Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
Wisconsin Public Service Commission	)	Bureau/CPD No. 00-01
Order Directing Filings	)	

MEMORANDUM OPINION AND ORDER

Adopted: January 28, 2002 Released: January 31, 2002

By the Commission:

I. INTRODUCTION

1. In this *Memorandum Opinion and Order* (*Order*), we grant the LEC Coalition's[1] application for review of the Bureau's March 2, 2000 Order[2] (*Bureau Order*) that directed the four largest LECs in Wisconsin[3] to submit to the Federal Communications Commission (Commission) their currently effective tariffs for intrastate payphone service offerings. The *Bureau Order* stated that we would review the Wisconsin LECs' intrastate payphone service offerings for compliance with section 276 of the Communications Act of 1934, as amended (the Act),[4] and our rules, including the *Payphone Orders*.[5] While we do agree to review the LEC

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1 The members of the LEC Coalition (Coalition) are: Ameritech Corporation, the Bell Atlantic companies (Bell Atlantic-Delaware, Inc., Bell Atlantic-Maryland, Inc., Bell Atlantic-New Jersey, Inc., Bell Atlantic-Pennsylvania, Inc., Bell Atlantic-Virginia, Inc., Bell Atlantic-Washington, D.C., Inc., Bell Atlantic-West Virginia, Inc., New York Telephone Company, and New England Telephone and Telegraph Company), BellSouth Telecommunications, Inc., GTE Service Corporation, SBC Telecommunications, Inc., Wisconsin Bell (d/b/a Ameritech Wisconsin), and U S WEST Communications, Inc. (now Qwest Corporation). The LEC Coalition's Application for Review of the Common Carrier Bureau's "New Services Test" Order at 1 n.1 (April 3, 2000) (LEC App.).

2 *In the Matter of Wisconsin Public Service Commission: Order Directing Filings*, DA No. 00-347, Order, 15 FCC Rcd 9978 (March 2, 2000).

3 Wisconsin Bell, Inc. (d/b/a Ameritech Wisconsin), Century Telephone Enterprises, Inc., GTE North Incorporated, and Telephone Data Systems, Inc. (collectively, the Wisconsin LECs).

4 47 U.S.C. §§ 151-614.

5 *Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-128, First Report and Order, 11 FCC Rcd 20541 (Sept. 20, 1996) (*First Payphone Order*), Order on Reconsideration, 11 FCC Rcd 21233 (Nov. 8, 1996) (*Payphone Reconsideration Order*), *aff'd in part and remanded in part*, *Illinois Pub. Telecomms. Ass'n v. FCC*, 117 F.3d 555 (D.C. Cir. 1997); Second Report

(continued....)

Coalition's application for review, we deny the Coalition's request to withdraw or stay the *Bureau Order*.[6]

2. After careful review of section 276 and its legislative history, we conclude that Congress enacted section 276 to "promote competition among payphone service providers and promote the widespread deployment of payphone service to the benefit of the general public."[7] To advance these pro-competitive statutory goals, Congress directed the Commission to "terminat[e] the current system of payphone regulation" and "eliminate *all* discrimination between [Bell Operating Company (BOC)] and independent payphones and all subsidies or cost recovery for BOC payphones."[8] In compliance with this statutory mandate, we affirm the Bureau's conclusion that section 276 requires BOCs to set their intrastate payphone line rates in compliance with the Commission's cost-based, forward-looking "new services" test.[9] Although the administrative record for this matter shows disparate applications of the new services test in various state proceedings,[10] we believe that this *Order* will assist states in applying the new services test to BOCs' intrastate payphone line rates in order to ensure compliance with the *Payphone Orders* and Congress' directives in section 276.

3. Payphones are an important part of the nation's telecommunications system. They are critical not only for emergency communications, but also for those Americans who cannot afford

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and Order, 13 FCC Rcd 1778 (Oct. 9, 1997) (*Second Payphone Order*), *vacated and remanded*, *MCI Telecomms. Corp. v. FCC*, 143 F.3d 606 (D.C. Cir. 1998); Third Report and Order and Order on Reconsideration of the Second Report and Order, 14 FCC Rcd 2545 (Feb. 4, 1999) (*Third Payphone Order*), *aff'd*, *American Pub. Communications Counsel v. FCC*, 215 F.3d 51 (D.C. Cir. 2000). The *First Payphone Order* and the *Payphone Reconsideration Order* are collectively known as the *Payphone Orders*.

[6] LEC App. at 1-2.

[7] 47 U.S.C. § 276(b).

[8] H.R. Rep. No. 104-204, at 88 (1995) (emphasis added).

[9] *Payphone Reconsideration Order*, 11 FCC Rcd at 20614, para. 146. *See also infra* note 26 and accompanying text.

[10] State payphone association filings in this proceeding, and related proceedings before this Commission, have described diverse state public service commission approaches to the requirements of the *Payphone Orders* in more than a dozen states. *See* Reply Comments of the Ind. Payphone Ass'n (Oct. 23, 2000); Reply Comments of the Midwest Independent Coin Payphone Ass'n (Oct. 23, 2000) (discussing Missouri Public Service Commission proceedings); Reply Comments of the Independent Payphone Ass'n of N.Y., Inc. (Oct. 23, 2000); Reply Comments of the Northwest Payphone Ass'n (discussing Oregon Public Utility Commission proceedings); Joint Reply Comments of Atl. Payphone Ass'n and Central Atl. Payphone Ass'n (filed Oct. 23, 2000) (discussing proceedings in Maryland, Virginia, and Washington, DC); Reply Comments of the Illinois Pub. Telecomms. Ass'n, Michigan Pay Tele. Ass'n, Payphone Ass'n of Ohio, and the Kentucky Payphone Ass'n (filed Oct. 23, 2000). *See also* North Carolina Payphone Ass'n, Petition for Expedited Review, File No. CCB/CPD No. 99-27 (filed Aug. 13, 1999); Michigan Pay Tele. Ass'n, Petition for Declaratory Ruling, File No. CCB/CPD No. 99-35 (filed Nov. 12, 1999). *See also* Public Serv. Comm'n of S.C., *In re Request of BellSouth Telecommunications, Inc. for Approval of Revisions to its General Subscriber Service Tariff and Access Service Tariff to Comply with the FCC's Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, Docket No. 97-124-C, Order Setting Rates for Payphone Lines and Associated Features, Order No. 1999-285 (April 19, 1999), *reconsideration denied*, Order No. 1999-497 (July 19, 1999); Tennessee Regulatory Auth., *In re: All Telephone Companies Tariff Filings Regarding Reclassification of Pay Telephone Service as Required by Federal Communications Commission (FCC) Docket 96-128,* Docket No. 97-00409, Interim Order (Feb. 1, 2001).

their own telephone service.[11] Thus, despite evidence that payphones are losing market share to wireless services,[12] the basic pay telephone remains a vital telecommunications link for many Americans.

II. BACKGROUND

A. OVERVIEW OF SECTION 276

4. Before addressing the *Bureau Order*, we summarize the applicable statutory and regulatory provisions. We also review the *Payphone Orders*, other Commission orders, and the procedural history of this matter.

5. *The Requirements of Section 276*. Section 276(a) prohibits any BOC from: (1) subsidizing "its payphone service directly or indirectly from its telephone exchange operations or its exchange access operations;" and (2) preferring or discriminating "in favor of its payphone service" after the effective date of rules prescribed under section 276(b).

6. Section 276(b)(1) requires the Commission to prescribe regulations to "promote competition among payphone service providers and promote the widespread deployment of payphone services for the benefit of the general public."[13] The statute sets out five requirements to meet these goals. First, section 276(b)(1)(A) requires the Commission to "establish a per call compensation plan to ensure that all payphone service providers are fairly compensated for each and every completed intrastate and interstate call using their payphone." Second, under section 276(b)(1)(B), the Commission must promulgate regulations that "discontinue the intrastate and interstate carrier access charge payphone service elements and payments . . . and all intrastate and interstate payphone subsidies from basic exchange and exchange access revenues." Third, section 276(b)(1)(C) directs the Commission to "prescribe a set of nonstructural safeguards for Bell operating company payphone service to implement the provisions of paragraphs (1) and (2) of subparagraph (a), which safeguards shall, at a minimum, include the nonstructural safeguards equal to those adopted in the Computer Inquiry-III (CC Docket No. 90-623) proceeding."[14] Fourth, pursuant to section 276(b)(1)(D), the Commission shall "provide for Bell operating company payphone service providers to have the same right that independent payphone providers have to negotiate with the location provider on the location provider's selecting and contracting with, and, subject to the terms of any agreement with the location provider, to select and contract with, the carriers that carry interLATA calls from their payphones." Finally, section 276(b)(1)(E) directs the Commission to "provide for all payphone service providers to have the

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[11] *See* Liza Mundy, *Hearing the Call*, The Wash. Post Magazine, Sept. 2, 2001, at 26. *See also* Raymond McCaffrey, *For the Phone Booth, It's Last Call*, The Wash. Post, Sept. 17, 2001, at B3.

[12] *Hearing the Call*, *supra* note 11, at 12, 25. We find nothing in section 276 that would authorize intervention into competitive issues as between the wireless and payphone services markets. Nevertheless, we acknowledge the concerns expressed in many letters to Congress and the Commission about competition from wireless services.

[13] 47 U.S.C. § 276(b)(1).

[14] *See In the Matter of Computer III Remand Proceedings: Bell Operating Company Safeguards and Tier I Local Exchange Company Safeguards*, CC Docket No. 90-623, Report and Order, 6 FCC Rcd 7571 (Dec. 20, 1991) (*Computer III*).

right to negotiate with the location provider on the location provider's selecting and contracting with, and, subject to the terms of any agreement with the location provider, to select and contract with, the carriers that carry interLATA calls from their payphones."

7. *Preemption.* Section 276(c) states that, "[t]o the extent that any State requirements are inconsistent with the Commission's regulations, the Commission's regulations on such matters shall preempt such State requirements."

8. *Definition of "Payphone Service."* Section 276(d) broadly defines the term "payphone service" as the "provision of public or semi-public pay telephones, the provision of inmate telephone service in correctional institutions, and any ancillary services."

B. THE *PAYPHONE ORDERS* AND RELATED COURT CHALLENGES

9. *The First Payphone Order.* We addressed the statutory requirements of section 276(b)(1) in the *First Payphone Order*.[15] To implement section 276(b)(1)(A)'s "fair compensation" plan requirements, we directed interexchange carriers (IXCs) that carry calls originating from payphones to compensate the payphone service provider (PSP).[16] Previously, PSPs received no revenue for originating certain calls (such as subscriber 800 and other toll-free number calls) and were prohibited from blocking callers from making some of those calls (such as access code calls).[17] We concluded that PSPs must be compensated for all such calls and determined that IXCs, as the primary beneficiaries of those calls, should be responsible for providing that compensation.[18]

10. We decided that the best way to ensure fair competition was to allow the market to set the price for each call.[19] Because no market existed for so-called "dial around" coinless calls, we first adopted a market-based surrogate – the price of a local coin call at a typical deregulated payphone of $0.35. In selecting this regime, we stated that "the cost[s] of originating the various types of payphone calls are similar."[20]

11. To discontinue access charges and subsidies under section 276(b)(1)(B), we concluded that, in order to receive compensation for completed calls originating from its payphones, a LEC PSP "must be able to certify" that it has complied with several requirements, including the institution of "effective intrastate tariffs reflecting the removal of charges that recover the costs of payphones and any intrastate [payphone] subsidies."[21] We also required that all incumbent LEC payphones be treated as deregulated and detariffed customer premises

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[15] *First Payphone Order,* 11 FCC Rcd at 20543-45, paras. 1-8.

[16] *Id.* at 20566, para. 48.

[17] *In the Matter of Bell Atlantic-Dela. v. Frontier Comms. Servs., Inc.,* No. E-98-48/49, Mem. Opinion and Order, 14 FCC Rcd 16050, 16053-54, para. 5 (Sept. 24, 1999).

[18] *Id.*; *First Payphone Order*, 11 FCC Rcd at 20584, para. 83.

[19] *First Payphone Order*, 11 FCC Rcd at 20577, para. 70.

[20] *Id.*

[21] *Payphone Reconsideration Order*, 11 FCC Rcd at 21293, para. 131 (summarizing certification requirements).

equipment (CPE).[22]

12. To implement the nonstructural safeguards requirement of section 276(b)(1)(C), we stated that all BOCs must comply with the nonstructural safeguards from our *Computer III* order.[23] We stated that such safeguards will "ensure that BOCs do not discriminate or cross-subsidize in their provision of payphone service."[24] We concluded that, to comply with *Computer III*, LECs must unbundle payphone line services and file tariffs with the Commission for such services using the price cap "new services" test.[25] The new services test is a cost-based test that sets the direct cost of providing the new service as a price floor and then adds a reasonable amount of overhead to derive the overall price of the new service.[26] The Commission has applied this test to new interstate access service proposed by LECs subject to price cap regulation.[27]

13. Finally, subsections 276(b)(1)(D) and (E) concern the ability of BOCs and independent PSPs to negotiate with location providers on the selection of presubscribed interLATA and intraLATA carriers, respectively.[28] In the *First Payphone Order*, we identified certain "market-distorting factors" affecting these negotiation rights, such as conflicting state rules and discriminatory access, but we stated that the nonstructural safeguards in *Computer III* would address our concerns.[29] Pursuant to the express authority provided under Section 276(c), we also preempted any intrastate rules that limited or affected these negotiation rights.[30]

14. *The Reconsideration Order*. Acting on several petitions for reconsideration, we modified certain requirements for LEC tariffing of payphone services and unbundled network functionalities. We stated that LECs should file tariffs for basic payphone lines at the state level only. Unbundled features and functions provided by LECs to their own payphone operations or to others should be tariffed at both the state and federal levels.[31] We confirmed that, even if LEC payphone tariffs were filed at the state level, they should nevertheless comply with section 276 as implemented by the Commission and, as such, should be cost-based, nondiscriminatory, and

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[22] *First Payphone Order*, 11 FCC Rcd at 20611, para. 142.

[23] *Id.* at 20640-41, paras. 199-200. *See supra* note 14.

[24] *Id.* at 20640, para. 199.

[25] *Id.* at 20614, para. 146.

[26] *See Amendment of Part 69 of the Commission's Rules Relating to the Creation of Access Charge Subelements for Open Network Architecture*, CC Docket No. 89-79, Report and Order and Order on Further Reconsideration and Supplemental Notice of Proposed Rulemaking, 6 FCC Rcd 4524 (July 11, 1991) (*Part 69/ONA Order*); *In the Matter of Telephone Company-Cable Television Cross-Ownership Rules*, CC Docket No. 87-266, Mem. Opinion and Order on Reconsideration and Third Further Notice of Proposed Rulemaking, 10 FCC Rcd 244, 340-47, paras. 209-22 (Nov. 7, 1994) (defining new services test) (*Video Dialtone Reconsideration Order*).

[27] *See Amendment of Sections 64.702 of the Commission's Rules and Regulations (Third Computer Inquiry)*, CC Docket No. 85-229, Report and Order, 104 FCC 2d 958 (1986).

[28] *First Payphone Order*, 11 FCC Rcd at 20644, para. 208, and 20667, para. 253.

[29] *Id*. at 20644, para. 208, and 20660, para. 238.

[30] *Id.* at 20669-70, para. 261.

[31] *Payphone Reconsideration Order,* 11 FCC Rcd at 21307-09, paras. 162-65.

consistent with both section 276 and our *Computer III* tariffing guidelines.[32] Thus, rates assessed by LECs for payphone services tariffed at the state level should satisfy the new services test.

15. In the interest of federal-state comity, we stated that we would rely initially on state commissions to ensure that the rates, terms, and conditions applicable to the provision of basic payphone lines comply with the requirements of section 276.[33] We noted, however, that state commissions that are unable to review these tariffs may ask incumbent LECs operating in their states to file such tariffs with the Commission.[34] We also preempted all state rules that were inconsistent with our nonstructural safeguards.[35]

16. *Illinois Public Telecommunications Association v. FCC.* Various parties sought review of several portions of the *Payphone Orders.*[36] As an initial matter, the D.C. Circuit held that the Commission has jurisdiction to set purely intrastate local coin rates for payphones as part of a compensation plan under section 276(b)(1)(A).[37] The court also upheld those portions of the two challenged orders that deregulated local coin rates for payphones, set such rates according to the market, established a "carrier pays" compensation plan for toll-free payphone calls, and required IXCs to track calls from payphones.[38] The court remanded the coinless call rate determination to us, however, stating that we had overlooked record evidence that the costs of coin calls and coinless calls are not similar.[39]

17. *MCI Telecommunications Corp. v. FCC*. On remand, we re-calculated the coinless call rate using a "top down" methodology.[40] Several parties challenged portions of the *Second Payphone Order* in the D.C. Circuit.[41] The court invalidated the Commission's methodology for calculating the local coinless call rate and remanded the order for further proceedings.

18. *American Public Communications Counsel v. FCC*. On remand, the Commission developed and applied a "bottom up" methodology to calculate the local coinless call rate.[42] The D.C. Circuit upheld the Commission's order, finding that the bottom up methodology was a reasonable exercise of the Commission's authority to establish per-call compensation rates.[43]

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[32] *Id.* at 21308, para. 163.

[33] *See* Letter to Joseph P. Mettner, Chairman, Public Service Commission of Wisconsin, from Kathryn C. Brown, Chief, Common Carrier Bureau, 13 FCC Rcd 20865, 20866 (Oct. 28, 1998) (1998 CCB Letter).

[34] *Payphone Reconsideration Order*, 11 FCC Rcd at 21308, para. 163.

[35] *Id.* at 21328-29, paras. 218-220.

[36] *Illinois Pub. Telecomms. Ass'n v. FCC*, 117 F.3d 555 (D.C. Cir. 1997) (*IPTA v. FCC*)

[37] *Id*. at 562.

[38] *Id*. at 562-67.

[39] *Id*. at 563-64.

[40] *Payphone Reconsideration Order,* 11 FCC Rcd 21233.

[41] *MCI Telecomms. Corp. v. FCC*, 143 F.3d 606 (D.C. Cir. 1998).

[42] *Third Payphone Order*, 14 FCC Rcd at 2577, para. 72.

[43] *American Pub. Communications Counsel v. FCC*, 215 F.3d 51 (D.C. Cir. 2000). Neither the top down nor bottom up methodology is at issue in this proceeding, but we include this discussion to provide context.

C. PROCEDURAL HISTORY OF THIS MATTER

19. In July 1997, the Wisconsin Pay Telephone Association filed a petition with the Wisconsin Commission "request[ing] that the [Wisconsin Commission] determine the cost basis for each network service provided by Wisconsin [LECs] to payphone providers under the federal New Services Test, determine whether the network services provided by LECs to payphone providers discriminate in favor of the LECs' own payphone operations, [and] determine whether LECs are subsidizing payphone operations with revenue from noncompetitive services."[44]

20. Four months later, in November 1997, one month after the D.C. Circuit remanded the *Second Payphone Order* to the Commission, the Wisconsin Commission held that its ability to investigate the rates charged by LECs to payphone service providers "is very narrowly circumscribed to enforcing a prohibition on cross subsidy . . . and discriminatory practices."[45] The Wisconsin Commission also stated that the statutory remedies available under Wisconsin law "only address whether the retail rates charged by telecommunications utilities for competitive telecommunications service recover the underlying cost for that service."[46] The Wisconsin Commission concluded that it could not review the rates, terms, and conditions of basic payphone services for compliance with the requirements of section 276 and the Commission's rules.[47]

21. On October 28, 1998, the Bureau sent a letter to the Wisconsin Commission stating that, in light of the Wisconsin Commission's decision, the Bureau would require the Wisconsin LECs to file with the Commission "tariffs that set forth the rates, terms, and conditions associated with pay phone services, along with the required supporting documentation."[48] The Bureau stated that its review of such rates would ensure that LEC payphone line service tariffs in Wisconsin complied with section 276 and the *Payphone Orders*.[49]

22. On March 2, 2000, the Bureau issued an order directing Wisconsin Bell, Inc. (d/b/a Ameritech Wisconsin), GTE North Incorporated, Century Telephone Enterprises Inc., and Telephone Data Systems, Inc., to submit to the Commission copies of their companies' currently effective intrastate tariffs that set forth the rates, terms, and conditions associated with payphone line services in Wisconsin.[50] The *Bureau Order* also requested documentation demonstrating compliance with the requirements of section 276 and the Commission's rules.[51]

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[44] Wisconsin Public Service Commission Letter Order, Docket No. 05-TI-156 (Nov. 6, 1997) (unpublished).

[45] *Id.*

[46] *Id.*

[47] *Id.*

[48] *See* 1998 CCB Letter, 13 FCC Rcd at 20866.

[49] *Id.*

[50] *Bureau Order*, 15 FCC Rcd at 9980, para. 5.

[51] *Id.*

1. Cost-Based Federal Pricing Standards

23. The *Bureau Order* summarized the guidelines to be applied under *Computer III* and other Commission proceedings concerning the application of the new services test and cost-based ratemaking principles to services that incumbent LECs offer to competitors.[52] The Bureau explained that, to satisfy these requirements, an incumbent LEC must demonstrate that the proposed payphone line rates do not recover more than the direct costs of the service, plus "a just and reasonable portion of the carrier's overhead costs."[53] Costs must be determined by an appropriate forward-looking, economic cost methodology that is consistent with the principles articulated in the *Local Competition Order*.[54]

24. The *Bureau Order* confirmed our longstanding policy that the new services test requires the use of consistent methodologies in computing direct costs for related services.[55] As a result, the *Bureau Order* stated, cost study inputs and assumptions used to justify payphone line rates should be consistent with the cost inputs used in computing rates for comparable services offered to competitors.[56]

2. Just and Reasonable Overhead Allocations

25. The *Bureau Order* stated that overhead allocations must be based on cost and may not be set artificially high in order to subsidize or contribute to other services.[57] The *Bureau Order* required the Wisconsin LECs to justify the methodology used to determine such overhead costs.[58] Absent justification, the *Bureau Order* stated, the Wisconsin LECs may not recover a greater share of overheads in rates for the service under review than they recover for comparable services.[59] The Bureau concluded that, for purposes of justifying overhead allocations, unbundled network elements (UNEs) appear to be "comparable" to payphone line services because both provide critical network functions to a BOC's competitors and are subject to a "cost-based" pricing requirement.[60] The Bureau stated its expectation that the Wisconsin LECs should explain any overhead allocations for payphone line services that depart significantly from overhead allocations approved for UNE services.[61]

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[52] *Id.* at 9981-82, paras. 7-12.

[53] *Id.* at 9981, para. 9.

[54] *Id. See also In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket 96-98, First Report and Order, 11 FCC Rcd 15499 (Aug. 8, 1996) (*Local Competition Order*).

[55] *Bureau Order*, 15 FCC Rcd at 9981-82, para. 10.

[56] *Id.* at 9982, para. 10.

[57] *Id*. at 9982, para. 11. *See Computer III*, 6 FCC Rcd at 7601, para. 64 n.108; *Part 69/ONA Order*, 6 FCC Rcd at 4532, para. 46.

[58] *Bureau Order*, 15 FCC Rcd at 9982, para. 11.

[59] *Id.*

[60] *Id.*

[61] *Id.*

26. Finally, the *Bureau Order* stated that any forward-looking cost studies required for an overhead allocation demonstration should produce cost estimates on an "unseparated" basis.[62] The *Bureau Order* explained that, to avoid double recovery of costs, the BOC must demonstrate that in setting its payphone line rates it has taken into account other sources of revenue (*e.g.*, subscriber line charges (SLC), presubscribed interexchange carrier charges (PICC), and carrier common line (CCL) charges).[63]

27. The *Bureau Order* required that copies of tariffs and supporting documentation be filed by May 12, 2000.[64] On April 3, 2000, the LEC Coalition filed an application for review and request for stay of the Order. On April 10, 2000, the American Public Communications Council (APCC) and the Wisconsin Pay Telephone Association (WPTA) filed oppositions to the LEC Coalition's request for stay. On April 12, 2000, the Bureau, on its own initiative, deferred the date for the filings required by the *Bureau Order* until August 12, 2000, and issued a public notice requesting comment on the LEC Coalition's request for stay and application for review.[65] Oppositions to the request for stay and application for review were filed by APCC, WPTA, and several other state payphone associations on May 12, 2000. The LEC Coalition replied on May 30, 2000. On August 12, 2000, the Wisconsin LECs filed their tariff submissions pursuant to the March 2 Order. We requested comments and reply comments on those submissions, which were filed on October 2, 2000 and October 23, 2000, respectively.

28. The LEC Coalition argues that our application of the new services test to intrastate payphone line rates is improper.[66] The Coalition states that the new services test is flexible and need not be based on forward-looking costs.[67] The LEC Coalition also contends that the pricing regime of sections 251 and 252 does not apply to payphone services.[68] The Coalition states that overhead loading rates should not be based on those for UNEs.[69] Finally, the LEC Coalition argues that the Commission lacked the jurisdiction under section 276 to issue the *Bureau Order* in the first place and that, in any event, it violates the Tenth Amendment.[70]

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[62] *Id.* at 9982, para. 12.

[63] *Id.*

[64] *Id.* at 9982, para. 13.

[65] *FCC Public Notice: Pleading Cycle Established for CCB/CPD No. 00-01*, 15 FCC Rcd 6238, 6238 (April 12, 2000).

[66] LEC App. at 5-7.

[67] *Id.* at 10.

[68] *Id.* at 11.

[69] *Id.*

[70] *Id.* at 20-22. Although the LEC Coalition did not challenge our jurisdiction to issue the *Payphone Orders*, *see infra* note 74, we believe that, by challenging the jurisdictional basis of the *Bureau Order* concerning federal review of intrastate payphone line rates, the LEC Coalition necessarily challenges those portions of the *Payphone Orders* on which the *Bureau Order* relies.

29. APCC and other payphone associations counter that we properly asserted jurisdiction in the *Payphone Orders* and in the *Bureau Order*.[71] They argue that we cannot possibly fulfill Congress' directive to prevent the BOCs from discriminating against other PSPs if the underlying payphone line rate is not subject to a cost-based standard such as the new services test.[72]

30. Before turning to the merits of the LEC Coalition's arguments concerning pricing and related issues from the *Bureau Order*, we first address the claim that the Commission lacks jurisdiction to require BOCs to set their intrastate payphone line rates in compliance with the new services test.[73]

III. DISCUSSION

A. INTRASTATE JURISDICTION UNDER SECTION 276

31. The threshold question before the Commission is whether we have the authority to set the standard that states must apply in reviewing payphone line rate tariffs. Because these rates have been considered intrastate rates and thus traditionally handled by the states, the central issue is whether the Commission has jurisdiction over the intrastate component of payphone line rates. In the *First Payphone Order,* we asserted such authority and ordered that all LEC payphone line rates be cost-based, as measured by the new services test. Four years after the Commission first asserted jurisdiction over intrastate payphone line rates, the LEC Coalition now challenges our authority over intrastate payphone line rates.[74] For the reasons set forth below, we confirm the holding of our previous orders that we have jurisdiction over the intrastate payphone

[71] Letter from A.H. Kramer and R.F. Aldrich, counsel for APCC, to Dorothy Attwood, Chief, Common Carrier Bureau (March 20, 2001).

[72] *Id.*

[73] The LEC Coalition also makes three other arguments. First, it alleges that the *Bureau Order* violates the Bureau's delegated authority under 47 C.F.R. § 0.291(a)(2) as a "novel" assertion of federal power "without precedent." LEC App. at 10. As the discussion below shows, however, the *Bureau Order* adheres to the commands of section 276 and also is consistent with our prior orders concerning pricing and payphones. Accordingly, we conclude that the *Bureau Order* was within the Bureau's delegated authority. Second, the Coalition claims that the *Bureau Order* is a "legislative rule" that must go through notice and comment. *Id.* at 10. We disagree. The *Bureau Order* simply applies our existing authority. In any event, many parties, including the LEC Coalition and APCC, have submitted thorough *ex parte* comments on the jurisdictional issue. Finally, the Coalition contends that the *Bureau Order* violates the Tenth Amendment by "dictat[ing] the content of state law." *Id.* at 21. Section 276 simply sets a federal standard, and the Supreme Court has repeatedly validated "Congress' power to offer States the choice of regulating [an] activity according to federal standards or having state law pre-empted by federal regulation." *New York v. United States*, 505 U.S. 144, 167 (1992) (citations omitted). *See also FERC v. Mississippi*, 456 U.S. 742, 759 (1982).

[74] This new challenge is inconsistent with position taken by the BOC coalition in 1997, when it sought and obtained a 45-day waiver for compliance with the new services test, acknowledging in the process that the Commission *does* in fact have jurisdiction over intrastate payphone services *See In the Matter of Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-128, Order, 12 FCC Rcd 21370, 21375-76, paras. 13-14 (April 15, 1997). The Commission noted that the "RBOC Coalition *concedes* that the Commission's payphone orders . . . mandate that the payphone services a LEC tariffs at the state level are subject to the new services test and that the requisite cost-support data must be submitted to the individual states." *Id.* at 21378, para. 18 (emphasis added).

line rates charged by BOCs, but also hold that we do not have jurisdiction over such rates charged by non-BOC LECs. Nevertheless, as discussed below, states may find it appropriate to apply to all LECs the same cost-based requirement that they must apply to BOCs.

32. We must determine whether Congress through section 276 has granted us authority to regulate this traditionally intrastate matter. Our interpretation of section 276 is guided by section 2(b), which states that "nothing in this Act shall be construed to apply or give the Commission jurisdiction with respect to" intrastate services.[75] As a result of that interpretive rule, the Commission may regulate intrastate services when Congress has conferred intrastate jurisdiction in a manner that is "unambiguous or straightforward."[76] Thus, we will examine section 276 to determine whether it constitutes such a grant of authority.

33. We begin with the terms of the statute. Sections 276(a)(1) and (2) provide that any BOC that provides payphone service "shall not subsidize its payphone service directly or indirectly from its telephone exchange service operations or its exchange access operations" and that a BOC "shall not prefer or discriminate in favor of its payphone service."[77] Those prohibitions necessarily apply to both intra- and interstate payphone service provided by BOCs because the statutory language is unqualified and contains no limitation whatsoever on the discrimination, subsidies, and preferences that are prohibited. Congress would not have directed the elimination of subsidies and discrimination if BOCs were free to subsidize and discriminate at the intrastate level. To the extent that it is "not possible to separate the interstate and the intrastate components" of telephone regulation, the Commission may ensure effective regulation of the federal component, despite section 2(b), by asserting jurisdiction over the state component as well.[78]

34. Other provisions of section 276 support the conclusion that sections 276(a)(1) and (2) apply to intrastate service. In place of the subsidies that formerly supported the LEC-owned payphone system, Congress in section 276(b)(1)(A) substituted a "per call compensation plan" that applies to "each and every completed intrastate and interstate call." The D.C. Circuit held in *IPTA v. FCC* that this provision gives the Commission authority to deregulate the price charged to payphone users, which like the line rate had long been the subject of state regulation.[79] The compensation plan's explicit application to intrastate matters significantly indicates that Congress also intended to reach intrastate subsidies when it forbade BOCs from subsidizing payphone operations in section 276(a)(1). Similarly, Congress effectuated the anti-subsidy policy of section 276(a) through section 276(b)(1)(B), which directs the Commission to "discontinue the intrastate and interstate carrier access charge payphone service elements and payments . . . and all intrastate and interstate payphone subsidies from basic exchange and exchange access revenues." Thus, section 276(b)(1)(B) applies explicitly to both intrastate and

[75] 47 U.S.C. § 152(b).

[76] *Louisiana Pub. Serv. Comm'n v. FCC*, 476 U.S. 355, 377 (1986).

[77] 47 U.S.C. § 276(a)(1), (2).

[78] *Louisiana*, 476 U.S. at 375 n.4.

[79] *IPTA v. FCC*, 117 F.3d 555. The Commission previously determined that payphone line rates are the greatest single cost associated with providing payphone service. *Third Payphone Order*, 14 FCC Rcd at 2623-25, paras. 170-74, and 2632, para. 191. *See also* APCC, "New Services Test Presentation," Tab 1 at 1 (July 19, 2001).

interstate subsidies and by doing so strongly indicates that section 276(a)(1), the provision it effectuates, was also intended to apply to intrastate discrimination.[80]

35. In addition to individual provisions of the statute indicating Congress' intent that the non-subsidy provision (and by implication the non-discrimination provision) apply to both intra- and interstate service, the statutory language and structure as a whole demonstrate that Congress so intended. Section 276 establishes a comprehensive federal scheme of payphone regulation, both intra- and interstate, to be administered by the Commission. The statute eliminates the subsidies that supported the old system and implements in its place a new market-oriented approach. Four of the five specific regulatory directives in the statute, contained in subsections A, B, D, and E of section 276(b)(1), refer directly to intrastate regulation.[81] That focus on intrastate regulation alone indicates Congress' intent that the Commission occupy the field. This is not surprising. An overarching federal program is necessary to achieve Congress' goal of eliminating subsidies in order to "promote competition among payphone service providers and promote the widespread deployment of payphone services."[82] The importance of federal control is driven home by section 276(c), which expressly preempts "any State requirements . . . inconsistent with the Commission's regulations" implementing the statute. Such a comprehensive plan also shows that Congress intended the BOC non-discrimination and non-subsidization provisions to apply to *all* BOC payphone activity, both intra- and interstate.[83]

36. The legislative history of section 276 supports that interpretation of the statutory language. Congress intended to "terminat[e] the current system of payphone regulation" -- *i.e.*, the subsidization and state regulation that had long prevailed -- and to "eliminate *all* discrimination between BOC and independent payphones and *all* subsidies or cost recovery for BOC payphones from regulated interstate or intrastate exchange or exchange access revenue."[84] The Senate Committee Report similarly recognizes that BOCs have the "incentive and the potential for *all* the forms of discrimination, cross-subsidy, and leveraging of bottleneck facilities that both the divestiture and the Commission's regulatory regime for competitive [BOC] offerings are supposed to prevent."[85] Thus, Congress' stated intention to eradicate all forms of discrimination was made manifest in the broad mandate of section 276(a) to eliminate all subsidies and discrimination, intra- or interstate.

37. Subsection 276(b)(1)(C) is the only sub-part of section 276(b)(1) that does not use the term "intrastate" or otherwise refer directly to such service. But subsection C directs the

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[80] Section 276(b)(1)(B) is somewhat broader than section 276(a)(1) because it applies to all LECs and is not limited to the BOCs, as is section 276(a)(1). That distinction explains why Congress included a separate directive to the Commission to eliminate subsidies.

[81] Subsections D and E refer to intraLATA and interLATA services, which necessarily include intrastate service.

[82] 47 U.S.C. § 276(b)(1).

[83] In that respect, section 276 is akin to section 251 in that it extends the Communications Act into an area previously controlled by the states. In those circumstances, the Supreme Court held, section 2(b) "may have less practical effect" than before Congress instituted a federal payphone policy. *AT&T Corp. v. Iowa Utils. Brd.*, 525 U.S. 366, 381 n.8 (1999).

[84] H.R. Rep. No. 104-204, at 88 (emphasis added).

[85] S. Rep. No. 104-23, at 57-58 (March 30, 1995) (emphasis added).

Commission to impose nonstructural safeguards on BOC payphone operations in order to "implement the provisions of paragraphs (1) and (2) of subsection (a)," *i.e.*, sections 276(a)(1) and (2). If section 276(a) applies to intrastate payphone services, as we have shown it does, then section 276(b)(1)(C) necessarily applies to intrastate services, especially in light of the comprehensive regulatory scheme intended by Congress.

38. The preemption provision of section 276(c) comes strongly into play here. That provision preempts "*any* State requirement" that is "inconsistent with the Commission's regulations" implemented pursuant to section 276(b)(1). Nonstructural safeguards implemented under subsection C would, of course, be implemented pursuant to section 276(b)(1) and would fall within the scope of the preemption provision. Thus, a federal policy that payphone line rates be cost-based would be binding on the states. But if sections 276(a) and (b)(1)(C) do not apply to intra- as well as interstate matters, our broad preemption authority would greatly exceed our jurisdiction to issue rules in the first place. We find no evidence that Congress intended us to implement such a fractured regime.

39. In reviewing our authority in the matter before us, Congress' directive in section 276(b)(1)(C) to implement, "at a minimum," *Computer III* safeguards requires that we direct the states to apply the cost-based new services test to the payphone line rate. In *Computer III* itself, the Commission "adopted a cost-based approach to the initial pricing of new ONA services" to prevent BOCs from discriminating against independent service providers.[86] *Computer III* is not the only Commission order in which we evaluated purely intrastate services for compliance with a federal pricing standard.

40. In the *Phase I ONA Order*, for example, the Commission extensively discussed federal jurisdiction over tariffs for the BOCs' intrastate ONA services.[87] The Commission stated that "unbundling and economical pricing are two hallmarks of an ideal tariff structure for ONA services."[88] The Commission reviewed, and ultimately approved, the fundamental intrastate tariff structures of many of the plans under review. The Commission did, however, require several BOCs to file amendments explaining their intrastate ONA pricing strategies.[89] These BOCs had not demonstrated that their intrastate ONA services were either cost-based or sufficiently unbundled, characteristics that we lauded in NYNEX's intrastate ONA services plan, for example.[90] We concluded that, "[i]f a BOC's ONA plan contains elements that are so inconsistent with ONA policies that they would jeopardize fulfillment of these goals, we cannot approve that plan."[91] We cautioned that, "[t]o do otherwise could create a discriminatory or

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[86] *Computer III*, 6 FCC Rcd at 7601, para. 64 n.108. *See also Part 69/ONA Order*, 6 FCC Rcd at 4531, paras. 38-41.

[87] *Phase I ONA Order*, 4 FCC Rcd at 162-71, paras. 309-25.

[88] *Id.* at 164, para. 313.

[89] *Id.* at 166-67, paras. 316-17.

[90] *Id.* at 166-67, para. 317.

[91] *Id.*

inefficient environment for [providers] that rely on the BOC's ONA services."[92]

41. The LEC Coalition argues that the absence of the word "intrastate" from subsection C is evidence of Congress' intent that structural safeguards apply only to interstate services. The absence of that word means little in light of the clear overall thrust of the statute.[93] As the Supreme Court stated, "the mere lack of parallelism [in one subsection] is surely not enough to displace [the Commission's] explicit authority" under another subsection.[94] In addition, the LEC Coalition's interpretation would "produce[] a most chopped-up statute" of the sort rejected in that case.[95] Further, as we have also discussed, section 276(b)(1)(C) itself implicitly applies to intrastate payphone service. The nonstructural safeguards called for by Congress must include, "at a minimum," the safeguards adopted in *Computer III*. In the course of the *Computer III* proceedings, we preempted various state regulations and asserted federal jurisdiction over a number of intrastate matters.[96]

42. In sum, we require that BOC payphone line rates be cost-based, in accordance with the standards we set forth below.[97] It is important to note that we require only BOCs, and not LECs generally, to provide payphone lines at cost-based rates. Because sections 276(a) and (b)(1)(C) apply only to BOCs, we do not find that Congress has expressed with the requisite clarity its intention that the Commission exercise jurisdiction over the intrastate payphone prices of non-BOC LECs. Since there are statutory provisions that empower us to apply the new services test to payphone line rates and grant us that authority only over BOCs, we do not have a Congressional grant of jurisdiction over non-BOC LEC line rates. Although the federal regulatory program implemented in section 276 would surely benefit if all LECs were required to use cost-based rates for their payphone line services, we cannot say that, with respect to non-BOC LECs, Congress has spoken with sufficient clarity to overcome the presumption of section 2(b). We do, however, encourage states to apply the new services test to all LECs, thereby extending the pro-competitive regime intended by Congress to apply to the BOCs to other LECs that occupy a similarly dominant position in the provision of payphone lines.

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[92] *Id*. *See also Part 69/ONA Order*, 6 FCC Rcd at 4532, para. 45 ("ONA services do present an increased danger of unreasonable discrimination.").

[93] The LEC Coalition's argument that the absence of the word "intrastate" from section 276(b)(1)(C) is dispositive of the jurisdictional question cannot be squared with the Coalition's recent statement that the Commission's "authority with respect to the rates that BOCs charge for intrastate payphone services extends only to ensuring that the BOCs' state tariffs do not undermine the Commission's federal regulatory structure." Letter from Aaron M. Panner, counsel for LEC Coalition, to Magalie Salas, Secretary, FCC, at 6 (Oct. 15, 2001). That is, having conceded that the Commission has jurisdiction *at all* over intrastate payphone line rates -- even if limited to ensuring compliance with federal standards -- the LEC Coalition cannot also claim that the Commission's intrastate jurisdiction fails for want of a single word.

[94] *Iowa Utils. Bd.*, 525 U.S. at 385.

[95] *Id.* at 381 n.8.

[96] *Computer III*, 6 FCC Rcd at 7625-37, paras. 110-131. *See supra* paras. 39-41.

[97] When the Commission's jurisdiction over intrastate services arises by implication, federal regulation of intrastate services must be as narrow as possible. *IPTA v. FCC*, 117 F.2d at 563. In this case, however, we have been given an express mandate to preempt state regulation of intrastate payphone line rates; therefore, our jurisdiction does not arise by implication, and it need not be narrowly construed. *Cf. id.*

B. PRICING STANDARDS FOR PAYPHONE SERVICES

1. Application of the New Services Test

43. The Commission previously concluded that rates for ONA services must satisfy the flexible, cost-based "new services test."[98] Contrary to the claims of the LEC Coalition,[99] the Commission's longstanding precedent shows that we have used forward-looking cost methodologies where we have applied the new services test.[100] Thus, the ONA safeguard from *Computer III* and section 276 requires that payphone service rates comply with the flexible, cost-based, forward-looking new services test. Consistent with the plain language of section 276(b)(1)(C), however, only BOC's intrastate payphone services need satisfy the new services test.[101]

44. We note that many states have relied on our *Payphone Orders* and have diligently applied the new services test, as we directed, to intrastate payphone line rates.[102] We commend those states. Other states have been awaiting additional guidance from us on this issue.[103]

2. Use of TELRIC and TSLRIC

45. The LEC Coalition contends that the *Bureau Order* contains three primary substantive errors. The Coalition first asserts that payphone services are not new and therefore should not be subject to the new services test. The LEC Coalition also argues that the pricing regime of sections 251 and 252 does not apply to payphone services. Finally, the Coalition claims that the *Bureau Order* mandates the provision of payphone services using only the "total element long-run incremental cost" (TELRIC) pricing methodology.[104] We address these contentions below and conclude that they lack merit.

46. The Coalition argues that payphone lines are not themselves a "new service" and that they are therefore exempted from the new services test requirement to use forward-looking

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[98] *Computer III*, 6 FCC Rcd at 7601, para. 64 n.108; *Part 69/ONA Order,* 6 FCC Rcd at 4531, paras. 38-41.

[99] LEC App. at 10.

[100] *In the Matter of Open Network Architecture Tariffs of Bell Operating Companies*, CC Docket No. 92-91, Order, 9 FCC Rcd 440, 454-55, paras. 36, 40, 41 (Dec. 15, 1993) (*ONA Tariff Order*); *Local Competition Order*, 11 FCC Rcd at 15911-12, paras. 825-26.

[101] To the extent that the *Bureau Order* required application of the new services test to non-BOCs, we hereby vacate that conclusion.

[102] *E.g.,* Public Serv. Comm'n of Md., *In the Matter of the Inquiry into the Payphone Tariffs of Bell Atlantic-Md., Inc.*, Case No. 8763, Order No. 76787 (Feb. 27, 2001).

[103] *E.g.,* Letter from James Connelly, Chairman, Mass. Dept. of Telecomms. & Energy, to Michael K. Powell, Chairman, FCC (March 5, 2001) (requesting decision on whether new services test applies to intrastate payphone line rates).

[104] LEC App. at 12. *See also Local Competition Order*, 11 FCC Rcd at 15846, para. 679 (defining TELRIC); *AT&T Corp. v. FCC*, 220 F.3d 607, 615-16 (2000) (same); *Video Dialtone Reconsideration Order*, 10 FCC Rcd at 340-47, paras. 209-22 (same).

costs.[105] Nothing in the *Payphone Orders* or section 276 supports this argument. In the *Payphone Orders,* the Commission adopted a new regulatory regime for payphone services, and we therefore required the application of the "new services" test to payphone line services, whether or not BOCs consider those services to be "new."

47. As we previously explained, "[b]ecause the incumbent LECs have used central office coin services in the past, but have not made these services available to independent [PSPs] for use in their provision of payphone services, we require that incumbent LECs' provision of payphone transmission services on an unbundled basis be treated as a new service under the Commission's price cap rules."[106] We noted that the new services test is necessary to ensure that central office coin services are priced reasonably because "incumbent LECs may have an incentive to charge their competitors unreasonably high prices for these services."[107] We stated that, because we required "dumb" lines to be re-priced on the same basis as "smart" lines, existing dumb lines would also have to meet the new services test.[108]

48. Second, the Coalition states that the pricing regime set forth in sections 251 and 252 does not apply to all section 276 payphone services offered by incumbent LECs.[109] We previously reached the same conclusion in the *First Payphone Order*.[110]

49. Finally, the LEC Coalition asserts that the *Bureau Order* mandates the exclusive use of the TELRIC pricing methodology and that this mandate is improper.[111] The *Bureau Order*, however, contains no such directive. Indeed, the *Bureau Order* states that the LECs should use a forward-looking methodology that is "consistent" with the *Local Competition Order*.[112] TELRIC is the specific forward-looking methodology described in 47 C.F.R. § 51.505 and required by our rules for use by states in determining UNE prices.[113] States often use "total service long run incremental cost" (TSLRIC) methodology in setting rates for intrastate services. It is consistent with the *Local Competition Order* for a state to use its accustomed TSLRIC methodology (or another forward-looking methodology) to develop the direct costs of payphone line service costs.[114]

50. As such, we do not impose on payphone line services the sections 251 and 252 pricing regime for local interconnection services. For example, while we have prohibited LECs

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[105] LEC Coalition's Reply in Support of Its Application for Review and Request for Stay at 7 (filed May 30, 2000) (LEC Reply).

[106] *First Payphone Order*, 11 FCC Rcd at 20614, para. 146.

[107] *Id.*

[108] *Id.*

[109] LEC App. at 14-15.

[110] *See First Payphone Order*, 11 FCC Rcd at 20615, para. 147.

[111] LEC App. at 9.

[112] *Bureau Order*, 15 FCC Rcd at 9981, para. 9.

[113] *Local Competition Order*, 11 FCC Rcd at 15844-46, paras. 672-78.

[114] *Id.* at 15845-46, paras. 677-78.

from including certain "retail" costs in their prices for UNEs,[115] no such prohibition applies to payphone line services. If they wish, the LECs may include in their direct cost calculations those "retail" costs, such as marketing and billing costs, that they can show are attributable to payphone line services.

C. OVERHEAD ALLOCATION AND LOADING FACTORS

51. With respect to overhead loading factors, the *Bureau Order* states that:

> the LECs must justify the methodology used to determine [payphone service] overhead costs. Absent justification, LECs may not recover a greater share of overheads in rates for the service under review than they recover in rates for comparable services. Given that the new services test is a cost-based test, overhead allocations must be based on costs, and therefore may not be set artificially high in order to subsidize or contribute to other LEC services. For purposes of justifying overhead allocations, UNEs appear to be "comparable services" to payphone line services, because both provide critical network functions to an incumbent LEC's competitors and both are subject to a "cost-based" pricing requirement. Thus, we expect incumbent LECs to explain any overhead allocations for their payphone line services that represent a significant departure from overhead allocations approved for UNE services.[116]

52. The *Bureau Order* correctly states our policy that our pricing requirements do not mandate uniform overhead loading, provided that the loading methodology as well as any deviation from it is justified.[117] As the above quotation shows, the Bureau approved the use of UNE loading factors to determine an appropriate overhead allocation for payphone services. We agree with the Bureau that UNE overhead loadings may be used in this manner, and states that have used this methodology are in full compliance with section 276 and our *Payphone Orders*. We do not agree, however, with the Bureau that UNE overhead loadings must serve as a default ceiling. There are other approaches that are also consistent with our precedent regarding overhead assignments to new services provided to competitors.

53. In the *Physical Collocation Tariff Order*,[118] we stated that, to calculate the appropriate overhead loading, the incumbent LECs must (1) compute the direct costs of providing the DS-1 and DS-3 services that compete with the services offered by collocated competitors; and (2) subtract those costs from the lowest rates charged for those services, taking

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115 *Id.* at 15851, para. 691.

116 *Bureau Order*, 15 FCC Rcd at 9982, para. 11.

117 *In the Matter of Local Exchange Carriers' Payphone Functions and Features*, CC Docket No. 97-140, Mem. Opinion and Order, 12 FCC Rcd 17996, 18002, para. 13 (Oct. 29, 1997) (*Payphone Features Order*); *Part 69/ONA Order*, 6 FCC Rcd at 4531, para. 44.

118 *Local Exchange Carriers' Rates, Terms, and Conditions for Expanded Interconnection Through Physical Collocation for Special Access and Switched Transport*, CC Docket No. 93-162, Second Report and Order, 12 FCC Rcd 18730 (June 13, 1997) (*Physical Collocation Tariff Order*).

into account all volume and term discounts.[119] The difference between the retail rates and the direct costs represents the contribution to overhead from these competitive services.[120] The Commission then prescribed overhead loading factors for each LEC's expanded interconnection services that did not exceed the lowest overhead loading resulting from the calculation described above.[121] By limiting the overheads applicable to expanded interconnection rates to the lowest overheads applied by LECs to competitive services, the Commission sought to prevent the incumbent LECs from disadvantaging competitors.[122]

54. We have expressed similar concerns about the potential for discriminatory practices in the context of payphone services.[123] Indeed, as we explained above, Congress expressly directed the Commission to prevent the BOCs from discriminating against competing PSPs in the provision of payphone services. For these reasons, we believe that it is appropriate for states to adopt the same method for calculating a ceiling for overhead allocation as we did in the *Physical Collocation Tariff Order*, recognizing that states that continue to use UNE overhead allocations for payphone services are also in full compliance with section 276 and our precedent. Moreover, it is also consistent with our past application of the price cap new services test, and permissible in this context, for states to determine overhead assignments using the methodology that the Commission used to evaluate the reasonableness of ONA tariffs in the *ONA Tariff Order*.[124] In that investigation, the Commission used ARMIS data to calculate an upper limit for both the ratio of direct cost to direct investment and the ratio of overhead cost to total cost. Analogously, states could use ARMIS data relating to the plant categories used to provide payphone services in calculating an upper limit on overhead loadings.

55. The LEC Coalition claims that BOCs are free to apply to payphone line service rates whatever markup over direct cost is incorporated in their business line rates, even though business line rates may include subsidies for other BOC services.[125] The Coalition asserts that BOCs have virtually unlimited flexibility in determining the overhead component of payphone line service rates because "the amount of overhead costs that are recovered in the rate does not affect whether the rate is based on costs."[126] The LEC Coalition argues that any overhead loading a BOC might choose is "reasonable" for purposes of the new services test so long as it is justified by "some plausible benchmark."[127]

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[119] *Id.* at 18858-59, para. 313.

[120] *Id.*

[121] *Id.* paras. 313-14.

[122] *Id.* at 18855, para. 307.

[123] *First Payphone Order*, 11 FCC Rcd at 20614, para. 146, and 20640, para. 199; *Payphone Reconsideration Order*, 11 FCC Rcd at 21308, para. 163.

[124] *In the Matter of Open Network Architecture Tariffs of Bell Operating Companies*, CC Docket No. 92-91, Order, 9 FCC Rcd 440, 458-59, para. 50, and 477-80, Attach. C (Dec. 15, 1993) (*ONA Tariff Order*).

[125] LEC Reply at 9.

[126] *Id.* at 10.

[127] *Id.* at 7.

56. We reject the LEC Coalition's argument. As noted above, under the new services test and our precedent, BOCs bear the burden of affirmatively justifying their overhead allocations. In general, in our decisions applying the new services test to services offered to competitors, we have allowed BOCs some flexibility in calculating overhead allocations, but we have carefully reviewed the reasonableness of BOCs' overhead allocations. We have *not* simply accepted any "plausible benchmark" proffered by an BOC.[128]

57. We also reject the Coalition's argument that the Commission's *Payphone Features Order*[129] supports the proposition that any overhead allocation within a wide range is "reasonable" for purposes of the new services test. In fact, that decision shows that our evaluation of overhead allocations under the new services test has been very fact-specific. We did permit an unusually high overhead loading in that matter based on adequate justification. We stressed, however, that our decision was specific to the circumstances of the particular investigation, which involved payphone features whose monthly costs did not exceed a few cents per line. We specifically ruled that "we do not find that it will necessarily be determinative in evaluating overhead loadings for other services."[130]

58. In sum, we establish a flexible approach to calculating BOCs' overhead allocation for intrastate payphone line rates. States may continue to use UNE loading factors to evaluate BOCs' overhead allocation for payphone services, but we do not require that UNE overhead allocations must serve as a ceiling on payphone service overhead loading. To evaluate such a ceiling, states should use the methodology from either the Commission's *Physical Collocation Tariff Order* or *ONA Tariff Order*. Consistent with Commission precedent, the BOCs bear the burden of justifying their overhead allocations for payphone services and demonstrating compliance with our standards.

D. ADJUSTMENT FOR FEDERALLY TARIFFED COMMON LINE CHARGES

59. The *Bureau Order* stated that "cost based" payphone line service rates calculated pursuant to the *Payphone Order* requirements must be adjusted to take account of federally tariffed charges, *i.e.*, the SLC and PICC.[131] We affirm this requirement with respect to the SLC but not with respect to the PICC.

60. Under the new services test, the BOC may not charge more for payphone line service than is necessary to recover from PSPs all monthly recurring direct and overhead costs incurred by BOCs in providing payphone lines. The forward-looking cost studies used to make these determinations are usually calculations of total costs, not jurisdictionally separated costs. If an incumbent BOC files in its state tariff a charge that fully recovers these unseparated costs and also assesses on the PSP its federally tariffed SLC, the BOC will over-recover its costs, and the PSP will over-pay, in violation of the new services test and the cost-based rates requirement of

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[128] *See, e.g., ONA Tariff Order,* 9 FCC Rcd at 455, para. 40; *Physical Collocation Tariff Order*, 12 FCC Rcd at 18856, paras. 308-09.

[129] *Payphone Features Order,* 12 FCC Rcd 17996.

[130] *Id.* at 18003, para. 13.

[131] *See supra* note 63 and accompanying text.

the *Payphone Orders*. The multiline business PICC, on the other hand, does not recover the costs of the lines on which it is assessed. Rather, it recovers costs that would be recovered through charges on residential and single line business lines, if those charges were not capped.[132] It is a temporary subsidy element that is being phased out of the interstate access charge system.[133] PICC revenues should not, therefore, be subtracted in determining a forward-looking cost-based rate for payphone lines.

61. Therefore, in establishing its cost-based, state-tariffed charge for payphone line service, a BOC must reduce the monthly per line charge determined under the new services test by the amount of the applicable federally tariffed SLC. Verizon contends that cost-based rates need only be adjusted to account for SLC rate levels as of April 1997.[134] We disagree. At whatever point in time a state reviews a BOC's payphone line rates for compliance with the new services test, it must apply an offset for the SLC that is then in effect.

E. COST SUPPORT FOR USAGE ELEMENTS

62. The *Bureau Order* stated that the new services test applies to usage sensitive as well as flat-rate elements of the services offered to PSPs. We affirm.

63. The LEC Coalition argues that, in the *Payphone Orders*, we only required the new services test to be applied to the monthly rate for the payphone line.[135] Two years ago, however, the Bureau clarified that the new services test applies to all payphone line service rates, including per-call or per-minute rates applicable to local usage.[136] Nevertheless, the Coalition contends that we did not require application of the test to local usage rates that are uniformly applicable to PSPs and business line subscribers. According to the LEC Coalition, rates that are equal to business usage rates are not "payphone-specific" and were not intended to be covered by the new services test.[137]

64. We reject the LEC Coalition's interpretation of the Commission's orders. In the *Payphone Orders*, we required LECs to provide PSPs with local exchange services that would enable payphone service providers to offer payphone service using either "smart" or "dumb" payphones.[138] Providing only a line, without allowing local calls over the line, does not satisfy

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[132] *In the Matter of Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Low-Volume Long-Distance Users, Federal-State Joint Board on Universal Service*, CC Docket Nos. 96-262, 94-1, 99-249, and 96-45, Report and Order, 15 FCC Rcd 12962, 13004, para. 106 (May 31, 2000). We note that parties have filed a reconsideration petition seeking relief from application of the multiline business PICC to payphone lines. This petition is currently pending.

[133] *Id.*

[134] Response of Verizon North at 6-7 (filed Oct. 23, 2000) (Verizon Response).

[135] LEC App. at 16 n.14; Verizon Response at 12-14.

[136] Letter from Yog R. Varma, Deputy Chief, Common Carrier Bureau, to Caroline Vachier, Deputy Attorney General of New Jersey, 14 FCC Rcd 17091, 17092 (Oct. 5, 1999).

[137] LEC App. at 16 n.14.

[138] *Payphone Reconsideration Order*, 11 FCC Rcd at 21307-08, para. 162.

this requirement.[139] We required these payphone line services to be priced at cost-based rates in accordance with the new services test.[140] Therefore, any rate for local usage billed to a payphone line, as well as the monthly payphone line rate, must be cost-based and priced in accordance with the new services test. This requirement applies regardless of whether current payphone line service tariffs specify a particular rate for payphone line usage, or whether they currently incorporate by reference the applicable rate from a business service tariff.

65. This conclusion advances our purpose in requiring cost-based payphone line rates in the first place. A high usage rate would undermine our and the states' efforts to set the payphone service rates in accordance with a cost-based standard. A non-cost-based usage rate would also constitute an impermissible "end run" around the requirements of section 276.

F. WISCONSIN PAYPHONE RATES

66. We do not now review or evaluate the cost support materials submitted by Ameritech and Verizon. We urge the Wisconsin Commission to review its jurisidiction to apply the new services test in light of the fact that, as we have described above, it is intended to address potentially discriminatory practices in accordance with the requirements of section 276 and would seem to be within the Wisconsin Commission's authority to prevent such discrimination.[141]

67. We also relieve TDS and Century, and by extension other small rural incumbent LECs, of the obligation to comply with the application of the new services test as set forth herein. Neither TDS nor Century are BOCs, and, as we have discussed above, our federal jurisdiction to apply the new services test was intended to reach BOCs only.[142] Nevertheless, nothing prevents states from applying the new services test to all non-BOC LECs, whether rural or not, but we conclude that the states themselves should determine whether that is appropriate and warranted.[143]

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[139] The LEC Coalition cites a prior Bureau order discussing "payphone specific" services in support of its position that a BOC may exempt local usage from *Payphone Orders* requirements by not including local usage rates in a "payphone specific" tariff or by not offering local usage at a "payphone specific" rate. LEC App. at 16 n.14. The Bureau used the term "payphone specific" to distinguish those network "features and functions" that must be *federally tariffed* from those that may be offered solely under *state tariffs*. Nothing in the Bureau's orders supports the proposition that a BOC could avoid subjecting necessary network services, such as local usage, to any of the *Payphone Orders'* tariffing requirements, under *either* federal *or* state tariffs, by the simple device of tariffing those services in a "non-payphone-specific" manner.

[140] *Payphone Reconsideration Order*, 11 FCC Rcd at 21308, para. 163 & n.492.

[141] *See supra* note 45 and accompanying text.

[142] *See supra* para. 42.

[143] *See also id.*

IV. CONCLUSION

68. In sum, we issue this *Order* to assist states in determining whether BOCs' intrastate payphone line rates comply with section 276 and our *Payphone Orders*. This *Order* includes the following basic propositions: First, BOCs' intrastate payphone line rates, including usage rates, should comply with the flexible, cost-based new services test. Second, these rates should be calculated using a forward-looking, direct cost methodology such as TELRIC or TSLRIC, but the full pricing regime of sections 251 and 252 does not apply. Third, overhead loading rates for payphone line rates should be cost-based, and such rates may be calculated using UNE overhead loading factors, provided that such rates do not exceed an upper limit calculated using the methodology from either the *Physical Collocation Tariff Order* or the *ONA Tariff Order*. Finally, BOCs' payphone line rates should be adjusted to account for SLC charges, as set forth herein.

V. ORDERING CLAUSES

69. Accordingly, pursuant to sections 4(i), 205, and 276 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 205, and 276, IT IS HEREBY ORDERED that the Application for Review of the LEC Coalition is hereby GRANTED and that the LEC Coalition's request that we withdraw or stay the *Bureau Order* is hereby DENIED.

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton
Acting Secretary