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

In the Matter of	)	
	)	
2001 Annual Access Tariff Filings	)	CC Docket No. 01-206
	)	
	)	
	)	

ORDER DESIGNATING ISSUES
FOR INVESTIGATION

Adopted: August 28, 2001 **Released:** August 29, 2001

Direct Case Due Date: September 12, 2001
Oppositions to Direct Case Due Date: September 26, 2001
Rebuttal Due Date: October 3, 2001

By the Chief, Common Carrier Bureau:

I. INTRODUCTION

1. On July 2, 2001, we released the *2001 Annual Access Tariff Filings Suspension Order*,[1] which, *inter alia*, suspended for five months and set for investigation the rates for the traffic sensitive basket filed by Moultrie Independent Telephone Company, Inc. (Moultrie). In the *2001 Annual Access Tariff Filings Suspension Order*, we also suspended for one day several local exchange carriers' (LECs') 2001 annual access tariffs in certain areas, imposed an accounting order, and initiated an investigation into the lawfulness of a number of issues raised by these tariff filings. We subsequently reconsidered on our own motion our decision to suspend and investigate the proposed multi-line business subscriber line charges of Ameritech Operating Companies, Frontier Telephone of Rochester, Inc., Pacific Bell Telephone Company, Qwest Communications, Inc., and Sprint Local Telephone Companies-Nevada.[2]

2. In this Order, we designate for investigation issues regarding Moultrie's treatment of costs related to the sale/lease back of assets to and from an affiliated company, as reflected in the traffic sensitive rates submitted by Moultrie in its tariff revision in Transmittal Number 4 to Tariff FCC Number 1. We also designate for investigation issues regarding ALLTEL Telephone

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[1] *2001 Annual Access Tariff Filings*, CCB/CPD File No. 01-08, Memorandum Opinion and Order, DA 01-1563 (Comp. Pric. Div. rel. July 2, 2001) (*2001 Annual Access Tariff Filings Suspension Order*).

[2] *2001 Annual Access Tariff Filings*, CCB/CPD File No. 01-08, Order on Reconsideration, DA 01-1841 (Comp. Pric. Div. rel. July 31, 2001).

Systems' (ALLTEL's) derivation of a dial equipment minutes (DEM) allocation factor in setting local switching rates in Transmittal Number 90 to its Tariff FCC Number 1.

II. ISSUES DESIGNATED FOR INVESTIGATION

A. Moultrie's Calculation of Sale/Lease Back Costs

1. Background

3. Moultrie is a rural independent LEC serving 853 access lines in central Illinois.[3] In 1997, Moultrie transferred ownership of certain non-loop-related assets to an affiliate and leased them back.[4] This transaction was designed to maximize Moultrie's USF support recovery.[5] In reporting the transaction to NECA for determining its USF support allocation, Moultrie applied the Commission's part 32 accounting rules, which would allow Moultrie to remove the investment of the sold assets from its cost calculations while including the lease payments to the affiliate in its operating expenses. As a result of this transaction, Moultrie's loop cost and expense adjustment data for1997 increased significantly.[6] The calculation used to derive USF loop costs compares a company's loop-related investment to total investment. After the sale of its non-loop assets, Moultrie's loop investment represented a much higher percentage of its total company investments. Specifically, the sale/lease-back transaction as reported by Moultrie for purposes of calculating USF support would have increased Moultrie's USF support by 2887 percent, from $15 per loop per year to $433 per loop per year.[7]

4. On March 8, 1999, NECA sought a determination from the Common Carrier Bureau as to the calculation of USF expense adjustments when affiliate sale/lease-back arrangements are involved.[8] NECA noted that Moultrie's lease rates were in conformance with the Commission's part 32 rules, but questioned whether Moultrie should have applied section 36.2(c)(2) of the Commission's rules, which applies to property rental that is substantial in amount. Section 36.2(c)(2) applies to affiliate sale/lease-back arrangements for cost separation purposes, and requires the seller/transferor to include the property and related expenses and

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[3] *See* Letter from David A. Irwin, Irwin, Campbell & Tannenwald, P.C., to Dorothy Attwood, Chief, Federal Communications Commission Common Carrier Bureau at 2 (Feb. 2, 2001) (Moultrie Feb. 2, 2001 *Ex Parte* Letter).

[4] *See* Moultrie Independent Telephone Company Petition for Declaratory Ruling, CC Docket No. 96-45 at 5 (filed Mar. 29, 1999) (Moultrie Petition). These assets include motor vehicles, other work equipment, land and buildings, furniture, office equipment, general purpose computers, circuit equipment, and non-loop-related buried cable. *See* Letter from Gina Harrison, Senior Counsel and Director, NECA Washington Office, to Magalie Roman Salas, Secretary, Federal Communications Commission at 2 (Mar. 10, 1999) (NECA Mar. 10, 1999 *Ex Parte* Letter).

[5] In its petition, Moultrie states, "Moultrie structured the transfer to optimize its recovery under the USF and to maximize tax benefits." Moultrie Petition at 5.

[6] *See* NECA Mar. 10, 1999 *Ex Parte* Letter at 2.

[7] *See* NECA Mar. 10, 1999 *Ex Parte* Letter at 3.

[8] NECA Mar. 10, 1999 *Ex Parte* Letter at 3.

exclude rent expenses from its own account.[9] Moultrie filed a Petition for Declaratory Ruling on March 29, 1999, seeking clarification of the "patent ambiguity" between sections 32.27(a)-(c) and 36.2(a) and (c) of the Commissions rules.[10]

5. The Bureau provided guidance on this issue by letter on August 4, 1999.[11] According to the Bureau, subpart F of part 36 of the Commission's rules governs USF.[12] Section 36.2 of part 36 sets out the basic principles that govern all of part 36, including subpart F.[13] Therefore, the underlying principle of section 36.2(c)(2) regarding treatment of property sold to and rented from affiliates applies to USF expense adjustment computations under part 36.[14] The Bureau further stated that Moultrie's sale/lease-back arrangement described by NECA should be accounted for under section 36.2(c)(2), i.e., by including the property and related expenses with, and excluding the rent expenses from, the carrier's regulated telephone operations.[15]

6. Based upon this guidance, NECA requested Moultrie to file amended cost studies reflecting the sale/lease-back arrangement in accordance with section 36.2(c)(2). Moultrie refused to do so.[16] As a result, the Universal Service Administrative Company (USAC), the administrative body tasked with administering USF support, determined that it could no longer rely on the cost data submitted by Moultrie and suspended all high cost loop and local switching support USF payments to Moultrie, effective January 1, 2001.[17] When Moultrie filed its 2001 annual access tariff filing, it proposed to increase its local switching rate by more than 335 percent, from $0.05713 per minute to $0.191586 per minute, to reflect the loss of USF switching

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9 47 C.F.R. § 36.2(c)(2).

10 Moultrie Petition at 1. Moultrie has also filed a Motion for Stay of section 69.605 of the Commission's rules to preclude NECA from collecting cost information from Moultrie until the Commission rules on the Petition for Declaratory Ruling. Moultrie Independent Telephone Company Motion for Stay of Section 69.605 of the Commission's Rules, CC Docket No. 96-45 (filed Feb. 2, 2001) (Motion for Stay). *See also* Moultrie Independent Telephone Company Amendment to Petition for Declaratory Ruling, CC Docket No. 96-45 (filed Apr. 6, 1999) (requesting the Commission to direct NECA to re-open the 24-month window in which members may adjust cost studies); *and* Moultrie Independent Telephone Company Amendment to Motion for Stay of Section 69.605 of the Commission's Rules, CC Docket No. 96-45 (filed Feb. 6, 2001) (requesting expedited action on the Motion for Stay).

11 Letter from Lisa Zaina, Acting Deputy, Federal Communications Commission Common Carrier Bureau, to John A. Ricker, Executive Director-Universal Service Program Support, National Exchange Carrier Association, Inc. (Aug. 4, 1999) (Aug. 4 Bureau Letter).

12 *See* 47 C.F.R. §§ 36.601 to 36.641.

13 *See* 47 C.F.R. § 36.2(a).

14 *See* Aug. 4 Bureau Letter at 1.

15 *See* Aug. 4 Bureau Letter at 1-2.

16 *See* Letter from David A. Irwin, Irwin, Campbell & Tannenwald, P.C., to Jane Mago, General Counsel, Federal Communications Commission, Attachment (July 17, 2001).

17 *See* Letter from David A. Irwin, Irwin, Campbell & Tannenwald, P.C., to Dorothy Attwood, Chief, Federal Communications Commission Common Carrier Bureau, Attachment (Dec. 29, 2000).

support payments.[18] The Competitive Pricing Division suspended and set this rate for investigation on July 2, 2001.[19]

2. Discussion

7. The issue before us in this investigation is the increase in Moultrie's traffic sensitive rates, particularly of its local switching per minute rate. Moultrie attributes the major increase in this rate to its loss of USF local switching support. This non-payment of USF switching support stems from Moultrie's ongoing dispute with NECA regarding the treatment of affiliate sale/lease-back transactions for purposes of calculating USF support, as described above. If Moultrie correctly calculated its costs, then it should receive USF support from USAC and its local switching rates should be reduced. If Moultrie did not correctly calculate its costs, then Moultrie should not be able to benefit from this miscalculation at the expense of local switching ratepayers, but should recalculate its costs so it can be determined what the correct level of USF support would be and correspondingly what the correct local switching rates would be.

8. We direct Moultrie to provide in its direct case a detailed explanation of why it is appropriate for it to increase its local switching rate to recover from ratepayers any amount of USF support that it is not receiving due to the dispute over its affiliate sale/lease-back transaction. We further direct Moultrie to provide evidence demonstrating that the increase in switching rates would recover only Moultrie's switching revenue requirement and would not be used to compensate for Moultrie's loss of USF support for other network elements. Moultrie should provide data explaining how it determined its interstate local switching rate, including all the elements used to calculate the revenue requirement and its usage estimates. We direct Moultrie to provide this same information for the three years prior to its entering into the sale/lease-back arrangement with its affiliate. We also direct Moultrie to submit a cost study recalculating its costs by including the property and related expenses with, and excluding the related rent expenses from, its regulated telephone operations. Moultrie should also calculate the USF local switching support to which it would be entitled under this revised cost study, and should recalculate its proposed local switching rate after taking account of this support.

B. ALLTEL's DEM Allocation Factor

1. Background

9. DEM factors are used in calculating access services costs and in allocating local switching equipment investment costs between the interstate and intrastate jurisdictions. DEMs are defined in section 36.125(a)(3) of the Commission's rules as the minutes of holding time of the originating and terminating local switching equipment.[20] For each one-minute call, there is

[18] *See* Letter from Steve Bowers, President, Moultrie Independent Telephone Company, Inc., to Secretary, FCC, Description and Justification (June 18, 2001) (Moultrie Transmittal No. 4).

[19] *2001 Annual Access Tariff Filings Suspension Order* para. 5.

[20] 47 C.F.R. § 36.125(a)(3). Holding time is the time in which an item of telephone plant is in actual use either by a customer or an operator. 47 C.F.R. Part 36 Appendix-Glossary.

one minute during which the switching equipment originating the call is in use (an originating minute), and one minute during which the terminating switching equipment is in use (a terminating minute). The interstate DEM factor is the ratio of the interstate DEM to the total DEM.[21] On June 25, 2001, AT&T filed a petition seeking suspension and investigation of several LECs' annual access tariff filings.[22] Among the issues identified as problematic by AT&T was ALLTEL's proposed increase in its interstate DEM allocation factor.[23] Specifically, AT&T argued that ALLTEL's DEM factors have been decreasing, and, according to a linear regression analysis, should continue to decrease, but ALLTEL has proposed to increase its interstate DEM factor.[24]

10. ALLTEL responded by explaining that its interstate DEM factor had increased because it had changed the method it used for estimating terminating interlocal minutes of use.[25] For shared trunks carrying both toll and interlocal traffic, ALLTEL is able to determine the number of originating minutes of traffic placed by its customers that are attributable to toll and interlocal calls. It is not able to determine how many minutes of terminating traffic, calls placed by other carriers' customers, are toll and how many are interlocal because switch measurements can not determine where an incoming call originated. Historically, ALLTEL had counted one terminating minute for each originating interlocal minute over these shared trunks. In 2000, however, ALLTEL conducted traffic studies which indicated that Internet traffic does not follow this one-terminating-to-one-originating-minute relationship.[26] Instead, ALLTEL determined that applying a factor of 0.5 to its number of originating Internet minutes more accurately represented the number of terminating Internet minutes it received over the shared trunks.[27] This is because ALLTEL's customers call ISPs, creating originating minutes, but ISPs do not call back, therefore ALLTEL was not receiving terminating minutes corresponding to these originated Internet calls. For purposes of calculating its DEM factor, ALLTEL applied a one-terminating-to-one-originating relationship only to non-Internet interlocal traffic, and applied a factor of 0.5 to Internet interlocal originating minutes to derive Internet interlocal terminating minutes (i.e., a one-terminating-to-two-originating minutes relationship). ALLTEL assigned all originating interlocal traffic, including Internet, plus the lower number of derived interlocal terminating

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21 47 C.F.R. § 36.125(a)(5).

22 Petition of AT&T Corp., CCB/CPD File No. 01-08 (filed June 25, 2001) (AT&T Petition).

23 AT&T Petition at 33-35, Exhibit 14. AT&T also provided information on Western Reserve's and TXU Communications' interstate DEM allocation factors, but we declined to investigate these carriers' DEM factors.

24 AT&T Petition at 33-34, Exhibit 14.

25 Reply Comments of ALLTEL Corporation, CCB/CPD File No. 01-08, DA 01-1105 (filed June 29, 2001) (ALLTEL Reply).

26 ALLTEL Reply at 1.

27 To determine the number of its originating Internet minutes, ALLTEL identified numbers with high call durations, i.e., calls that lasted for more than 60 minutes with at least 500 total minutes to the number per month. ALLTEL then called the numbers to which these calls were placed. Any numbers that were answered with a modem tone were determined to be ISP numbers and the corresponding minutes were determined to be Internet minutes. *See* Letter from David Bartlett, ALLTEL Corporation, to Magalie Roman Salas, Secretary, Federal Communications Commission (July 23, 2001) (ALLTEL July 23 *Ex Parte* Letter).

traffic to the local jurisdiction. This decrease in the number of minutes attributed as interlocal terminating minutes reduced the total amount of traffic allocated as interlocal, and created a corresponding increase in traffic allocated to other jurisdictions, including interstate.[28] Therefore, ALLTEL's decision to apply a 0.5 factor rather than a 1.0 factor to terminating Internet interlocal traffic caused its interstate DEM allocation factor to increase. This change increased interstate costs, but left interstate minutes unchanged, resulting in a proposed increase to ALLTEL's interstate charge for a minute of use of its switches.

2. Discussion

11. We question ALLTEL's method of setting its interstate DEM allocation factor. ALLTEL's description of the method it used to count Internet traffic appears to be based on switched minutes of use (SMOU).[29] The difference between a SMOU factor and a DEM factor is that SMOU counts each minute of use only once, while DEM counts each minute of a local call twice, as one originating and one terminating minute.[30] The Commission rejected the use of SMOU as an allocator for switching investment in favor of a DEM allocator in 1987.[31] In an order released earlier this year, the Commission affirmed that under section 36.125(a)(3), each minute of use is counted as two DEMs for local calls.[32]

12. Even if ALLTEL is correct in asserting that it has less terminating than originating interlocal minutes due to outgoing calls to ISPs from its customers, ALLTEL still must demonstrate that its method of calculating the interstate DEM factor comports with the Commission's rules. In the *Separations Freeze* proceeding, the Commission considered and rejected a proposal from the Joint Board to lower and freeze the local DEM at 95 percent of the current year level due to imbalance in Internet traffic.[33] The Common Carrier Bureau sought

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28 ALLTEL Reply at 1-2.

29 *See Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Recommended Decision and Order, 12 FCC Rcd 2551, 2554, para. 26 (Fed.-State Joint Bd., 1987) (*Joint Board Recommended Decision*).

30 *See id.*; *Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Order Inviting Comments and Request for Data, 2 FCC Rcd 3787, 3788, para. 7 (Fed.-State Joint Bd., 1987).

31 *See MTS and WATS Market Structure, Amendment of Part 67 (New Part 36) of the Commission's Rules and Establishment of a Federal-State Joint Board*, CC Docket Nos. 78-72, 80-286, and 86-297, Report and Order, 12 FCC Rcd 2639, 2640, 2642, paras. 5 and 15 (1987) (adopting the Joint Board's recommendation to use study area measured DEM as the investment allocator for switching equipment). *See also Joint Board Recommended Decision*, 12 FCC Rcd at 2559, para. 48 (the Joint Board found that DEM better reflected the relative state and interstate usage of local dial switching equipment than the other allocators proposed, including SMOU).

32 *General Communication, Inc. v. Alaska Communications Sys. Holdings, Inc.*, EB-00-MD-016, Memorandum Opinion and Order, FCC 01-32, paras. 43-44 (rel. Jan. 24, 2001) (holding that a one-minute intraoffice call generates two DEMs; one originating and one terminating minute).

33 *Jurisdictional Separations and Referral to the Federal-State Joint Board*, CC Docket No. 80-286, Report and Order, FCC 01-162, paras. 34-35 (rel. May 22, 2001) (*Separations Freeze Order*).

comment on the Internet/DEM reduction issue as framed by the Joint Board.[34] The Commission, however, found that the commenters had not supplied reliable data upon which to set the amount of any local DEM factor reduction that might be warranted.[35] Instead, the Commission committed to seek specific comment on the status of this issue when it examines the effects of the separations freeze, and to work with the Joint Board to address the impact of the Internet and the growth of local minutes during the interim freeze.[36]

13. ALLTEL's computation of its interstate DEM allocation factor appears inconsistent with the current practice of calculating DEMs under section 36.125(a)(3) of the Commission's rules. ALLTEL asserts that it has an imbalance of originating to terminating traffic because its customers call ISPs in other LECs' calling areas and ALLTEL's customers do not receive terminating calls from these ISPs. The DEM allocation factor, however, does not address traffic imbalances. Historically there have been many types of traffic imbalances. For example, generally terminating minutes exceed originating minutes for interstate traffic.[37] Carriers are not allowed to choose which types of traffic imbalances they correct in their DEM allocation factor under the Commission's rules.

14. We direct ALLTEL to submit, as part of its direct case, a recalculated DEM factor counting one terminating minute for each originating minute for all traffic, including Internet traffic. ALLTEL must provide the data underlying this recalculated DEM factor. In accordance with the *Separations Freeze Order*, ALLTEL should use only data from calendar year 2000 in calculating its DEM allocation factor.[38]

III. PROCEDURAL MATTERS

A. Filing Schedules

15. This investigation will be conducted as a notice and comment proceeding, for which we have designated CC Docket No. 01-206. Moultrie Independent Telephone Company, Inc. and ALLTEL Telephone Systems are the parties designated to this investigation.

16. These parties shall file their direct cases no later than **September 12, 2001.** The direct cases must present the parties' positions with respect to the issues described in this Order. Pleadings responding to the direct cases may be filed no later than **September 26, 2001**, and

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[34] *Separations Freeze Order* at para. 36; *Comment Sought on Recommended Decision Issued By Federal-State Joint Board on Jurisdictional Separations*, CC Docket No. 80-286, Public Notice, 15 FCC Rcd 25580 (2000).

[35] *Separations Freeze Order* at para. 40 ("We have no reliable data, therefore, upon which to set any reasonable local DEM reduction on an across-the-board, nationwide basis in order to compensate for any effects that Internet usage may have had on jurisdictional allocations or consumers.").

[36] *Separations Freeze Order* at para. 42.

[37] *See, e.g., Statistics of Communications Common Carriers*, Federal Communications Commission, Table 2.20 (1998/1999 ed.).

[38] *See Separations Freeze Order* at para. 27.

must be captioned "Oppositions to Direct Case" or "Comments on Direct Case." The companies may each file a "Rebuttal" to oppositions or comments no later than **October 3, 2001**.

17. An original and four copies of all pleadings shall be filed with the Secretary of the Commission. In addition, parties shall serve with three copies: Competitive Pricing Division, Common Carrier Bureau, 445 12th Street, S.W., Room 5-A452, Washington, D.C. 20554, Attn: Jennifer McKee. Parties shall also serve with one copy: Qualex International, Portals II, 445 12th Street, S.W., Room CY-B402, Washington, D.C. 20554, (202) 863-2893. Members of the general public who wish to express their views in an informal manner regarding the issues in this investigation may do so by submitting one copy of their comments to the Office of the Secretary, Federal Communications Commission, 445 12th Street, S.W., Room TW-A325, Washington, D.C. 20554. Such comments should specify the docket number of this investigation, CC Docket No. 01-206. Parties are also encouraged to submit their pleadings via the Internet through the Electronic Comment Filing System at <http://www.fcc.gov/e-file/ecfs.html>. Generally, only one copy of an electronic submission must be filed. In completing the transmittal screen, commenters should include their full name, Postal Service mailing address, and the applicable docket number, which in this instance is CC Docket No. 01-206. Parties may also submit an electronic comment via Internet e-mail. To get filing instructions for e-mail comments, commenters should send an e-mail to <ecfs@fcc.gov>, and should include the following words in the body of the message: "get form <your e-mail address>." A sample form and directions will be sent in reply.

18. All relevant and timely pleadings will be considered by the Commission. In reaching a decision, the Commission may take into account information and ideas not contained in pleadings, provided that such information, or a writing containing the nature and source of such information, is placed in the public file, and provided that the fact of reliance on such information is noted in the order.

B. *Ex Parte* Requirements

Pursuant to 47 C.F.R. § 1.1200(a), which permits the Commission to adopt modified or more stringent *ex parte* procedures in particular proceedings if the public interest so requires, this proceeding will be governed by "permit-but-disclose" *ex parte* procedures that are applicable to non-restricted proceedings under 47 C.F.R. § 1.1206. Designating this proceeding as "permit-but-disclose" will provide an opportunity for all interested parties to receive notice of the various technical, legal, and policy issues raised in *ex parte* presentations made to the Commission in the course of this proceeding. This will allow interested parties to file responses or rebuttals to proposals made on the record in this proceeding. Accordingly, we find that it is in the public interest to designate this proceeding as "permit-but-disclose."

19. Parties making oral *ex parte* presentations are reminded that memoranda summarizing the presentation must contain a summary of the substance of the presentation and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented generally is required. *See* 47 C.F.R. § 1.1206(b)(2), as revised. Other rules pertaining to oral and written presentations are set forth in section 1.206(b) as well. Interested parties are to file any written *ex parte* presentations in this proceeding with the Commission Secretary, Magalie Roman Salas, 445 12th Street, S.W., TW-B204, Washington,

D.C. 20554, and serve with three copies: Competitive Pricing Division, Common Carrier Bureau, 445 12th Street, S.W., Room 5-A452, Washington, D.C. 20554, Attn: Jennifer McKee. Parties shall also serve with one copy: Qualex International, Portals II, 445 12th Street, S.W., Room CY-B402, Washington, D.C. 20554, (202) 863-2893.

C. Paperwork Reduction Act

20. This Order Designating Issues for Investigation contains no new or modified information collections subject to the Paperwork Reduction Act of 1995, Pub. Law 104-13.

IV. ORDERING CLAUSES

21. IT IS ORDERED that, pursuant to sections 4(i), 4(j), 201(b), 203(c), 204(a), 205, and 403 of the Communications Act, 47 U.S.C. §§ 154(i), 154(j), 201(b), 203(c), 204(a), 205, and 403, and sections 0.91 and 0.291 of the Commission's rules, 47 C.F.R. §§ 0.91, 0.291, the issues set forth in this Order ARE DESIGNATED FOR INVESTIGATION.

22. IT IS FURTHER ORDERED that Moultrie Independent Telephone Company, Inc. and ALLTEL Telephone Systems SHALL BE parties to this proceeding.

23. IT IS FURTHER ORDERED that each local exchange carrier that is a party to this proceeding SHALL INCLUDE, in its direct case, a response to each request for information that it is required to answer in this Order.

FEDERAL COMMUNICATIONS COMMISSION

Dorothy T. Attwood
Chief, Common Carrier Bureau