically averaged rate pattern. For there to be rate integration, there must be national geographically averaged rates.^{23/} Incursions on national geographic rate averaging could undermine or eliminate rate integration and impede

^{22/} In addition, for the reasons discussed above and in its prior comments, the State believes that establishment of separate "funds" for so-called "bush" areas, or other areas, is not consistent with rate integration and rate averaging and would undermine both. Accordingly, the State has not supported this approach.

^{23/} See Integration of Rates and Services, 96 F.C.C.2d 567,571 (1984).

achievement of universal service for Alaska and the rest of the nation.

There are, at present, two substantial and troublesome risks to the future of national geographic rate averaging. One involves the attack on national geographic rate averaging made in this proceeding when AT&T argues that costs of providing service to Alaska are high, so high that it should not have to provide such service at rate integrated rates without special compensation. But, as the Joint Board has noted, "AT&T is fully compensated for the losses it experiences in the Alaska market through the rate averaging process." (Supplemental Order at n.39.) No showing of harm by nationwide rate averaging nor any showing of material impact on competitiveness has been made. (*Id.*)

Costs of and rates for service to and from Alaska must continue to be treated in the same way as costs of and rates for service to and from other states are treated. To do otherwise would both violate Section 202(a) of the Communications Act,^{24/} and undermine the universal service objective. AT&T's attack on rate integration, and the geographic averaging on which it rests, must continue to be rejected.

^{24/} The rate integration policy "should be interpreted as implicitly recognizing that a rate structure which averages rates in 48 states and de-averages rates in two states may subject the residents of those two states to an unreasonable prejudice or disadvantage within the meaning of Section 202(a)" MTS and WATS Structure, 81 F.C.C.2d 177, 192 (1980). "[A] rate structure which uses different ratemaking methods to determine the rates which different users pay for comparable service is inconsistent with the national policy expressed in Section 202(a)." *Id.* See also Supplemental Order at ¶25.

Another risk for national geographic rate averaging is found in the Commission's price cap proceeding.^{25/} Debate about that proceeding once again focused on the previously recognized fact that departure from nationally averaged rates would not be in the public interest.^{26/} For this reason, in the price cap proceeding, a number of Senators and Congressmen expressed their concern about and support for national geographic rate averaging.^{27/} In an exchange of correspondence to the Congress, Chairman Patrick has commented:

Since its creation by Congress in 1934, the Commission has adhered to a policy of supporting geographic rate averaging. I personally am committed to this policy,

^{25/} News Release, CC Docket No. 87-313, Report No. DC-1379 (March 16, 1989).

^{26/} See, e.g., the views of the Federal-State Joint Board in CC Docket Nos. 78-72 and 80-286:

This Joint Board is concerned about the potential adverse effects of widespread deaveraging of interstate toll rates. Thus, we recommend that the Commission continue uniform nationally averaged MTS and WATS rates for the dominant interexchange carrier.

MTS and WATS Market Structure, Recommended Decision and Order, CC Docket Nos. 78-72 and 80-286, FCC 87J-1, at 33, n.85 (March 31, 1987). See id. at 62, n.164.

See also letter of November 18, 1986 to Chairman Mark S. Fowler from Senator John C. Danforth, then Chairman, Senate Committee on Commerce, Science and Transportation ("I firmly support the policy of nationally averaged rates"). See also H.R. 1572, "The Telephone Rate Verification Act of 1989" and its Introductory Statement, 135 Cong. Rec. E943 (daily ed. March 22, 1989) ("Customers . . . fear that price caps threaten our long held policy of geographic rate averaging which ensured that prices for telephone services are the same for urban and rural areas.").

^{27/} See, e.g., letter from Chairman John Dingell, House Committee on Energy and Commerce, and Chairman Edward J. Markey, Chairman, Subcommittee on Communications and Finance, to Chairman Dennis R. Patrick, dated September 28, 1988.

and I assure you that all decisions that have been and will be made in this proceeding will be consistent with -- and will in no way contribute to undermining -- geographic rate averaging.

* * * *

Moreover, as an additional demonstration of my personal commitment to the continuation of geographically averaged rates, I pledge to you that the incentive regulation proposal I am urging my colleagues to adopt on March 16, 1989, will contain clear and unambiguous language stating that any AT&T tariff proposal to deaverage rates will be extended for the full notice period provided under Section 203 of the Communications Act, and will be suspended for the full period provided for under Section 204 of the Act and investigated.^{28/}

In addition, both Chairman Patrick and Common Carrier Bureau Chief Brock repeated the "renewed commitment to geographic rate averaging" at the March 16, 1989 Sunshine Meeting in which price caps were approved. It is, therefore, to be hoped that this risk to national geographic rate averaging will be avoided.

2. The Alaska-Hawaii Route.

The Joint Board has asked for comments with respect to rate integration of the Alaska - Hawaii route. (Supplemental Order at ¶95.) The State has previously stated its view that the Commission "long ago settled the question of whether [these] routes should be rate integrated and determined they should be."^{29/} Accordingly, the State supports the tentative conclusion of the Joint Board that "rate integration should be implemented on the Alaska-Hawaii route." (Id.)

^{28/} Letter from Chairman Dennis R. Patrick to Daniel K. Inouye, Chairman, Subcommittee on Communications, Senate Committee on Commerce, Science and Transportation, dated February 24, 1989.

^{29/} Comments of the State of Alaska, filed March 10, 1987, at 2.

C. The Jurisdictional Revenue Requirement Neutrality Objective.

As discussed above, any Joint Board recommendation must recognize the impact of Joint Board action on intrastate rates and service. There can be no universal service if intrastate rates are so high as to make service unaffordable, and therefore, unavailable. The State believes, accordingly, that universal service must comprehend both intrastate rate impacts and the concept of affordability of service.

To promote affordability and to discourage increases in intrastate rates which could make universal service impossible to achieve, the State strongly supports the Joint Board's tentative conclusion that "resolution of the issues in this proceeding, including adoption of any changes in the Alaska interstate market structure, should be accomplished without generating any material increase in the intrastate revenue requirements." (Supplemental Order at ¶32.)^{30/} While there may be disagreement as to what would constitute "a material increase", the State nonetheless agrees with the principle behind the Joint Board's tentative conclusion, that actions taken in this proceeding should be based

^{30/} The Senate Committee on Commerce, Science, and Transportation has stated (in connection with rate integration) that separations policies should not create substantial shifts to the intrastate jurisdiction:

It is the intent of the Committee that any change in the prescription of separations and settlements methodologies of the noncontiguous States necessary to implement rate intergration not result in the shifting of a greater percentage of the costs of providing long distance facilities from the Federal to the State jurisdictions that [sic] is now the case.

on the jurisdictional revenue requirement neutrality objective.^{31/} To achieve such neutrality and to promote universal service, the renewed attempt by AT&T to reassign to the intrastate jurisdiction approximately \$35 to \$40 million in revenue requirements associated with Category 4.23 (formerly Category 8.23) Central Office Equipment must be firmly and explicitly rejected.^{32/}

The Joint Board has asked for comments on how to measure achievement of revenue requirement neutrality and appropriate processes for implementing and enforcing it. (Supplemental Order at ¶7C.) Given the lack of data on what the revenue requirement effects would be of adopting any new market structure,^{33/} achievement of this objective cannot be left to chance. The Joint Board must make recommendations to assure that, in fact, no material revenue requirement shifts take place.

In the past, jurisdictional revenue requirement neutrality has been achieved by such steps as freezing the interstate-intrastate percentage allocations for specific cost categories.^{34/} It may be that such an approach would be useful here, and might

^{31/} The State also believes the Joint Board correctly concluded that it "must consider the overall level of the Alaska intrastate cost allocation, not specific intrastate tariff rates." (Supplemental Order at n.55.)

^{32/} The Joint Board apparently has reached the same tentative conclusion. See Supplemental Order at ¶31 and n.59.

^{33/} See pages 20-24, below.

^{34/} MTS and WATS Market Structure, Report and Order, 2 FCC Rcd. 2639 (1987), adopting Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, Recommended Decision and Order, 2 FCC Rcd. 2551 (1987).

present a simple, clear, easy to administer method of ensuring that no revenue requirement shifts occur.

D. The Increased Efficiency Objective.

The State believes that improving efficiency is a worthwhile goal in this proceeding, if it is consistent with the Joint Board's "other public interest concerns". (Supplemental Order at ¶33.) To the State, these other public interest concerns are universal service and the related objectives discussed above.

Efficiency, however, can be determined only by viewing both interstate and intrastate markets. Telephone plant can be, and in most cases is, used for both intrastate and interstate communications. The most efficient market structure is one that maximizes the combined use of telephone plant and does not create stranded investment or involve uneconomic duplication of facilities.^{35/}

E. The Market Based Competitive Entry Objective.

The Joint Board states that it is "examining the market structure rules applicable to provision of Alaska interstate service on a competitive basis." (Supplemental Order at ¶26.) Its tentative conclusion is that the "Alaska interstate market structure should allow for market based competitive entry." (Id.) That appears to have occurred already in Alaska. All areas of Alaska served by a competing MTS provider (representing 79 percent

^{35/} See Memorandum Opinion and Order, CC Docket No. 80-584, RM-3304, FCC Mimeo 86-68 (February 25, 1986) (Bush Reconsideration I); further reconsideration denied, Memorandum Opinion and Order, CC Docket No. 80-584, RM-3304 (October 24, 1986) (Bush Reconsideration II).

of access lines statewide) have completed pre-subscription balloting^{36/} and more are scheduled to do so.

The issue for the Joint Board, therefore, is not whether to create competition; that has been done. Rather, the question is how to treat it, consistent with promotion and enhancement of universal service and maintenance of rate integration and jurisdictional revenue requirement neutrality. The Commission has previously found that competition and geographically averaged rates are neither inconsistent nor incompatible.^{37/} There are cost advantages to averaging, which could be substantial in pricing services such as MTS and WATS.^{38/} No basis has been established here for changing these conclusions, or for modifying existing rate averaging policies.

Alaska supports competition and its potential for enhancing economic efficiency and innovation. Competition is, however, a means, not an end.^{39/} It must, therefore, serve the public interest and not compromise affordable universal service.^{40/} The

36/ GCI Data Response to Supplemental Order (GCI Data Response), at 1.

37/ MTS and WATS Market Structure, 81 F.C.C.2d 177, 192-95 (1980).

38/ Id. at 193.

39/ FCC v. RCA Communications, Inc., 346 U.S. 86, 92, 94 (1953).

40/ See letter from Senator Ted Stevens to Chairman Mark S. Fowler, dated January 10, 1984 ("I support pro-competition policies, but I urge the Commission not to pursue such policies at the expense of rate integration, the rate support mechanism or universal intrastate telephone service")

steps outlined in Paragraph 27 of the Supplemental Order appear to move in the appropriate direction.

III. THE DATA RESPONSES.

The State is concerned that the data provided by the carriers are inadequate to support a decision in this proceeding. Certain data which the State believes are essential for an adequate record have not been provided. Much of the data that have been provided raise more questions than they answer. Perhaps additional data will be provided by the carriers in this round of comments. At this point, however, the record is virtually barren on many important issues.

Most significantly, no meaningful data are presented concerning the impact of either Plan A or Plan B on jurisdictional revenue requirements. Data that were presented were brief and lacking in underlying documentation. Alascom presented data, in response to the Joint Board's specific request, which provide some information on separations results under the present arrangement.^{41/} It provided very little data information on what the likely separations results would be under Plan A or Plan B. Like the Joint Board, it apparently assumed that Plan A could be or would be implemented in such a way as to create no jurisdictional cost shifts.^{42/} As to Plan B, no meaningful

^{41/} Alascom Data Response to Supplemental Order (Alascom Data Response), Response No. 11.

^{42/} Id., Response Nos. 6, 8.

separations data or analysis are provided. The other carriers, moreover, provided even less data.^{43/}

Alascom itself indicates there are substantial questions about the separations data it did provide. It states with regard to its separations data:

Alascom goes on record to caution the Joint Board that the templates provided by the Commission reflect total interstate separations of Alascom and therefore do not display the costs of the joint service arrangement with AT&T.

* * *

Alascom has concerns about the usefulness of the templates

* * *

Alascom feels that if ~~any~~ modeling is attempted by changing separations ratios, than erroneous results would occur.^{44/}

The problems identified by Alascom are compounded by the fact that much of its analysis of 1988 revenue requirements mingles together 1987 and 1988 data.^{45/} No clear view of actual 1987 or 1988 results or trends, therefore, is possible.

Moreover, the data presented by Alascom and AT&T do not always appear consistent. For example, they do not agree on the costs of providing service under alternate arrangements. Alascom estimates that adoption of Plan B would reduce its cost of

^{43/} For example, AT&T says, with respect to Plan A, that it "can not identify any difference in costs, revenues or shortfall . . . by comparison to the existing joint provisioning arrangement." AT&T Data Response to Supplemental Order, at 6. AT&T also states that "under Plan B, cost reductions are expected, but can not be precisely quantified at this time." Id. at 7.

^{44/} Id., Response Nos. 11, 12.

^{45/} Id., Response No. 8, Exhibits 1-3; Response No. 11, Exhibits 3-4; Response No. 12, Exhibit 2.

providing interstate service by \$15.3 million.^{46/} AT&T states that under Plan B \$30.9 million in costs incurred by Alascom would be avoided (\$126.6 million minus \$95.7 million).^{47/}

New questions are raised by the data responses concerning facilities improvements Alascom seeks to make. Alascom identified several major new investments. It plans to introduce a fiber optic link to connect Alaska to the Lower 48 and Japan; to launch a new satellite; to make improvements in its microwave network connecting southeastern Alaska to the Lower 48; and to make improvements in bush earth station facilities.^{48/} While supportive of technological innovation and high standards of service quality, the State is concerned about the cost of the these improvements and the manner in which these costs will be recovered. Significant increases in intrastate revenue requirements and accordingly, intrastate rates, cannot be reconciled with the statutory mandate and Joint Board objective of universal service. Additional data are needed concerning how these facilities will be used, the amount and jurisdictional type of traffic they will carry, and the amount and separations treatment of the costs at issue.

The basis for the State's concern is shown in what appears to be Alascom's proposed treatment of its satellite. The Joint

^{46/} Alascom Data Response, Response No. 8, Exhibits 1 and 3 (Cost of Analysis of Joint Service Arrangement -- 1988-1989 (showing \$177.5 million in costs under current plan arrangement and \$162.2 million in costs under Plan B)).

^{47/} AT&T Data Response at 7-8 and n.*.

^{48/} Alascom Data Response, Response No. 2 at 6.

Board's Supplemental Order clearly contemplates that Alascom's satellite would be considered a facility used for the interstate link segment in a Plan B scenario. (Supplemental Order at ¶68.) Alascom, however, does not list its existing satellite on its exhibit of facilities to be used in the interstate link segment.^{49/} This suggests that Alascom views the satellite primarily as a distribution link facility in a Plan B scenario. Such treatment concerns the State because of its potential impact on intrastate revenue requirements.

Another concern is the present lack of clarity with regard to use of the proposed fiber optic link. Alascom appears to reserve the right to use that facility for intrastate purposes, despite the fact that the facility is designed for international and interstate communications.^{50/} As Alascom acknowledges, under present separations rules, such incidental intrastate use could have the inequitable effect of greatly increasing intrastate revenue requirements.^{51/} Further information concerning the anticipated cost, uses, and separations treatment of this facility must be provided for the Joint Board to evaluate whether or how intrastate use of the fiber optic link is consistent with its objectives, particularly revenue requirement neutrality.

In short, the data responses do not provide an adequate basis for analyzing the possible consequences of adoption of either Plan A or Plan B. Should the Joint Board decide to pursue

^{49/} Alascom Data Response, Response No. 3, Exhibit 1.

^{50/} Alascom Data Response, Response No. 6, Exhibit 1.

^{51/} Id.

either of those plans (in particular, Plan B, because it differs from present arrangements to a greater extent than Plan A) additional data concerning the likely impact of such a plan will need to be developed.

IV. THE PLANS.

The Joint Board asked for comments on how the existing market structure and each of the two new plans proposed by it address the five objectives discussed above. (Supplemental Order at ¶72.) Suggested improvements to the Joint Board's plans and the present market structure are also requested. (Id. at ¶¶73-74.) In this section, the State responds to these requests.

As an initial matter, it must be noted that only the most preliminary comments concerning the Joint Board's new plans are possible. The plans themselves, as the Joint Board undoubtedly realizes, are skeletal. The actual impact of either plan (particularly Plan B) is difficult to predict with any precision. In addition, the price cap proposal adopted by the Commission on March 16, 1989 could have extraordinary impact on this proceeding.^{52/} Nonetheless, in an effort to respond to the Joint Board's request, the State submits these general comments, but reserves the right to reassess its comments in light of further data and more complete information about the price cap proceeding.

^{52/} Although the Commission has adopted a price cap plan, its order implementing that plan, rumored to be approximately 500 pages in length, has not yet been released. The State has reviewed the Commission's public releases on its decision and bases these comments on those releases. Nonetheless, much about the Commission's price cap plan is unknown, in particular, how and to what extent it applies to Alascom and how it will affect Alaska service provisioning.

It may also be necessary for the Joint Board to ask for further comments from the parties once the price cap order is available and there is an opportunity for the Joint Board and the parties to analyze it.

A. Present Market Structure.

Although not perfect, the present market structure furthers the objectives the State believes are most important in this proceeding. Present service arrangements can address effectively universal service concerns and have resulted in achievement for Alaska of full rate integration. Because the costs and revenues of providing message toll service to and from Alaska are combined with the costs and revenues of providing such service to and from other states, present arrangements assure the continuation of rate integration and geographic rate averaging with respect to Alaska. And, by definition, the present market structure best achieves the objective of revenue requirement neutrality. Intrastate revenue requirements under the present market structure form the baseline against which other plans are (and must be) measured.

(Supplemental Order at ¶31.) Lastly, as noted above, under the present market structure, interstate message toll competition has come to most of Alaska.^{53/}

^{53/} It appears that the market share of the dominant carrier in Alaska in the market of interstate toll calls originating in Alaska is no greater than the market share of the dominant carrier in the Lower 48 in the market of interstate toll calls originating in the Lower 48. Compare Alascom Data Response, Response No. 9, Exhibit 1 (showing approximately 22 million minutes per month of interstate calling originating in Alaska with GCI Data Response, Section III (showing approximately 10 million minutes per month of interstate calling originating in Alaska). Thus, it appears that the
(Fn. continued)

In short, there has been no showing that the present system is irremediably defective. While maximizing the objectives of universal service, rate integration and revenue requirement neutrality, the present arrangement has allowed competition to develop and has not placed unfair or undue burdens on AT&T or any other party. (See Supplemental Order at ¶25 and n.39 and discussion at pages 11-15, above.) The challenge for the Joint Board is to improve the present market structure or to develop an alternative that satisfies these objectives as well.

The State believes that improvements to the present market structure can and should be made. The key to improving the present arrangement, however, is to focus on that aspect of it that is of greatest concern to the Joint Board -- that it encourages inefficiency and may be competitively unfair -- and not to throw the universal service baby out with the claimed inefficient and competitively unfair bathwater.

The State suggests that the Joint Board alter the present service arrangement in a manner that gives Alascom more clear incentive to reduce investments and costs and become more efficient.^{54/} This incentive could be created by changing the manner by which Alascom is compensated by AT&T. The Joint Board describes and criticizes the AT&T/Alascom relationship as like a "cost plus percentage" contract. (Supplemental Order at ¶58.)

(Fn. continued)
market share of the dominant carrier in Alaska is less than 70 percent.

54/ Such an alteration would appear to be consistent with the Commission's as yet unreleased price cap order, which seeks to create those same incentives for AT&T.

Alascom is guaranteed reimbursement of all prudent costs and a rate of return on its prudent investment, and, therefore, the Joint Board notes, Alascom may have little reason to control costs and may have incentives to increase its rate base. (Id.)

The Federal Government has recognized these same attributes in "cost plus percentage" contracts and has developed an alternative which creates an incentive in favor of efficiency. The State believes this alternative would be useful here. Rather than "contracting" with Alascom on a "cost plus percentage" basis, AT&T should "contract" with Alascom on a "cost plus incentive fee" basis.^{55/} A target cost for Alascom's portion of the jointly provided service would be arrived at through Commission processes.^{56/} A separate fee for Alascom that would be designed to provide it a reasonable profit would also be established.

Reimbursement of all prudent costs would be allowed, even if those costs exceed the agreed upon target. The fee (or profit) for Alascom, however, would be reduced by some amount in the event costs exceed the target. For example, the fee might be reduced by an amount equal to 20 percent of the excess costs.^{57/} Assume the cost target was \$100 million and the negotiated fee was \$25 million. If costs exceeded the target by \$15 million, Alascom's fee (or profit) would decline by 20 percent of that amount (or \$3

^{55/} See Federal Acquisition Regulations § 16.404-1 (48 C.F.R. § 16.404-1) concerning a cost plus incentive fee (or "CPIF") contract.

^{56/} This cost could be fixed at an absolute level, or could be based on a formula that contains variables such as usage.

^{57/} There is, of course, nothing magical about a 20 percent figure. It is used only as an example.

million) so that it would receive \$22 million in profit. The incentive arrangement would work in the other direction as well. The incentive fee for Alascom would be increased by some amount in the event costs were less than the target amount.^{58/} Using the same 20 percent incentive factor, \$100 million target cost, and \$25 million negotiated fee, assume actual costs were \$85 million. In that event, Alascom's profit would be increased by \$3 million (20 percent of the \$15 million differential between target and actual costs) to \$28 million.

There would be significant benefits from such a system. First, it would give Alascom a clear incentive to become more efficient, to the benefit of itself, AT&T, the ratepayers and shareholders of both, and the public interest.^{59/} Any incentive to invest merely to compete unfairly would be reduced, enhancing competition. Second, the benefits of increased efficiency would be shared. In the examples above, 80 percent of the financial benefits of increased efficiency would revert to AT&T. This increased efficiency would reduce AT&T's nationwide costs for providing interstate message toll service, and all AT&T's ratepayers would benefit as well.

Third, this improvement to the system should further universal service and related objectives by reducing costs, and do

^{58/} The incentive factor for costs below the target would not have to be the same as the incentive factor for costs in excess of the target, though there is some logic for using the same factor.

^{59/} The higher the percentage applied to the differential between target and actual costs (20 percent in the examples above), the greater the incentive would be.

so in a manner consistent with the Commission's price cap plan. Rate integration would be maintained and it does not appear that revenue requirement shifts would occur.^{60/}

Fourth, this approach provides for more stability in the market than would occur if either Plan A or Plan B were implemented. In light of the enactment of price caps, an entirely new method of regulation, there may be substantial benefits in not implementing a radically new market structure in Alaska. Changing too many aspects of market structure and regulation at once may make it impossible to monitor or evaluate the effects of any one change.^{61/}

B. Plan A.

The Joint Board's proposed Plan A has much to recommend it, although it has certain key defects. Despite the fact that it changes the present service provisioning arrangements, it maintains many of the desirable economic aspects of those arrangements. AT&T is required to use Alascom's facilities to complete Alaska-bound calls originating in the Lower 48, and to accept from Alascom interstate calls originating in Alaska. The point of interconnection between the carriers remains in the Lower 48. AT&T would not be permitted a point of presence in Alaska.

^{60/} If necessary, policies and other appropriate restrictions might have to be adopted to make sure that interstate service costs were not reduced merely by shifting costs to the intrastate jurisdiction.

^{61/} As Congressman Markey has noted, "[T]he full impact of the price cap proposal on telephone service, especially for residential customers and rural users, is still unknown." 135 Cong. Rec. E943 (daily ed. March 22, 1989).

Although the description of Plan A is skeletal, and the relationship of the data submitted to the impact of Plan A is not now clear, Plan A appears far more consistent with the objectives the State believes the Joint Board should emphasize than Plan B would be. Alascom's state-wide network would continue to be used by AT&T, thus assuring service throughout the state without the need for duplicative facilities, particularly in the most rural locations. AT&T would continue to be responsible for ensuring interstate service in Alaska at rate integrated levels and the costs of such service would be recovered by AT&T through nationwide averaged rates. (*Id.* at 166.)

Because (1) AT&T would continue to use Alascom facilities, (2) the point of interconnection between the carriers would be unchanged, and (3) AT&T would not have a point of presence in Alaska, it would appear that revenue requirement shifts would not be significant. Although the State preliminarily believes the Joint Board and Alascom may be correct in this regard, it is not willing merely to assume that no cost shifts would occur and urges that data on this point be developed and considered.

One major distinction between the arrangements and Plan A is that Plan A would replace the present relationship between AT&T and Alascom with a tariff-based relationship. This tariff arrangement would, as the Joint Board undoubtedly intends, ensure use of standard tariff procedures for evaluation of Alascom's costs. Using standard tariff procedures, the result might be

lower costs than would be the case under the existing arrangement.
(Id. at ¶ 65.)^{62/}

Plan A does take steps to further competition in the Alaska interstate communications market. In permitting other common carriers (OCCs) to have points of presence in the State, Plan A encourages market entry.

Plan A also appears more efficient than Plan B. Unlike Plan B, Plan A should not result in a large decline in the relative interstate use of Alascom's jurisdictionally joint facilities, thus maximizing the efficient use of those facilities. Because it is less likely to result in the construction of duplicative distribution facilities in Alaska, Plan A is more consistent with the realities of the Alaska marketplace than is Plan B, and more efficient.

Plan A, however, does raise some serious concerns for the State. First, it is not clear that the cost recovery system that the Joint Board apparently envisions is consistent with its objectives. The Joint Board states that Alascom should charge rates that approximate costs on "competitive routes."

(Supplemental Order at ¶ 65.) Separating "competitive rates" (whatever routes that term encompasses) from other routes is unwise. This appears to contemplate deviation from cost averaging in a manner inconsistent with geographic rate averaging and other universal service concerns, to the detriment of residents of high cost areas, and the public interest.

^{62/} As noted above, it is unclear how, and to what extent, the Commission's rate cap procedure will apply to Alascom, and how the price cap proposal would affect Plan A.

Second, Plan A's division of carrier of last resort responsibilities between Alascom and AT&T is troublesome. (Id. at 11 64-65.) The effects of that divided responsibility are not clear. Oftentimes, divided responsibility is no responsibility. The last complication the State needs in times of emergency, for example, is an unclear division of responsibility.

C. Plan B.

The State has grave concerns about Plan B, particularly given the state of the record in this proceeding. Plan B involves complex, multiple, phased changes, although most are only barely described. Plan B would fundamentally change the Alaska interstate market (and would create changes in the intrastate market as well). The data needed to evaluate those changes do not exist and many of the decisions that would be of critical importance to the State (such as the development of various cost allocation rules) would not be made until after Plan B was adopted. For this reason, as well as others discussed below, the State opposes Plan B. The State cannot risk the future of Alaska telecommunications on a plan that would be implemented without any informed understanding of what would eventually occur.

As noted in Section III of these comments, there are virtually no data to evaluate the potential revenue requirement shift that would be created by Plan B. Perhaps it is impossible to obtain such data because there are too many unknowns in the plan. Such unknowns would include, for example, how many points of presence AT&T would establish; how AT&T would distribute traffic within Alaska; how much interstate traffic would continue

to be carried on Alascom's distribution network; where the line between Alascom's interstate link and distribution segments would be drawn; how carriers' costs would change; whether Alascom would enter the interstate market in competition against AT&T and GCI.^{63/}

Some information on some of these issues is present in the record, but it is at best impressionistic and not susceptible to meaningful analysis. The difficulty of knowing these unknowns, however, does not remove the requirement for reasoned decision-making. If the Joint Board and Commission do not know the consequences of a regulatory option, that option cannot and should not be selected.

Plan B does not seem likely to promote the objectives the State believes the Joint Board should advance in this proceeding. It seems likely to reduce use of Alascom's physically intrastate network, thus putting upward pressure on Alascom's intrastate rates, contrary to the universal service objective. Although interstate carrier of last resort responsibility is placed on AT&T alone, intrastate carrier of last resort responsibility remains with Alascom, again raising concerns about divided responsibility (as well as efficiency). Moreover, AT&T provides no meaningful information concerning how it would discharge this responsibility.

Plan B also creates risks of significant known and unknown revenue requirement shifts. A key aspect of Plan B is that it would permit AT&T to have one or more points of presence in

^{63/} Alascom appears to conclude it would, under Plan B, no longer participate in the interstate market. Alascom Data Response, Response No. 6 at 5.

Alaska. The State has long been concerned that such a change in the method by which service is provided could have a significant jurisdictional cost shift. In the CC Docket No. 80-286 Joint Board proceeding (as well as in this proceeding), AT&T has contended that, because the point of interconnection between Alascom and AT&T is in the Lower 48, Alascom under present separations rules allocates \$35 to \$40 million in Category 4.23 (formerly Category 8.23) expenses to the interstate message toll service which, AT&T believes, should be allocated elsewhere. Alascom's separations data in its data response confirm the continued existence and relatively unchanged magnitude of this cost.^{64/}

The CC Docket No. 80-286 Joint Board and the Commission concluded AT&T was wrong and explicitly decided to maintain Alascom's separations treatment of former Category 8.23 expenses.^{65/} That decision should not be undone here. Given that there are only about 250,000 access lines in Alaska, a \$35 to \$40 million annual cost shift could result in an increase in intrastate revenue requirements by approximately \$140 to \$160 per line per year. A shift of such an unprecedented amount cannot be squared with universal service concerns. Different aspects of Plan B could create other cost shifts as well, and such shifts must not be allowed to occur. The Joint Board's objectives of universal service and revenue requirement neutrality require no less.

^{64/} Alascom Data Response, Response No. 11.

^{65/} See n. 34, above.

Plan B also involves putting the cart before the regulatory horse. Under this proposal, Plan B would be adopted before fundamental decisions concerning cost allocation rules and implementing proposals are made. Regulatory oversight and involvement would continue for years to resolve fundamentally important questions. The Joint Board admits that after the plan is adopted, "[c]ost allocation rules would have to be developed to allocate Alascom's investment and expenses between these two [distribution and interstate link] segments." (Supplemental Order at ¶68.) It also acknowledges that "Alascom and AT&T would be required to file engineering and cost allocation proposals reflecting their plans for implementing the new market structure." (*Id.* at ¶70.) Although these rules and proposals would presumably be finished prior to actual implementation of Plan B, they would not be finalized prior to a Joint Board commitment to implement that plan. The State cannot endorse a plan based on such uncertainty.

V. CONCLUSION.

The State urges the Joint Board to prioritize the objectives in this proceeding in the manner set forth in these Comments. It also requests the Joint Board to consider the

CERTIFICATE OF SERVICE

I, Linda K. Smith, do hereby certify that, on April 13, 1988, I have caused to be sent a copy of the foregoing "Comments of The State of Alaska In Response To The Supplemental Order Inviting Comments" by United States mail, postage prepaid, to the following:

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5-15-89

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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Federal Communications Commission
Office of the Secretary

In the Matter of)
)
Integration of Rates and Services)
for the Provision of Communications)
by Authorized Common Carriers)
Between the Contiguous States and)
Alaska, Hawaii, Puerto Rico and)
the Virgin Islands)

CC Docket No. 83-1376

RM 4436

TO: THE FEDERAL-STATE JOINT BOARD

REPLY COMMENTS OF THE STATE OF ALASKA
IN RESPONSE TO THE SUPPLEMENTAL
ORDER INVITING COMMENTS

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TO: THE FEDERAL-STATE JOINT BOARD

REPLY COMMENTS OF THE STATE OF ALASKA IN
RESPONSE TO THE SUPPLEMENTAL ORDER INVITING COMMENTS

The State of Alaska ("Alaska" or "the State"), by its attorneys, hereby submits its reply comments pursuant to the Supplemental Order Inviting Comments, FCC 88J-4, released January 3, 1989 ("Supplemental Order") in the above-captioned proceeding.

As a preliminary matter, the State notes that the comments submitted by the parties have been helpful in crystallizing the objectives for this proceeding. They have been less helpful, however, in presenting a clear and specific picture of how the Joint Board's proposed plans would be implemented and what the consequences of those plans would be. Theories and ideas, but very little predictive data, have been presented. As a result, it is not possible to predict the specific impact of alternative proposals.

I. SUMMARY

The Joint Board has correctly identified and ranked the objectives in this proceeding. With only one exception, the comments of the parties, both those from Alaska and those with nationwide or other constituencies, support the Joint Board's approach. Universal service, with the related goals of rate integration and revenue requirement neutrality, must be given the highest priority. Enhanced efficiency and competition, while worthwhile objectives, should not, as the Joint Board noted, be implemented at the expense of these top priority goals. These latter goals can be adequately promoted by addressing economic incentives, either by the method the State proposed in its prior comments or by another method. More wholesale changes, such as those envisioned by Plan B, are not necessary.

Implementation of the Joint Board's objectives should not include reversal of the decision by the Commission and a sister Joint Board concerning the separations treatment of the costs of Category 4.23 central office equipment. It should, however, include appropriate steps to freeze separations to maintain jurisdictional revenue requirement neutrality.

There has been no showing that adoption of Plan B would be in the public interest. The record does not support adoption of Plan B. Critical data have not been submitted, and claimed advantages of Plan B are unsubstantiated. It is not now possible to determine how Plan B would be implemented by the carriers, or to

assess its impact. Uncertainty is heightened by the fact that cost allocation rules and implementing proposals would be left for further proceedings.

Arguments in favor of Plan B have previously been addressed and found wanting. For example, costs of Alaska service are recovered in the current nationwide rates for service, so there is no failure to compensate carriers. There has not been any showing of competitive harm. In addition, arguments relying on competitive impact are undercut by the new price cap procedures. Further, the proposal for an Alaska only special fund for high cost areas is inconsistent with national geographic rate averaging and the nondiscrimination provisions of the Communications Act. The proposed special fund is based on a premise that does not appear consistent with the facts, that is, that interexchange service in Alaska is equivalent to local exchange service in the Lower 48.

Plan A, while it has positive features, should be modified and should address the issue of incentives to promote economic efficiency. Other proposals are also worthwhile exploring further, to determine whether one, or a combination of several, incentive based proposals could be a workable approach to resolve the issues in this proceeding.

II. THE JOINT BOARD HAS CORRECTLY IDENTIFIED AND PRIORITIZED THE OBJECTIVES.

A. The Identification and Prioritization of Objectives.

In its Supplemental Order, the Joint Board identified five objectives to guide its resolution of this proceeding: (1) continuation of rate integration; (2) market based competitive entry; (3) preservation of universal service; (4) jurisdictional revenue requirement neutrality; and (5) increased efficiency. (Supplemental Order at ¶¶ 24-34.) It emphasized that preservation of universal service and the related objectives of rate integration and revenue requirement neutrality must be given primary importance:

In particular, we emphasize that measures to increase efficiency and promote market based competitive entry should not be implemented at the expense of universal service, rate integration or revenue requirement neutrality.

(Supplemental Order at ¶ 24.)

The State believes that the Joint Board's prioritization of objectives is not only correct, but also compelled by the Communications Act of 1934, as amended, and federal communications policy as established by Congress and the Commission.¹ Every party submitting comments in response to the Supplemental Order, except AT&T, agrees with the Joint Board on this prioritization of objectives.

¹ See generally Comments of the State of Alaska in Response to the Supplemental Order Inviting Comments at 4-20 (April 13, 1989) ("Alaska Comments").

Alascom explicitly endorsed the Joint Board's prioritization and added:

The massive record accumulated to date leaves little doubt as to the critical importance of universal service, continuation of rate integration and avoidance of jurisdictional cost shifts for the Alaska market.²

The Alaska Telephone Association ("ATA"), representing the twenty-two local exchange companies in Alaska, strongly endorsed the goals of universal service, rate integration and revenue requirement neutrality.³ It noted that it had "previously demonstrated that cost assignment to the intrastate jurisdiction in Alaska is not disproportionately low in comparison with other geographical areas," and that other separations rule changes are likely to increase intrastate cost allocations by approximately \$73 per access line per year.⁴ ATA noted that further cost shifts to the intrastate jurisdiction must be avoided because they would create excessive burdens on intrastate ratepayers.⁵

United Utilities, Inc. ("United") stated its strong concurrence in the Joint Board's prioritization of the universal service, rate integration and revenue requirement objectives.

These objectives are fundamental to the continued availability of reliable communications in Alaska. Having access to telephone service has helped to save lives, improve medical care, allowed business to function and

² Comments of Alascom, Inc. at 4 (April 13, 1989) ("Alascom Comments").

³ Comments of the Alaska Telephone Association (April 13, 1989) (ATA Comments).

⁴ Id. at 3-4.

⁵ Id. at 4-5.

has brought isolated residents in touch with the rest of the world.⁶

The Joint Board's primary objectives are also supported by local exchange telephone companies throughout the United States. Small telephone companies, through the Organization for the Protection and Advancement of Small Telephone Companies ("OPASTCO"), understood the far reaching implications of the questions before the Joint Board. OPASTCO emphasized the need for rate integration and the established legal basis for it.⁷ It also noted the connection between universal service and geographic rate averaging and revenue requirement neutrality.⁸ Universal service and rate integration, OPASTCO said, must be given the greatest weight by the Joint Board.⁹

The United States Telephone Association ("USTA"), representing the local telephone company industry, agreed. Rate integration, it said, should not be abandoned and universal service, of which rate integration is a part, is of the utmost

⁶ Comments of United Utilities, Inc. at 2 (April 13, 1989) ("United Comments"). In addition, if the revenue requirement neutrality objective is to be achieved, United said it must be permitted to continue to use the frozen conversation minute mile factor in separating central office equipment Category 4.23 (formerly Category 8.23) costs. Id. at 2-3.

⁷ Comments of the Organization for the Protection and Advancement of Small Telephone Companies at 2-4 (April 13, 1989) ("OPASTCO Comments").

⁸ Id. at 4-5.

⁹ Id. at 6.

importance.¹⁰ USTA also stated that revenue requirement shifts must be kept to a minimum.¹¹

The State of Hawaii also supported the Joint Board's prioritization of objectives.¹² In particular, Hawaii stated that rate integration is a fundamental component of national telecommunications policy and is not subservient to competition.¹³

GCI, long a vigorous proponent of competition, agreed that maintenance of rate integration should be one of the ultimate objectives of this proceeding.¹⁴ It also stated support for universal service¹⁵ and its belief that revenue requirement neutrality should be attained, at least for MTS services.¹⁶

AT&T stands alone in its objection to the Joint Board's prioritization of objectives, citing competition and efficiency as more important objectives than universal service, rate integration and revenue requirement neutrality.¹⁷ Taken to its extreme, if accepted, AT&T's view of the proper prioritization of objectives,

¹⁰ Comments of the United States Telephone Association at 2-3 (April 13, 1989) ("USTA Comments").

¹¹ Id.

¹² Comments of the State of Hawaii at 5-6 & n.8 (April 13, 1989) ("Hawaii Comments").

¹³ Id. at 5.

¹⁴ Comments of General Communication, Inc. at 5 (April 13, 1989) ("GCI Comments").

¹⁵ Id. at 7.

¹⁶ Id. at 9.

¹⁷ Comments of American Telephone and Telegraph Co. at 7 (April 13, 1989) ("AT&T Comments").

however, would be inconsistent with the universal service mandate of the Communications Act. As the Commission (through the Chief of the Common Carrier Bureau) recently noted, "The Commission's overriding responsibility is not to foster the maximum level of competition in the industry it oversees, but to promote the public interest."¹⁸ Universal service is one of the public interest objectives the Commission must promote.¹⁹ Also, the Commission has repeatedly made clear that rate integration -- treating all areas of the country, including off-shore areas, alike -- is a primary goal and is mandated by the nondiscrimination requirements of the Communications Act.²⁰

Were AT&T's approach adopted, Alaskans (and others in other states) not only might no longer pay nationally averaged rates, but also might be forced to take second class telephone service. For example, AT&T stated its intention not to provide in Alaska the full panoply of telecommunications services which AT&T and others are marketing vigorously in the Lower 48, such as Integrated Services Digital Network ("ISDN") services and Common Signaling System 7 ("CCS7") capability.²¹ It suggests that it

¹⁸ In re Request of McCaw Cellular Communications, Inc., File No. 23333-CD-TC-1-89 et al., Memorandum Opinion and Order, DA 89-356 (released April 4, 1989).

¹⁹ 47 U.S.C. § 151.

²⁰ See Alaska Comments at 12-13; Hawaii Comments at 5-10.

²¹ AT&T Comments at 9, 19.

might not provide modern technology to Alaska unless the Joint Board recommends adoption of Plan B.²²

The Communications Act, however, requires that service be provided in a nondiscriminatory manner. It is "unlawful for any common carrier to make any unjust or unreasonable discrimination in charges, . . . facilities, or service."²³ Thus, facilities and service differentials made on the basis of geographic location are prohibited, just as rate differentials are proscribed. As the State of Hawaii notes, off-shore (as well as on-shore) points are entitled to the full benefits of this nation's telecommunications technology.²⁴ The Commission, in fact, has recently confirmed to AT&T, through rejection of a tariff, that geographic restrictions on provision of service to similarly situated customers are illegal.²⁵

B. Questions with Respect to Implementation
of the Objectives.

As most commentators recognize, the Joint Board's primary objectives can be attained only by taking steps to stabilize

22 Id. at 19.

23 47 U.S.C. § 202(a).

24 Hawaii Comments at 5-8.

25 FCC News, "AT&T Tariff 12 Offering Found to be Unlawful," CC Docket 87-568, Report No. DC-1393 (April 12, 1989). As AT&T has noted elsewhere, rejecting a tariff is an extreme remedy which the Commission adopts only when a tariff is prima facie unlawful in that it conflicts with the Communications Act or a Commission rule, policy or order. Reply of the American Telephone and Telegraph Company, Transmittal No. 1555 at 5 and n.* (April 24, 1989).

separations.²⁶ AT&T takes a different approach. It seeks to have the method by which Alascom separates central office equipment Category 4.23 (formerly Category 8.23) costs changed, claiming that current separations procedures result in the improper allocation to the interstate jurisdiction of approximately \$40 million.²⁷ As the Joint Board well knows, however, a sister Joint Board and the Commission have already explicitly rejected the arguments AT&T has raised here.²⁸ AT&T has offered this Joint Board no new facts or arguments to justify reversal of these recent decisions, and no such facts or arguments exist.²⁹

²⁶ Alaska Comments at 16-18; Alascom Comments at 6; GCI Comments at 8, 9; ATA Comments at 3-5; United Comments; OPASTCO Comments at 5.

²⁷ AT&T Comments at 15-16, 29-34.

²⁸ MTS and WATS Market Structure, Report and Order, 2 FCC Rcd. 2639 (1987), adopting Amendment of Part of the Commission's Rules and Establishment of a Joint Board, Recommended Decision and Order, 2 FCC Rcd. 2551 (1987).

²⁹ AT&T contends that Commission approved separations procedures improperly subsidize Alascom's private line and intrastate MTS/WATS services. AT&T Comments at 29-34. This contention has not only been explicitly rejected by the Commission, but is misleading. The costs of equipment commonly used for multiple services are not nearly as easily divisible as AT&T implies. There is no precise mathematical formula that can perfectly separate these costs in the "proper" manner. Separations issues necessarily involve universal service and other policy concerns as well as economic considerations. Jurisdictional Separation Procedures, Federal State Joint Board Recommended Decision, 48 Fed. Reg. 46,556, 46,564 (1983). See Gasel, Development of Separations in the Telephone Industry, Institute of Public Utilities, Michigan State University at vii; Separations Procedures in the Telephone Industry; The Historical Origins of a Public Policy, Harvard University Program on Information Resources, Policy Publication (P-77-2) (1977). See also Comments of the State of Alaska, CC Docket No. 83-1376 at 19-24 (Nov. 28, 1986). AT&T's contention that the questioned separations

[Footnote continued on following page]

Like Alaska, GCI contends that further steps need to be taken to assure that cost shifts to the intrastate jurisdiction do not occur.³⁰ It suggests that the Joint Board define and freeze the dollar amount of costs which will be assigned to the intrastate jurisdiction.³¹ The State has made an analogous proposal, suggesting that separations percentages (rather than dollar amounts) be frozen.³²

GCI correctly recognizes the need to address separations. Under GCI's proposal, both the full burden of cost increases and the full benefit of cost decreases would accrue to the interstate jurisdiction. The State hopes that incentive mechanisms and new technologies will result in efficiencies and lower costs. If lower costs do result, the effect of GCI's proposal would be to prevent the benefits of those lower costs from flowing to intrastate ratepayers. If lower costs do not result, freezing separations percentages would provide for a shared responsibility among the jurisdictions for cost increases, which appears more equitable than imposing that burden on one jurisdiction alone. In either event, the State believes its proposal to freeze

[Footnote continued from previous page]
procedures improperly subsidize private line and intrastate MTS/WATS service is, at bottom, no more than a continuing disagreement with the Commission on how such costs should be separated.

30 GCI Comments at 9.

31 Id.

32 Alaska Comments at 17-18.

separations percentages is preferable to the proposal to freeze dollar amounts.

As stated in its comments, the State noted that the objectives of enhanced efficiency and competition are worthwhile.³³ The Joint Board should not lose sight of the fact, however, that these goals should not, as it stated, be implemented at the expense of universal service, rate integration or revenue requirement neutrality. (Supplemental Order at ¶ 24.)³⁴

The State believes that competition and efficiency can be furthered, without sacrificing the essential public interest goals discussed above, by addressing economic incentives. Others agree. Alascom's concurrence is reflected in its incentive proposal, the Alascom Rate Cap ("ARC") plan.³⁵ GCI says that competition can be furthered if present service arrangements are changed to give Alascom responsibility for its own interstate costs.³⁶ Similarly, both GCI and AT&T state that efficiency problems are caused by the present nature of Alascom's relationship with AT&T.³⁷ Changing the economic incentives associated with current arrangements -- for example, by tying Alascom's profits to cost reductions, as the

³³ Id. at 18-19.

³⁴ See FCC v. RCA Communications, 346 U.S. 86 (1953); McCaw Cellular Communications, Inc., supra.

³⁵ Alascom Comments at 11-22.

³⁶ GCI Comments at 7.

³⁷ GCI Comments at 9; AT&T Comments at 17.

State suggested in its comments³⁸ -- would promote cost responsibility, efficiency and further competition.

III. PROPOSERS OF PLAN B HAVE FAILED TO SHOW THAT IT IS IN THE PUBLIC INTEREST.

The parties supporting Plan B have failed to show that adoption of it would be in the public interest, or would maximize the objectives selected by the Joint Board.

A. The Record Is Inadequate to Support Adoption of Plan B.

As the State discussed in its comments,³⁹ there are insufficient data in the record on which to base a decision to adopt Plan B. The State had hoped that the carriers would have submitted additional data on April 13, 1989, in response to the data submissions of February 27, 1989. As the State noted in its April 13 comments, information critical to the evaluation of Plan B was missing.⁴⁰ The inadequacies in the record before comments were filed on April 13, 1989 remain today.

Carriers supporting Plan B have not presented data on which a reasoned decision to implement Plan B could be based, nor even described how Plan B would be addressed by their serving arrangements. Accordingly, on the basis of the record, the Joint Board and Commission could not know what the impact of adopting Plan B would be. For example, there is no information on whether or how AT&T would satisfy the carrier of last resort

³⁸ Alaska Comments at 26-29.

³⁹ Id. at 24-25, 32-35.

⁴⁰ See, e.g., id. at 23-26.

responsibility Plan B would place on it, nor what its service configuration would be. There are no data on what the separations, revenue or traffic effects of Plan B would be. As the State has already noted,⁴¹ under Plan B important decisions concerning cost allocation rules and implementing proposals would be left for a later date, thus heightening the number and degree of unknown effects such a plan would create.

The claimed advantages of Plan B remain unsubstantiated and the manner in which Plan B would be implemented remains unknown. No cost savings from Plan B have been demonstrated.⁴² AT&T, five years after this proceeding began, has not set out the implementation scenario and cost savings that could be achieved under a plan which is substantially similar in relevant respects to the "Class 4 down" proposal it has long championed.⁴³

B. Plan B's Proponents Merely Repeat Dated Arguments That Have Already Been Discredited.

Plan B's proponents merely repeat arguments that are dated and have been discredited. Other parties, however, have come forward with new ideas based on incentive regulation.

AT&T argues that Plan B corrects what it perceives as unfairness to it. As the Joint Board has correctly noted, AT&T is compensated fully for Alaska service because it recoups all of its costs incurred in providing service under the present market

⁴¹ Id. at 35.

⁴² See Alascom Comments at 27.

⁴³ See AT&T Comments at 21.

structure by including such costs in its nationwide revenue requirement. (Supplemental Order at ¶ 25 and n.39.) Service to high cost areas at geographically averaged rates is balanced by the ability to charge the same rates in low cost areas. That is the essence of rate integration and nationally geographically averaged rates. Thus, as the two national telephone organizations submitting comments noted,⁴⁴ contentions that there is an improper subsidy funded by AT&T⁴⁵ are wrong.⁴⁶

Arguments by Plan B's proponents that a separate funding mechanism to support service to high cost areas of Alaska have also been rejected. AT&T's "Alaska Rural Service Fund",⁴⁷ is no different than its "Alaska Rural Fund," an approach which the Joint Board had available to it and did not propose. (Supplemental Order at ¶ 60.) Such a fund is not consistent with the nondiscrimination provisions of the Communications Act.

⁴⁴ OPASTCO Comments at 3; USTA Comments at 2.

⁴⁵ See AT&T Comments at 14; GCI Comments at 6.

⁴⁶ The gravamen of AT&T's concern appears to be that inclusion of the cost of serving Alaska (and other high cost areas) in its rate base, and accordingly in its service rates, makes it less competitive with other interexchange carriers. AT&T has provided no evidence, however, to support its contention that its competitive position with respect to other interexchange carriers is being harmed. Supplemental Order at ¶ 25 and n.39. In any event, the relevance of this argument is undercut by new price cap procedures, in which AT&T is given some flexibility to lower nationwide geographically averaged rates. Furthermore, competitive impact, even if substantiated, is not a justification for undermining national geographic rate averaging.

⁴⁷ See AT&T Comments at 25-29.

A special Alaska only fund would still move the obligation to cover the costs of serving high cost areas from AT&T -- in whose revenue requirement such costs are already included -- to others. It would still create a dangerous precedent by removing certain areas of the country from AT&T's unified cost pool for interstate MTS/WATS service, and thus would undermine national geographic rate averaging. And it would still create a separate fund for a special purpose which would be subject continuously to questioning and attack, and thereafter, to an ongoing need to defend the fund in repeated proceedings.⁴⁸

Furthermore, AT&T's proposal is still based on a Universal Service Fund/NECA model which appears inappropriate. Alascom is not a local exchange carrier ("LEC").⁴⁹ The Commission appears to have decided that NECA cost support is available only to LECs, and is not available to interexchange carriers, even when they resemble LECs.⁵⁰ Thus there appears no foundation for this approach. The complicated nature of the rule changes AT&T proposes to force an interexchange carrier into an exchange carrier mold confirms the inappropriateness of the AT&T approach.⁵¹

48 See Reply Comments of the State of Alaska, CC Docket No. 83-1376 at 10-16 (March 27, 1987), for more discussion of such special funds.

49 Alascom Comments at 27.

50 In the Matter of The Offshore Telephone Co., 3 FCC Rcd. 4137 (1988).

51 See AT&T Comments at Attachment II. GCI's separate fund approach fails for the same reasons. See GCI Comments at 29.

IV. PLAN A AND OTHER ALTERNATIVES TO THE PRESENT MARKET STRUCTURE ARE WORTH EXPLORING.

As noted in its comments,⁵² the State believes that Plan A, while it has certain positive features, must be modified. To satisfy universal service and related objectives, Plan A should be modified to provide that the costs of service from the point of interconnection out to all Alaskan locations should be averaged in the tariff under which AT&T would obtain service from Alascom.⁵³

The attacks on Plan A by AT&T and GCI largely ignore the fact that their preferred alternative is unsupported and contrary to the primary public interest objectives identified by the Joint Board, for the reasons set forth above.⁵⁴ Plan A, however, is criticized for doing little to change Alascom's incentives to promote enhanced competition and efficiency.

The State agrees with this criticism. The Commission's new price cap order⁵⁵ is suggestive of other mechanisms that could be

52 Alaska Comments at 29-32.

53 Thus, the State disagrees with Alascom's view that, under Plan A, the costs of Alaskan service from the Class 4 office out to all locations other than the three major cities should be averaged. See Alaska Comments at 31; Alascom Comments at 33. The State also disagrees with Alascom's contention that Plan A treats Alascom like an LEC. Alascom Comments at 27, 29. There is no more reason to view Plan A as analogous to an LEC access tariff than an end-on-end interexchange service tariff.

54 See pages 13-16, supra.

55 Policy and Rules Concerning Rates for Dominant Carriers, Report and Order and Second Further Notice of Proposed Rulemaking, CC Docket No. 87-313, FCC 89-91 (released April 17, 1989).

employed to create incentives to promote efficiency and competition without harming universal service and related goals.⁵⁶ The price cap order is approximately 500 pages in length and must be carefully reviewed by the Joint Board and the parties to determine how it affects this proceeding and the proposals put forward in it.⁵⁷

It appears that the proposals put forward by the State and Alascom, while very different, address the concerns about incentives in ways that seem consistent with price caps. As noted in its comments, the State believes that its cost plus incentive fee proposal,⁵⁸ if adopted, would give Alascom clear incentives to be efficient in a manner that would promote fair competition. This proposal could be implemented in conjunction with certain aspects of Plan A (for example, allowing OCCs to have points of presence in Alaska, although AT&T would still interconnect with Alascom in the Lower 48) to further enhance the efficiency and

⁵⁶ Another new development is the proposal of the Municipality of Anchorage to sell its local telephone system, the Anchorage Telephone Utility ("ATU"). An RFP has been announced, with the last round of submissions due on July 22, 1989.

⁵⁷ Footnote 197 of the Price Cap Order appears to state that the benefits of price caps will flow to Alascom's interstate MTS/WATS ratepayers because Alascom's MTS/WATS rates are set at levels that are equal to AT&T's rates. The order appears to imply, however, that the terms of the AT&T/Alascom operating arrangement are unchanged by price caps, an implication that has been informally confirmed by Commission staff. A copy of this footnote is attached to these comments at Appendix A for the convenience of the Joint Board.

⁵⁸ See Alaska Comments at 26-29.

competition objectives without endangering universal service and related objectives.

Alascom's ARC plan appears to address some of these concerns.⁵⁹ Alascom's plan, however, at least as presently structured, appears to give it the full benefits of incentive regulation, but little or none of the obligations. Many issues, including the following, need to be addressed before this proposed plan could be adopted.

First, as the State noted in connection with its incentive proposal,⁶⁰ steps need to be taken to make sure that, in an effort to keep interstate costs down, costs are not simply shifted to the intrastate jurisdiction. Incentive regulation in one jurisdiction and rate of return regulation in another create a powerful new "incentive" to shift costs to the jurisdiction with rate of return regulation. The result could be significantly increased intrastate rates.

Second, under ARC, there are no assurances that service quality will not suffer and no mechanism for monitoring or measuring service quality. Because an ARC-like scheme could create disincentives to invest, some steps to assure that service quality is maintained are important, especially given the unique geographic and climatic demands imposed on telecommunications facilities in Alaska.⁶¹

⁵⁹ See Alascom Comments at 11-22.

⁶⁰ Alaska Comments at 19 and n.60.

⁶¹ Similar steps would need to be taken in connection with the State's proposal as well.

Third, the 2.5 percent productivity offset and 0.5 percent consumer benefit offset contained in the ARC plan were taken from the Commission's AT&T price cap plan and may not be appropriate for the ARC plan. Further, the applicability of the consumer dividend to Alascom is unclear since, in at least one major sense, AT&T is Alascom's customer.

Fourth, Alascom suggests that its revenue cap should increase by an amount corresponding to the revenue attributable to 50 percent of the growth of southbound traffic.⁶² Although the State agrees that Alascom should have some incentive to increase revenue, given that AT&T currently, in effect, obtains 100 percent of the revenue from traffic growth, the State has concerns about the economics of Alascom's suggestion.

The State suggests that the Joint Board reexamine the issues in this proceeding in light of the price cap order and the various new proposals for incentive regulation put forth in this proceeding. It should then determine whether and how incentive regulation can help the Joint Board further the objectives it has identified and whether one, or a combination of several, incentive based proposals could be a workable approach to resolution of the issues in this proceeding.

V. CONCLUSION

The State believes the Joint Board has properly identified and prioritized the objectives to be furthered in this proceeding. It believes Plan B is antithetical to the primary objectives of

⁶² Alascom Comments at 14.

universal service, rate integration and revenue requirement neutrality. Although Plan A might be modified to further those objectives, the State suggests that the Joint Board consider whether and how incentive regulation could be useful in crafting the appropriate market structure for Alaskan interstate telecommunications services, and then take the appropriate steps to explore such an approach.

Respectfully submitted,

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rates.¹⁹⁵ British consumers will therefore be the direct beneficiaries of British Telecom's efficiency gains.

111. In addition to finding that incentive regulation is capable of eliminating, and even reversing, several significant flaws inherent in rate of return, we also find that incentive regulation is better for consumers. By acting directly on a carrier's costs of providing service, and by increasing a carrier's willingness to innovate, incentive regulation means that telecommunications consumers can look forward to low cost and innovative services that the current regulatory structure would discourage. Furthermore, as will be discussed as part of the implementation sections of this Order, we are introducing substantial ratepayer protections to ensure that consumers will be better off as a group, and in particular, that residential ratepayers receive benefits from our plan. Features such as the Consumer Productivity Dividend (CPD), review and adjustment of the productivity factor beginning three years from the date of inception, and careful attention to the design of baskets and bands ensures that consumers will benefit from an incentive system.

112. We reject arguments that carriers will be the only party to benefit from incentive regulation. Under incentive regulation, both carriers and ratepayers will benefit. Through ratepayer protections that guarantee that consumers share in carrier efficiency gains, consumers will see price reductions that would not have occurred in a rate of return setting. The elimination of inefficiencies through use of the CPD ensures that gains accrue to ratepayers first and foremost, before carriers obtain any benefits of increased earnings.¹⁹⁶

113. We conclude that incentive regulation is better suited to the task of regulating certain dominant carriers than is rate of return.¹⁹⁷ By

¹⁹⁵ Id. at 20 (proposing to change the productivity offset from 3 percent to 4.5 percent).

¹⁹⁶ The formula we adopt for AT&T and propose for the LECs, infra, ensures that 0.5 percent of productivity a carrier gains over its historical productivity must first be applied to decrease aggregate rates, before a carrier can reap any profit from its increased productivity. See Section III.C.1.c and Section IV.C.1, infra.

¹⁹⁷ In the Further Notice, we stated that, for the purposes of this proceeding, the term "dominant carrier" encompasses AT&T and the local exchange carriers. 3 FCC Rcd at 3203-03 (para. 8 n.13). We concluded that the revision of our rules concerning rate regulation of Comsat raised issues that could not be resolved in this docket. In addition, we concluded that, should AT&T elect price cap regulation, Alascom would be included under price cap regulation with regard to most of its facilities, because Alascom and AT&T

employing carriers' natural incentives to generate profit, we can devise a system of regulation that functions far more smoothly than the existing system. Our judgment on this issue has been informed by our lengthy experience with rate of return, and by the successful incentive-based

presently concur in each other's MTS and WATS tariffs. Id.

Cosat argues that there is no valid reason to exclude it from price cap regulation, and that its obligation to share in the costs of Intelsat should not render it ineligible. Cosat Comments at 4-5. Cosat argues that Intelsat is owned by and responsive to its signatories, and does not constitute a pooling arrangement of the type we found unsuitable for price caps in the Further Notice. Id. at 8-9. Cosat states that both Intelsat and Cosat have strong incentives to increase efficiency. Id. at 5. In addition, Cosat contends that price cap regulation would alleviate heavy administrative burdens for both this Commission and for Cosat. Id. at 10. We reiterate the conclusion of the Further Notice: alternative regulation for Cosat raises issues that cannot be resolved in this proceeding. Cosat has a statutory obligation to participate in a global communications network, and has been designated as the United States Signatory to the Agreement Relating to the International Telecommunications Satellite Organization "Intelsat" 23 U.S.T. 3813, T.I.A.S. 7532 (1971) (hereinafter Intelsat Operating Agreement). See also Section 102 of the Communications Satellite Act of 1962, 47 U.S.C. § 701. As a signatory to Intelsat, Cosat is obligated to share in the costs of Intelsat. Intelsat Operating Agreement, Article II. Thus, regulatory reform for dominant carriers cannot be mechanically applied to Cosat, whose corporate mission is given shape by federal legislation and treaty.

Alascom agrees that the operation of the Alascom-AT&T joint service agreement will necessarily include Alascom under price cap regulation, but only to the extent of its MTS and WATS services. Alascom argues that its private line services should also be subject to price cap regulation. Alascom Reply at 6. We conclude that it would not be wise to apply price cap regulation to Alascom's private line services at this time. The productivity factor in the price cap index is developed on a nationwide interstate basis. Alascom's contention that we should apply the price cap formula to its private line services alone raises the issue of whether the productivity number calculated on a nationwide interstate basis for AT&T in this Order would result in just and reasonable rates if applied in the context of private line services in the Alaska market. Alascom's argument therefore raises questions that cannot be resolved at this stage of the proceeding.

Finally, Hawaii raises the issue of price cap treatment for GTE Hawaiian's provision of international services. Hawaii Comments at 20-23. The issues raised by Hawaii regarding GTE Hawaiian's operations will be addressed as part of our discussion concerning the implementation of incentive

regulatory systems currently in use in the various states, as well as Great Britain. Furthermore, we believe that the potential pitfalls of incentive regulation identified by commenters can be avoided with careful attention to implementation.

114. Our determination that incentive regulation is superior to rate of return as a matter of policy does not end our task. Rather, it marks the beginning of the work of transforming incentive principles into a system of policies and rules that can be administered effectively on a day-to-day basis. We are not unmindful of the pitfalls identified by some commenters of the harmful effects that might attend the introduction of incentive regulation if such a system is not implemented properly, particularly as these comments relate to implementation of incentive regulation for local exchange carriers. Although any final judgment about incentive regulation depends in large measure on the specifics of implementation, we believe the pitfalls discussed in the record can be avoided. In the following section, we consider in detail the arguments raised concerning incentive-based regulation for AT&T. In the section thereafter, we consider implementation issues relating to incentive regulation for local exchange carriers.

III. INCENTIVE REGULATION FOR AT&T

115. In the previous section, we sketched the broad outlines of a plan to reform our regulation of dominant carriers, and concluded that the approach we outlined, which we have termed "incentive regulation," is superior to rate of return as a method for curbing the market power of dominant carriers. In that section, we addressed the general concerns of a number of parties about our comparison of rate of return and incentive regulation as a means of regulating dominant carriers. In this section, we address the specific concerns that have been raised about applying incentive regulation to AT&T.¹⁹⁸ We also set forth in detail the mechanisms we will employ in regulating AT&T under an incentive-based system that we call "price cap regulation."¹⁹⁹

regulation for the LECs in Section IV.C.2.b, infra.

198 In resolving implementation issues for AT&T, we have addressed arguments that are directed to AT&T, or that do not logically and explicitly exclude AT&T. LEC-specific issues are addressed in the portion of this Order that constitutes the Second Further Notice of Proposed Rulemaking.

199 The final rules implementing price cap regulation for AT&T are contained in Appendix B.

CERTIFICATE OF SERVICE

I, Linda K. Smith, do hereby certify that, on May 15, 1989, I have caused to be sent a copy of the foregoing "Reply Comments of The State of Alaska In Response To The Supplemental Order Inviting Comments" by United States mail, postage prepaid, to the following:

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