INITIAL COMMENTS OF
THE NEW JERSEY DIVISION OF RATE COUNSEL

Stefanie A. Brand
Director
Division of Rate Counsel
Christopher J. White
Deputy Rate Counsel
140 E Front Street, 4th Floor
Trenton, NJ 08625
Phone (609) 984-1460
Fax (609) 292-2923
www.rpa.state.nj.us
njratepayer@rpa.state.nj.us

July 12, 2013
TABLE OF CONTENTS

I. INTRODUCTION ......................................................................................................................... 1

II. SECOND FURTHER NOTICE OF PROPOSED RULEMAKING .............................................. 2
   A. Background .......................................................................................................................... 2
   B. Rate Counsel continues to oppose grants of forbearance related to structural separations. ........................................................................................................... 5

III. CONCLUSION ......................................................................................................................... 8
SUMMARY

The New Jersey Division of Rate Counsel ("Rate Counsel") opposes forbearance for rate-of-return incumbent local exchange carriers from the structural separation rules that the Federal Communications Commission ("FCC" or "Commission") set forth in Section 64.1903. As the FCC has previously recognized, "a portion of their interstate access charge compensation and universal service support is based on their costs of providing service," which "gives them an incentive to engage in cost misallocation, increase certain access charges, and facilitate a price squeeze." Further, there is no evidence that these rules inhibit carriers' innovation, broadband deployment or adoption of Internet-protocol ("IP") technology.

INITIAL COMMENTS OF
THE NEW JERSEY DIVISION OF RATE COUNSEL

I. INTRODUCTION

The New Jersey Division of Rate Counsel ("Rate Counsel") responds to the Federal Communications Commission ("FCC" or "Commission") Further Notice of Proposed Rulemaking ("Notice") seeking comment on the costs and benefits of the FCC's structural separations rules, specifically those set forth in Section 64.1903, as they are applied to rate-of-return carriers and whether those rules are still critical for ensuring that the carriers do not engage in anticompetitive behavior.  

Rate Counsel urges the FCC to retain its structural separations rules because non-structural safeguards do not provide the same level of protection against mis-allocation of costs as do separate affiliate requirements. Rate Counsel has previously opposed the Bell operating companies (in the context of the Section 272 Sunset Order) and then price cap incumbent local exchange carriers ("ILECs") (in the USTelecom Forbearance Order) from their petitions for

---

forbearance from these requirements and Rate Counsel continues to do so with regard to rate-of-return ILECs. Structural separations increases the accuracy of cost allocation and accounting, which in turn enables consumer advocates and regulators to participate effectively in state and federal regulatory proceedings that concern a wide range of issues, such as the impact of switched access charges on carriers’ local rates, the need for and size of state universal service funds, and the determination of appropriate inputs and assumptions for the cost models that will be used to quantify federal broadband service support.

Rate Counsel has participated previously in numerous proceedings concerning various carriers’ petitions for forbearance. Rate Counsel refers the Commission to and incorporates by reference Rate Counsel’s initial and reply comments filed on numerous prior forbearance petitions (some of which Rate Counsel submitted jointly with the National Association of State Utility Consumer Advocates (“NASUCA”)) because many of the arguments regarding those petitions continue to be germane to the Commission’s investigation of USTelecom’s Petition for forbearance.3

II. SECOND FURTHER NOTICE OF PROPOSED RULEMAKING

A. Background

Section 64.1903 of the FCC’s rules requires independent ILECs that provide facilities-based long distance services to set up a separate corporate subsidiary prohibited from joint ownership (with the local exchange company) of transmission and switching equipment; keep separate books of account; and purchase services from the ILECs pursuant to tariffs or

3/ See Attachment A.
interconnection agreements. In its Second Further Notice of Proposed Rulemaking, the FCC states:

In furtherance of our commitment to revisit "rules that may be outmoded, ineffective, insufficient, or excessively burdensome," while continuing to promote competition and consumer protection consistent with the Act, we evaluate in this Second Further Notice of Proposed Rulemaking (Second FNPRM) the structural separation requirements of section 64.1903 of the Commission's rules, as they apply to rate-of-return carriers providing facilities-based in-region, interexchange, interstate long distance services (in-region long distance services). Through this proceeding, we intend to modernize our rules to reflect the competitive and marketplace realities for long distance service—at one time an expensive service, today one frequently offered on an unlimited basis by numerous facilities-based providers.

In its USTelecom Forbearance Order, the FCC granted USTelecom's request for forbearance from section 64.1903 as it applies to price cap carriers. Rate Counsel opposed USTelecom's request for forbearance and respectfully disagrees with the FCC's grant of forbearance from section 64.1903 for price cap carriers. However, the FCC denied that relief to

---

4/ See, e.g., Notice, at para. 214. The FCC explains: "Section 64.1903 of the Commission's rules sets forth the structural requirements that apply to an independent ILEC's provision of in-region long distance services. That rule as written requires every independent ILEC providing those services using its own switching or transmission facilities to do so only through a separate affiliate that: (1) maintains books of account separate from those the independent ILEC maintains; (2) does not jointly own transmission or switching facilities with its independent ILEC; and (3) purchases tariffed services from the independent ILEC only pursuant to the ILEC's tariffs, except that the separate affiliate also may acquire unbundled network elements (UNEs) and exchange services pursuant to an approved interconnection agreement. Independent ILECs that provide long distance service exclusively through resale, however, may do so through a separate corporate division rather than an entirely separate company." Id. (cites omitted). Independent ILECs are classified as nondominant with respect to the provision of in-region long distance service and have not been required to file tariffs for those services. USTelecom Forbearance Order, at para. 136 (cites omitted).

5/ Notice, at para. 211.

6/ Id., at para. 213. The grant of forbearance is conditioned upon price cap carriers submitting special access performance metrics and imputation requirements. USTelecom Forbearance Order, at paras. 145-148.

7/ Petition of USTelecom For Forbearance Under 47 U.S.C. § 160(c) From Enforcement Of Certain Legacy Telecommunications Regulations, WC Docket No. 12-61, Comments of the National Association of State Utility Consumer Advocates, Maine Office of the Public Advocate, and The New Jersey Division of Rate Counsel, April 9, 2012.

8/ USTelecom Forbearance Order, at para. 139.
rate-of-return carriers, stating: “cost misallocation is still a concern for independent ILECs that operate under rate-of-return cost regulation because a portion of their interstate access charge compensation and universal service support is based on their costs of providing service. This gives them an incentive to engage in cost misallocation, increase certain access charges, and facilitate a price squeeze.”9 Despite that finding, the FCC concurrently released the current Notice seeking comments on those findings.

Rate Counsel acknowledges that the long distance market has been substantially transformed during the past sixteen years,10 with the elimination of MCI and legacy AT&T as national long distance carriers, the widespread popularity of bundled local and long distance packages, and the blurring of local and long distance calls. Nonetheless, as Rate Counsel has demonstrated in previous comments,11 the “bundled” market is dominated by a duopoly, which does not represent effective competition. Furthermore, a trend of increasing prices (especially in areas that are purportedly effectively competitive) suggests that cable industry (the major alternative suppliers to ILECs) lacks effective competition.12 Furthermore, a consumer that subscribes to an ILEC’s local service cannot subscribe to a cable company’s long-distance service. The overall effect is that there is minimal market pressure on the prices for bundled

---

9 / Id. at para. 151.

10 / Id., at para. 137: “Section 64.1903 was adopted in the 1997 LEC Classification Order, although it has its origins in the Commission’s Competitive Carrier Proceedings.”


12 / In the Matter of Implementation of Section 3 of the Cable Television Consumer Protection and Competition Act of 1992, Statistical Report on Average Rates for Basic Service, Cable Programming Service, and Equipment, MM Docket No. 92-266, Report on Cable Industry Prices, DA 13-1319, June 7, 2013. Among other things, the FCC found that “the price of expanded basic service averaged across all effective competition communities was higher than the price of expanded basic service averaged across noncompetitive communities,” and that the “difference is statistically significant.” Id., at para. 4.
services. Further, despite changes in the way that long distance service is offered and packaged, independent ILECs still possess the incentive and ability to misallocate costs among their various services, which, in turn, can affect their level of universal service support as well as their switched access charges. The consequence for consumers could be exaggerated claims for universal service funds, which consumers pay for through universal service contribution charges, and inaccurate cost data for switched access charges.

B. **Rate Counsel continues to oppose grants of forbearance related to structural separations.**

Rate Counsel opposes a grant of forbearance from section 64.1903 separate affiliate requirements and from dominant carrier treatment of long distance services.\(^\text{13}\) USTelecom contends that dominant carrier regulation is no longer appropriate because voice services are no longer provided by a “monopoly platform”\(^\text{14}\) and the FCC notes “significant marketplace changes have taken place since the Commission adopted section 64.1903 in 1997.”\(^\text{15}\) According to the FCC, these developments “call into question whether this rule remains the best alternative for promoting competition and protecting consumers in the long distance market.”\(^\text{16}\) According to the FCC, these changes include: declining interexchange revenues (para. 231); increasing subscription rates to wireless and cable-based local voice services (para. 232); and increases in demand for bundled local and long distance packages (para. 235). For the reasons discussed in Rate Counsel’s previous comments, which are incorporated by reference, Rate Counsel disagrees

---

\(^{13}\) As noted by the FCC the “practical consequence” of forbearance from structural separations requirements under section 64.1903 is that “once the Commission has forborne from the section 64.1903 requirements for a class of independent ILECs, there is no requirement under existing precedent to file tariffs for such services or otherwise comply with dominant carrier regulation of those services as a result of providing long distance services on an integrated basis.” Notice, at para. 228, citing USTelecom Forbearance Order, at para. 154.

\(^{14}\) See, id., at para. 229 citing USTelecom Petition for Declaratory Ruling filed on December 19, 2012.

\(^{15}\) Id., at para. 230.

\(^{16}\) Id.
with the implication that voice services are competitive, and disagrees with the premise that bundled services are competitive. The FCC has established an unambiguous precedent for applying traditional market power analysis to its review of petitions for forbearance.\(^{17}\) In its assessment of the pending petition in this proceeding to relax safeguards, the FCC should undertake a similarly rigorous analysis of empirical data for relevant markets. Caution is appropriate, because once the safeguards are eliminated, it is unlikely that they will be re-established.

The FCC, while stating that interexchange revenues have declined, concedes that the ILECs’ share of traditional long distance lines “increased dramatically by 2011” while at the same time the amount of calling has declined.\(^ {18}\) The FCC cites statistics indicating that cable-based local telephone service represents 37 percent of the local market and approximately 36% of households are wireless only.\(^ {19}\) Finally, the FCC cites its own findings that stand-alone long distance has become a “fringe market” and that 80% of residential switched access lines and interconnected VoIP have “+1” access to their local provider’s long distance service.\(^ {20}\)

The FCC recognized that section 64.1903 protects against ILEC use of exclusionary market power. Consequences of the exercise of exclusionary market power include: the ability to raise rivals’ costs; use of a price squeeze; and non-price discrimination.\(^ {21}\)


\(^{18}\) Notice, at para. 231.

\(^{19}\) Id., at paras. 233-234.

\(^{20}\) Id., at para. 235.

\(^{21}\) Id., at para. 237.
The FCC appropriately observes that reforms will cap or reduce switched access charges “but allow increases in common line and special access rates,” and states, “[t]hus, we believe that these changes in the access charge rules reduce, but may not eliminate, incentives for cost misallocation and potential access charge rate increases.” 22 To the extent that commenters in this proceeding contend that other methods can be used to address cost misallocation concerns in a less burdensome way, 23 in Rate Counsel’s view, those commenters have the burden of proof to demonstrate this contention. It is premature to conclude that the FCC’s access charge reform will eliminate the need for structural separations.

The FCC seeks comment on whether bundled services make non-price discrimination and price squeeze concerns obsolete and whether other safeguards are sufficient. 24 Finally, the FCC seeks information on the quantity of ILECs that use separate affiliates, the costs that would be saved if the FCC eliminated the separate affiliate requirement, the relative costs of maintaining a separate division in contrast with maintaining a separate corporation. 25 Also, the FCC seeks empirical data from those ILECs that have experience offering long distance service through a separate corporate affiliate or a separate division. 26 Rate Counsel will review the information that carriers submit, and may address that information in its reply comments.

The FCC asks whether ILECs’ economies of scope and scale are limited under current rules; whether innovation is deterred; and whether the transition to an Internet Protocol network is “more difficult” as a consequence of the prohibition against joint ownership of switching and

22 Id., at para. 238.
23 Id., at para. 238, seeking alternative ways to address cost misallocation concerns.
24 Id., at para. 241.
26 Id.
transmission equipment. The FCC also asks whether section 64.1903 “reduce[s] independent ILECs’ ability to increase telephone subscribership or extend broadband services to additional areas.” The record lacks any empirical evidence to justify a change in existing rules.

In addition, in Rate Counsel’s view ILECs’ transition to offering only VoIP services is irrelevant to whether section 64.1903 should continue to apply. ILECs’ choice of technology is a distinct matter from whether ILECs’ possess the ability and incentive to engage in anticompetitive practices. It is not clear how section 64.1903 would jeopardize ILECs’ ability to deploy broadband service, because deployment decisions typically depend on carriers’ assessment of potential revenues and costs.

**III. CONCLUSION**

Rate Counsel opposes forbearance for rate-of-return incumbent local exchange carriers from the structural separation rules that the Commission set forth in Section 64.1903 for the reasons set forth in these comments and the many comments incorporated by reference.

---

27 / _Id._ at para. 243.

28 / _Id._

29 / _Id._
Respectfully submitted,

Stefanie A. Brand
Director
Division of Rate Counsel
Christopher J. White
Deputy Rate Counsel
140 E Front Street, 4th Floor
Trenton, NJ 08625

Phone (609) 984-1460
Fax (609) 292-2923

July 12, 2013
Attachment A

Selected FCC Filings by New Jersey Division of Rate Counsel Regarding Forbearance Issues


Assignment Rules, WC Docket Nos. 08-190; 07-139; 07-204; 07-273; 07-21, Reply Comments of the New Jersey Division of Rate Counsel, December 12, 2008.

Ex Parte Letter from Ronald K. Chen, Public Advocate, Stefanie A. Brand, Esq., Director, and Christopher J. White, Esq., Deputy Public Advocate, Department of the Public Advocate, New Jersey Division of Rate Counsel; David C. Bergmann, Assistant Consumers' Counsel Office of the Ohio Consumers' Counsel, Chair, NASUCA Telecommunications Committee, National Association of State Utility Consumer Advocates, to FCC Chairman Kevin Martin and Commissioners Adelstein, Copps, Tate and McDowell, Re: Ex Parte Communication, WC Docket No. 07-139, September 3, 2008.

Petition of AT&T Inc. for Forbearance Under 47 U.S.C. § 160 from Enforcement of Certain of Commission's Cost Assignment Rules, WC Docket No. 07-21, Comments and Opposition of New Jersey Division of Rate Counsel, June 26, 2008; Reply Comments and Opposition of the New Jersey Division of Rate Counsel, July 7, 2008.

Petition to Establish Procedural Requirements to Govern Proceedings for Forbearance Under Section 10 of the Communications Act of 1934, as Amended, WC Docket No. 07-267, Initial and Reply Comments of the New Jersey Division of Rate Counsel and NASUCA, March 7, 2008 and March 24, 2008.


In the Matter of Petition of the Verizon Telephone Companies for Forbearance Pursuant to 47 U.S.C.§ 160(c) in the Philadelphia, Pittsburgh, Boston, New York City, Providence and Virginia Beach Metropolitan Statistical Areas, WC Docket 06-172, Comments of the National Association of State Utility Consumer Advocates, the Pennsylvania Office of Consumer Advocate, the Public Utility Law Project of New York, Inc., the Massachusetts Office of Attorney General, the Virginia Office of Attorney General, the Maryland Office
of People's Counsel, the New Jersey Division of Rate Counsel, the New Hampshire Office of Consumer Advocate and the Connecticut Office of Consumer Counsel, March 5, 2007; Reply Comments of the National Association of State Utility Consumer Advocates, the Pennsylvania Office of Consumer Advocate, the Public Utility Law Project of New York, Inc., the Massachusetts Office of Attorney General, the Virginia Office of Attorney General, the Maryland Office of People's Counsel, the New Jersey Division of Rate Counsel, the New Hampshire Office of Consumer Advocate, and the Connecticut Office of Consumer Counsel, April 18, 2007.

In the Matter of Jurisdictional Separations and Referral to the Federal-State Joint Board, CC Docket No. 80-286, comments of the National Association of State Utility Consumer Advocates, the New Jersey Division of Rate Counsel and the Maine Office of the Public Advocate, August 22, 2006; Reply Comments of the National Association of State Utility Consumer Advocates, the New Jersey Division of Rate Counsel and the Maine Office of the Public Advocate, November 20, 2006; comments of Rate Counsel, April 16, 2009; comments of NASUCA and Rate Counsel, April 19, 2010; comments of NASUCA and Rate Counsel, March 28, 2011.

Ex Parte Letter from Seema M. Singh, Esq., Ratepayer Advocate, State of New Jersey Division of the Ratepayer Advocate to Marlene H. Dortch, Secretary, Federal Communications Commission, Re: Ex Parte Meeting on June 19, 2006 on AT&T's Proposed Acquisition of BellSouth, WC Docket No. 06-74; Broadband Consumer Protection, WC Docket No. 05-271; Cable Television Franchise, Implementation of 621-A of the Cable Communications Policy Act, MB Docket No. 05-311; Petition of AT&T for Waiver of Commission’s Rules to Treat Certain Number Portability Costs as Exogenous Costs Under Section 61.45(d), CC Docket No. 95-116; Non-Rural High Cost Support, Docket Nos. CC 96-45, WC 05-337; Intercarrier Compensation, CC Docket No. 01-92; Petition of BellSouth for Forbearance from Cost Assignment Rules, WC Docket No. 05-342; Qwest Petition for Forbearance from Dominant Carrier Rules, WC Docket No. 05-333; and a laCarte options for consumers, June 20, 2006.


Qwest’s Petition for Forbearance from Enforcement of the Commission’s Dominant Carrier Rules as They Apply After Section 272 Sunsets, WC Docket No. 05-333, Comments of the New Jersey Division of the Ratepayer Advocate, January 23, 2006.