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WSR # 98-19-147

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

In the Matter of Adopting	)	DOCKET NO. UT-970325
	)	
WAC 480-120-540	)	GENERAL ORDER NO. R-450
	)	
Relating to Intrastate Carrier Access Charge	)	
Reform.	)	ORDER ADOPTING RULES
	)	PERMANENTLY
. . . .	)	

STATUTORY OR OTHER AUTHORITY: The Washington Utilities and Transportation Commission takes this action under Notice WSR # 98-11-082, filed with the Code Reviser on May 19, 1998. The Commission brings this proceeding pursuant to RCW 80.01.040, 80.04.160, and 80.36.140.

STATEMENT OF COMPLIANCE: This proceeding complies with the Open Public Meetings Act (chapter 42.30 RCW), the Administrative Procedure Act (chapter 34.05 RCW), the State Register Act (chapter 34.08 RCW), the State Environmental Policy Act of 1971 (chapter 34.21C RCW), and the Regulatory Fairness Act (chapter 19.85 RCW).

DATE OF ADOPTION: The Commission adopted this rule on June 25, 1998.

CONCISE STATEMENT OF PURPOSE AND EFFECT OF THE RULE: The rule conforms Washington’s telecommunications access charge system with state and federal laws encouraging competition. The rule will convert a pricing structure that retards competition to one designed to support emerging competition without favoring any class of participants. Ultimately this will enable greater customer choice throughout the state of Washington.

REFERENCE TO AFFECTED RULES: This rule adopts the following section of the Washington Administrative Code (WAC):

WAC 480-120-540 - Terminating Access Charges.

PREPROPOSAL STATEMENT OF INQUIRY AND ACTIONS THEREUNDER: The Commission filed a Preproposal Statement of Inquiry (CR-101) on October 22, 1997, at WSR # 97-21-153.

ADDITIONAL NOTICE AND ACTIVITY PURSUANT TO PREPROPOSAL STATEMENT: The statement advised interested persons that the Commission was considering entering a rulemaking on Access Charge Reform and the Cost of Universal Service. The Commission also informed persons of the inquiry into this matter by providing notice of the subject and the CR-101 to all persons on the Commission's list of persons requesting such information pursuant to RCW 34.05.320(3), providing notice to all registered telecommunications companies, and by providing notice to the Commission's list of telecommunications attorneys.

Pursuant to the notice, the Commission convened a workshop on Tuesday, January 13, 1998. The Commission followed that workshop with a January 21, 1998, notice of opportunity to file comments on the potential approaches to access charge reform and how each might affect companies, customers, and small businesses. A notice dated March 13, 1998, provided an opportunity to file reply comments and an opportunity to respond to Commission Staff's revised proposal. Seven parties responded to the CR-101, sixty-four individuals attended the workshop, eleven parties responded to the January notice, and twelve parties responded to the March notice.

Commission Staff recruited representatives of several small telephone companies, a large telephone company, Public Counsel, a few small business associations, and some Chambers of Commerce to serve on a small business economic impact statement study group. Commission Staff served a small business economic impact statement questionnaire on all local exchange companies to gain more information and a broader perspective regarding the proportionate cost impacts of the rule on small businesses. Twenty-four companies responded to the questionnaire. The results are summarized in the final Small Business Economic Impact Statement (SBEIS). This information and the participation of the Committee members led to the mitigations that the Commission adopted.

NOTICE OF PROPOSED RULEMAKING: The Commission filed a notice of Proposed Rulemaking (CR-102) on May 19, 1998, at WSR #98-11-082. The Commission scheduled this matter for oral comment and adoption under Notice WSR #98-11-082 on Thursday, June 25, 1998 in the Commission's Hearing Room, Second Floor, Chandler Plaza Building, 1300 S. Evergreen Park Drive S.W., Olympia, Washington. The Notice also provided interested persons the opportunity to submit written comments to the Commission.

COMMENTERS (WRITTEN COMMENTS):The Commission received written comments from AT&T Communications of the Pacific Northwest, Inc. ("AT&T"), the United States Department of Defense and all Federal Executive Agencies ("DOD/FEA"), GTE Northwest Incorporated (GTE-NW), the Independent Business Association ("IBA"), MCI Telecommunications Corporation ("MCI"), the Public Counsel Section of the Washington Attorney General and the American Association of Retired Persons ("PC/AARP"), Sprint

Corporation on behalf of Sprint Communications Company LP and United Telephone Company of the Northwest (“Sprint”), Teleport Communications Group/TCG Seattle (“TCG”), Telecommunications Ratepayers for Cost-based and Equitable Rates (“TRACER”), U S WEST Communications, Inc. (USWC or U S WEST), the Washington Independent Telephone Association (“WITA”), and WorldCom, Inc. (“WorldCom”).

Based on the comments and on all interaction with the public, Commission Staff suggested revised and clarified language, called the “clarification” in this order, without changing the intent or ultimate effect of the proposed rule. Staff distributed clarification to the commenting parties and other interested persons on the Commission’s list for this proceeding on June 17, 1998.

RULEMAKING HEARING: The rule proposal was considered for adoption, pursuant to the notice, on Thursday, June 25, 1998, before Chairwoman Anne Levinson, Commissioner Richard Hemstad, and Commissioner William R. Gillis. The Commission heard oral comments from Tim Zawislak and Glenn Blackmon, representing Commission Staff; Tom Vogel, representing GTE; Robert Snyder, representing Whidbey Telephone Company; Tim Peters, representing Electric Lightwave; Arne (Skip) Haynes, representing the Rainier Group (including Mashell Telecom and Rainier Cable); Theresa Jensen and Lisa Anderl, representing U S WEST Communications; Barb Young, representing Sprint/United; Rick Vitzthum, representing Kalama and Tenino Telephone Companies; Rick Finnigan, representing the Washington Independent Telephone Association; Joe Fabor, representing TCG; Tony Meinhardt, representing the Independent Business Association; Bob Munoz, representing WorldCom; and Simon ffitch, representing Public Counsel.

I. BACKGROUND INFORMATION - PRIOR TO DISCUSSION OF COMMENTS:

Access charge reform has been on the “to-do” list of every interest and industry segment in telecommunications for many years. Broad consensus exists that access charges pose a problem and should be reformed. This consensus about the existence of a problem, however, is not accompanied by agreement as to solution.

This section describes access charges, identifies problems created by the existing access charge structure of, and describes the operation of the rule.

A. What Are Access Charges?

Access charges are payments that long distance companies (“interexchange carriers” or “IXCs”) make to local exchange companies (“LECs”). IXCs pay LECs for access to the local exchange network. IXCs pay LECs at both the originating and terminating end of each long distance call.

Access to a local company's network is a monopoly service. The alternative would be for each company to build its own separate network connecting each of its customers. That is fundamentally at odds with the concept of a public switched network, in which every customer can call every other customer, even if they buy service from different phone companies.

The access service that IXCs buy from LECs is the same service that LECs buy from each other when they share a common local calling area. For local service it is called "interconnection" or "call termination." Regardless of where a call is coming from or going to, however, the service is the same.

A significant portion of the total cost of operating the local telephone network is recovered in access charges. Access charges paid by IXCs (and ultimately their customers) account for almost 20% of total retail revenues in this state, or about $18 per customer per month. It is important to remember that individual customers pay significantly more or less, and individual companies receive significantly different proportions of their total revenues from access charges.

Access charges are paid by IXCs, rather than by end use customers. While it is clear that IXCs must pass these through to their consumers in their long distance rates, the fact that they are paid in the first instance by IXCs affects the discussion of access charge reform.

B. Whose Interests Are at Stake in Access Charge Reform?

1. Customers - Customers pay both local and long distance rates. An overall decrease in access charges could put pressure on the potential need for an increase to local rates. A revenue neutral restructure within the area of access charges -- in which reductions in access charges are offset by other increases -- will not impact the overall body of customers directly, depending on when and how long distance providers pass through potential savings and local exchange companies seek alternative revenue. Depending on resulting rate structures, the effect on individual customers may vary depending on the customers' relative use of long distance services.

2. Incumbent LECs - Companies such as U S WEST Communications, GTE Northwest, PTI Communications (now CenturyTel) today provide local service to nearly all business and residential customers. Their rates are regulated by the Commission and must be fair, just, reasonable, and sufficient. A decrease in access charges will result in either a decrease in their overall profits (which must remain "sufficient") or an offsetting increase in other rates, or some combination of the two. All LECs are not alike in their reliance on access charges; small rural companies tend to get a higher proportion of their revenues from access charges than do larger companies serving

more densely populated areas. The larger LECs also provide toll service, and as payers of access charges they have some common interests with IXCs.

3. Facilities-based CLECs ("competitive LECS" or "CLECs") - Companies such as Electric Lightwave, TCG, MFS, Nextlink, and MCImetro provide local service in Seattle and Spokane. Their rates are filed with, but generally not regulated by the Commission. These companies generally pay and are paid for local access or "interconnection" with other LECs in the same local area. In some cases, CLECs gained entry into the telecommunications business by enabling customers with high long distance usage to bypass the access charges of incumbent LECs. Reducing access charges could make CLECs less attractive to customers, because the gains from bypassing access charges are reduced.

4. Reseller CLECs - Some CLECs plan to resell incumbent LEC services, perhaps combining local telephone service with other services. Resellers buy service from the incumbent at a discount off the prices paid by retail customers. All the access charges paid by an IXC serving a resale customer go to the incumbent LEC; the resale discount does not apply to access charges (access charges are considered a wholesale service, with toll being the retail service).

5. IXCs ("interexchange carriers" or "IXCs") - Companies such as AT&T, MCI, Sprint, and WorldCom provide long distance service and buy access service from LECs. Their intrastate rates are filed with, but generally not regulated by the Commission. Most IXCs are also CLECs or plan to become CLECs. Any decrease in access charges will accrue in the first instance to the IXCs. The extent to which IXCs will pass those decreases through to retail customers depends on the effectiveness of competition among IXCs and the way in which the charges are reformed.

6. Federal Communications Commission ("FCC") - The FCC regulates interstate telephone rates, including access charges collected by LECs for calls between states. Current (old) Washington intrastate access charges are modeled on the FCC's interstate access charges.

C. What Problems Does the Current Structure Cause?

From the perspective of incumbent LECs, the economic problem is that access charges are priced so high above economic cost that they present a very attractive bypass target. Bypass is not new. Larger customers today routinely buy "special access" on a flat monthly basis, instead of the per-minute rates paid by smaller customers. The potential for bypass increases greatly with the requirement that incumbent LECs offer unbundled network elements to CLECs.

High access charges also create an artificial distinction between “local” and “toll” service that is not based on differences in cost. Toll calls originally were priced higher because they cost more; that difference has largely dissolved. Access charges were created when the toll and local parts of the business were separated, and the purpose was to have toll calls contribute to the cost of the local network. Today a “local” call simply is a call that -- with regulatory permission -- is not required to pay access charges, and a “toll” call is one that does pay access charges.

Another problem with access charges is that they create misleading price signals. Almost all the costs of providing service are incurred whether or not a customer makes any long distance calls. Customers limit long distance calling because of the price, but in economic terms this is false economy. Recovering the same costs in the monthly flat rate would resolve this “problem” because customers are less sensitive to price in deciding whether to subscribe to basic local service.

Access charge structure also raises concerns about fair competition. In addition to providing local service, some LECs provide some long distance services. Regulators must guard against LECs setting their long distance prices too low, because LECs do not pay access charges to themselves. Were access priced at cost, this “imputation” of access charges in LEC toll prices (and the role of regulators in keeping prices high) would be unnecessary.

The new rule, as adopted in this order, is the result of a careful consideration of the problems and issues explained above. The new rule balances the interests of every type of company and customer to arrive at a new rate design in which customer choice begins to take the place of monopoly regulation. Monopoly regulation safeguards are retained (for example, rate-base rate-of-return regulation), while transitioning to a more competitive, market-based system.

The rule allows for a revenue-neutral implementation that will maintain the status quo for universal service support while identifying cost-based terminating charges in parity with local interconnection service. This will provide the launching pad for companies to offer customers more options and choices between and among services and providers. The mechanism will be flexible enough to facilitate transition to a cost-based and more competitively neutral form of universal service funding while universal service issues begin to become resolved later this year through Docket No. UT-980311(a), potential Legislative action early in 1999, and ongoing national efforts regarding this issue.

II. SUMMARY OF WRITTEN AND ORAL COMMENTS AND COMMISSION RESPONSE:

The comments can be categorized under the following general topics: A. “Universal Service,” B. “Competition,” C. “Revenue,” D. “Cost,” E. “Rate Design,” F. “Legal

Authority," and G. "Other Proposals." The related issues brought up by each commenter have been grouped together and are discussed in more detail under each general topic as outlined below. The Commission addresses each issue and explains how the new rule is consistent with the public interest (including economic theory, law, and public policy).

A. Universal Service

1. Universal Service and Access Charge Reform Linkage

Almost every ILEC commented on the necessity to link any changes in access charges to the express implementation of a new universal service fund, advocating full replacement of any and all lost access revenues as a result of this rule. The IBA also joined in this position to some extent.

The IXC's, Public Counsel/AARP, and to some extent other more competitive oriented parties argue the opposite. As Public Counsel/AARP states at page 2 of its June 8, 1998, comments, "A fundamental corollary of these principles is that universal service funding is not a "make whole" for access reform."

There is some logic and reason to both arguments, and the Commission adopts the staff-proposed "clarification" amendments to address both concerns to some extent. However, as the cost of universal service is revealed and explicitly recovered through the terminating rate additive or a future competitively neutral fund, the remaining base terminating access charge rate will be expected to be in parity with local interconnection and/or TSLRIC[1] cost as outlined in subsection (1) of the rule. We emphasize that a cost-based system is superior to revenue replacement without justification. One cannot make the assumption that all rates are currently based on "cost." If that were true, there would be no need for explicit recovery of implicit "subsidies" or for support. We address the "subsidy" and "cost" issues in more detail below under **Section D. Cost**.

To move forward with the rule at this time, and to mitigate adverse effects, we adopt the Staff-proposed implementation guidelines for revenue-neutral filings on an interim basis as policies to guide implementation of the rule until universal service costs are determined. After that it will be expected that any contribution above cost not allowed by the rule will be recovered first from originating access charges. If a company chooses to raise any other rates, such as local exchange service, it should be prepared to justify that increase with all of the necessary and normal rate case and cost support justification. The Commission makes it very clear that the rule allows a revenue neutral increase without

[1] TSLRIC stands for "total service long run incremental costs."

otherwise-applicable reviews only when the increase is applied to originating access charges. All other increases will be subject to applicable earnings reviews.

2. Impact on Rural Companies and Customers

Most of the ILECs and the IBA commented that the rule could cause adverse impacts on rural companies and local customers. Public Counsel/AARP stated concerns about unwarranted local rate increases for all customers, including rural customers. ILECs argued that the rule would cause them to lose terminating revenues and that they might not be able to recover the lost revenues through originating access charges because of the effects of competition.

The rule does not remove any of the normal protections that rate-base, rate-of-return-regulated rural telephone companies enjoy. The rule as clarified extends a revenue neutral opportunity for all companies including rural companies to recover lost revenues caused by reductions in terminating access charges. In addition, many rural companies already receive and will continue to receive explicit universal service funding to help keep local rates affordable for rural customers. It is important that the companies use these funds for their intended purpose.

If any company is not being fully compensated for its services under the pertinent standards, it may file a general rate case with the Commission at any time. In addition, if any company is providing service to high cost customers and is not being compensated sufficiently it has the opportunity to reveal the cost and what it believes is the necessary subsidy in Docket No. UT-980311(a) in which all ILECs in the State of Washington are already participating.

The Washington State Legislature and the Federal Congress have both mandated the development of a competitive and open telecommunications market with a diversity of providers and of services. Both also require that universal service be preserved at affordable rates. This is not an either/or proposition. The law is clear. We must do both. This rule will enhance competition and protect universal service, in the interim, as universal service issues are ultimately resolved. We can not delay one for the other.

Considering the protections in the rule, the protections of rate-base rate-of-return regulation, and the protections that will result from universal service inquiries, neither rural companies nor rural customers are under any unreasonable risk. Competition will benefit consumers in the long run, and companies successful at satisfying customers' demands will also reap rewards in the years to come.

3. Neutral and Non-discriminatory Funding of Universal Service

Both ILECs and IXCs argued that the rule would not be competitively neutral nor non-discriminatory as to universal service collection and distribution.

The companies' fears are not well grounded. First, supporting universal service implicitly through access charges and other "above cost" prices is less competitively neutral and non-discriminatory than the result of this rule. The rule makes progress toward a more competitively neutral, non-discriminatory, and cost-based system. Terminating access is just the first element, the most obvious anti-competitive rate design. We explain the "subsidy" issue in greater detail below under **Section D. Cost**.

The rule prescribes an equitable standard for pricing terminating access charges that does not put any company at an undue advantage or disadvantage. It also allows for companies to provide services to customers at the most efficient and cost-based levels possible. However, it is also flexible enough to accommodate markups sufficient for companies to earn a profit, and therefore allows flexibility in originating access and other prices. Although the rule prescribes a method for pricing the bottleneck of terminating access, it relies on the market and each company's discretion to price more competitive services - which will allow customers to be the ultimate regulator - rather than the Commission prescribing every price in every situation. Examples of how this pricing flexibility will work are explained in **Section E. Rate Design**.

By pricing terminating access in parity with local interconnection we are also taking a step toward undoing the practice of extracting all explicit universal service support from toll providers and ultimately long distance customers. This parity will provide the basis, under current Commission authority, for spreading the universal service support burden more broadly and among more telecommunications companies than presently exists.

This rule may not be a perfect solution, but it moves forward on a pro-competitive, fair, and equitable solution to the problems expressed by the parties commenting on this issue, and it does fit within our current statutory authority. If the Legislature approves a more competitively neutral and broader-based funding mechanism (or grants the authority to the Commission to do so), we will be in a better position to recommend what needs to be done and how much it will cost. However, if the Legislature chooses to be more cautious, we believe the system established in the rule is a good one.

4. Dialing Parity (Rural Customers as Less Economically Attractive Customers)

The rural ILECs brought up an issue during the adoption hearing. To the extent the rule causes originating access rates to rise in rural areas, these companies assert that toll providers will find rural customers less attractive to serve and may not market or volunteer to participate in a 2-pick system for equal access to interexchange

carriers, that is, dialing parity for both interLATA and intraLATA toll calling. Dialing parity was mandated by the federal Telecommunications Act of 1996 and FCC orders implementing it. The ILECs argue that their access rates will likely exceed the current market toll rates, and therefore toll service will become unprofitable in rural areas for toll providers.

There are adequate protections to ensure that rural customers continue to receive toll service. In fact, it is likely that toll services in several rural areas have in the past been operated at unprofitable levels, yet customers have had service. RCW 80.36.183 continues to authorize the Commission to retain jurisdiction over statewide average toll rates. The Telecommunications Act of 1996 at 47 U.S.C. Section 254(g) requires interexchange carriers to charge no higher rates in rural and high-cost areas than in urban areas within a state, and between states. The FCC's orders implementing this section also reinforce these toll averaging principles (see, FCC 96-424, released October 31, 1996). RCW 80.36.190 provides similar protections. Finally, the Obligation to Serve under RCW 80.36.090 "Service to be furnished on demand," applies to all registered telecommunications companies including interexchange carriers.

B. Competition

1. "Innovative New Products and Services"

Many of the ILECs and Rainier Cable argue that the rule will not result in the offering of innovative new products and services. They argue that nothing in the record would lead one to believe that anything good will result from the rule. MCI, on the other hand, and to some extent other parties, foresee many opportunities as a result of the new rule.

Commission Staff's November 6, 1997, memo regarding GTE-NW's Optional Local Calling Plans (OLCP) is one example of what may occur as a result of this rule. It will make it easier and more affordable to implement such plans - and other companies may wish to follow this model or create other options for consumers as a result of this rule. As Sprint/United notes in its comments, "It is true that the current level of access rates can make it difficult to pass imputation for such plans." In addition new technologies such as internet telephony and personal communications services (PCS) use the local interconnection services of the ILECS.

The parity proposed in this rule would remove one of the primary disadvantages previously placed on IXCs offering toll services, and one of the primary challenges impacting ILECs offering broader local calling areas. Especially in the local calling area example the new rule will enable ILECs to purchase local interconnection termination-type services "off the shelf" of other ILECs rather than spending months and years in negotiations and/or arbitrations and litigation.

There is more than ample information in this rulemaking file and in observations of the marketplace that this rule will enable innovative new services and products. We cannot mandate innovation but we can allow it to occur, and the rule encourages it by permitting companies to offer larger local (toll-free) calling areas without the high cost of terminating access.

2. Artificial Distortions

GTE-NW, Mashell Telecom, Rainier Cable, Sprint/United, U S WEST and WITA argued that the rule would provide perverse incentives and artificial distortions in the marketplace. They argue that implicit universal service and an unlevel playing field will put them at a disadvantage in a competitive market. They argue that prescriptive regulation has no basis in a competitive market (and in the next instance recommend mandatory flat rated primary interexchange carrier charges, or PICCs). They argue that the Commission should allow terminating access the same (upward) pricing flexibility and/or above-cost treatment that less-monopolistic services are afforded under the rule.

The Department of Defense and all Federal Executive Agencies, on the other hand, argue that the rule will actually remove artificial distortions that have been embedded in the current system and will remove perverse incentives and allow customers more choices and better services, at potential savings due to better price signals that will be more cost-based than ever before. DOD/FEA also recommend that the rule be used as "a model for the nation" due to the statewide, progressive, and proactive restructuring that will occur as a result of the rule.

The rule will remove artificial distortions in the market and provide incentives that will further the goal of promoting fair and efficient competition.

3. Competitive Neutrality

The ILECs and the IBA argue that the rule will not create a level, competitive playing field and will disadvantage ILECs.

MCI, on the other hand, argues that the rule will perpetuate the current system of placing all of the burden of supporting the ILECs' rural and high-cost areas on the IXCs. AT&T and MCI, respectively, argue that revenue replacement without cost justification is equivalent to institutionalizing, "an unwarranted and discriminatory tax for Washington's ratepayers," and "inequitable subsidy passthroughs." Public Counsel is in accord.

The rule prescribes an equitable basis for pricing terminating access charges. No matter who the local exchange company may be, the result will be the same --

the rule requires parity with local interconnection. All companies will have an opportunity to benefit from the availability of this policy. No company is unfairly prejudiced by this rule.

4. Small/Large Company Distinctions Within the Rule

Sprint/United and WITA would redefine a small company to be any Rural Company as defined in the Telecommunications Act, which would include every ILEC in Washington except USWC and GTE-NW.

Whidbey Telephone Company requested that when defining a small company within the rule that the Commission consider using a definition such as 20,000 or fewer access lines, or by using the provision in RCW 80.04.530 that allows reduced reporting requirements for companies serving less than 2 percent of the state's access lines, or approximately 50,000 lines.

The definition in RCW 19.85.020, based on 50 or fewer employees, best reflects the Legislature's intent with regard to the mitigations provided for the benefit of small businesses. To increase the threshold to include several larger companies, as the proposals by Sprint/United, Whidbey, and WITA would do, would have the effect of diluting the benefits of the mitigations to the very companies that need them the most. For these reasons we retain the definition outlined in the Regulatory Fairness Act in RCW 19.85.020. To the extent that any company is unique or needs an exception to this aspect of the rule it will have the opportunity to petition for waiver as provided under WAC 480-120-011. We also note that we did make changes from the noticed rule to mitigate its effect and reduce regulatory burdens on all companies, where feasible.

C. Revenue

1. Originating Bypass (Lost Revenue)

Every ILEC argued that "mandating" originating access charge rate increases would price them out of the market and cause reduced revenues due to competition from other companies or tariff shopping within each company's own service offerings (see also **E. Rate Design** under the heading, "4. Interstate Tariff Arbitrage", below). The ILECs argued that shifting "implicit subsidies" from the less competitive service of terminating access to the more competitive service of originating access would place a large percentage of their revenues "at risk."

DOD/FEA responded that greater competition and more customer choice is exactly what is needed for consumers to see any benefits.

The Commission adopts Commissioner Gillis' comment on this subject. He clearly explained during the adoption hearing, that "we are either going to have competition or we are not," -- we can't have it both ways.

The rule and the implementation process accepted as mitigation allow companies to continue to collect current terminating access charges on an interim basis. Today's implicit support and "subsidies" then will be replaced by tomorrow's explicit recognition of "cost" and any necessary support or subsidy which is clearly justified through the universal service proceeding. Companies may then shift charges to increases to originating access charges to the extent they wish to avoid an earnings review.

The opportunity to increase originating access charges without an earnings review is not a mandate, but an opportunity to exercise choice. To the extent any company wishes or perceives the need to raise any other rates (especially those that are currently below "cost") it always retains the right and opportunity to file for a general rate case. The Commission can not provide an unfettered opportunity for other rate increases due to its responsibility to prohibit non-competitive services from subsidizing competitive services (see RCW 80.36.300 and 47 U.S.C. 254(g)), and its responsibility to assure that rates are fair, just, reasonable, sufficient, and in the public interest.

The shift to originating access charges without a critical review is supported because the same class of customers, namely IXC's, pay access charges (both originating and terminating), and IXC's will continue to pay access charges. This adjustment to the rate design within access charges will be revenue neutral in the aggregate and will allow both the local and toll markets to become more competitive. Competition does not always result in a loss of revenue. Revenues will be a function of satisfying customer demand rather than monopolizing a bottleneck service.

2. Earnings Review

Public Counsel/AARP recommended at the adoption hearing that the Commission give the companies a clear indication that requests to increase local rates, or other rates than originating access, would not be entertained without an earnings review.

The language within the rule at subsection (6) will protect commenters' interest in guarding against unwarranted local rate increases. By giving the companies the opportunity to raise originating access rates we have allowed revenue-neutral filings. The Commission will continue in its responsibility to ensure that rates are fair, just, reasonable, sufficient, and in the public interest as this rule and other changes in the industry occur. Earnings reviews will continue to be one of the tools at the Commission's disposal in deciding whether to allow regulated companies to increase rates.

D. Cost

1. Implicit "Subsidy"

Most ILECs commented either in writing and/or orally at the adoption hearing that all implicit "subsidies," from switched access charges at least, must be identified and replaced with explicit support.

AT&T references previous comments in which it argues that, "For U S WEST and GTE, no high cost support should be provided if the statewide average earnings show that support is not needed to advance universal service objectives," and, "At least for the foreseeable future, and until GTE and U S WEST meet their obligations (e.g. 47 U.S.C. Sections 251 and 252) as required by the Act and local markets are irreversibly open to robust and widespread competition, U S WEST and GTE will not be able to demonstrate any need for high cost support."

We expect that the necessary level of explicit universal service support will be determined as a result of Docket No. UT-980311(a). We expect that the arguments surrounding the definition and levels of implicit "subsidies" may be answered at that point. The extent that any of the difference between the cost of terminating access and its current price includes any implicit "subsidy" (or support) towards the preservation of affordable universal service is not at issue here.

Until companies have had the opportunity in Docket Nol UT-980311(a) to show that they are serving high-cost areas requiring universal service support, it is reasonable consistent with the Staff-suggested mitigation approach to allow companies to bifurcate the existing terminating access rates into two elements: (a) a cost-based or interconnection-based terminating rate, and (b) a residual temporary universal service increment. This allows the companies to hold their total terminating access rates at current levels pending the resolution of universal service issues.

Based on the decision and determinations made in UT-980311(a) the subsidy necessary to maintain universal service for each company involved should be known. Then, the interim (residual) temporary universal service increment will be eliminated and replaced with a Commission-authorized increment (consistent with subsection (3) of the rule). The Commission authorized increment may be *more than* or *less than* the temporary interim residual increment allowed prior to the Commission's decision regarding the cost of universal service.

Finally, at either stage companies may merely shift responsibility for reduced terminating access revenues to originating access charges, under section (6) of the rule.

The rule will take effect 60 days after it is published in the Washington State Register. This provides companies with 30 days to prepare and file compliance tariffs and provides the Commission with 30 days to review those tariffs. This timing and implementation recognizes the linkage between access charges and universal service while continuing to make progress on both issues. We have found the "Terminating

Access Charge" rule to be in the public interest and we will deal with implicit subsidies, if any, through the adjudication in the universal service proceeding that is currently underway.

2. Loop Cost (Direct vs. Shared)

GTE-NW argues that the fixed cost of the loop should be attributed to the service that "causes" the cost to be incurred. It argues that the loop is a direct cost of local service and should not be "arbitrarily allocated" to anything else (such as access charges). It also argues that if the Commission continues to view the loop cost as a shared cost, the issues of access charge reform and removal of implicit subsidies becomes a very diluted issue.

Sprint/United, U S WEST, and WITA mention and/or concur in GTE-NW's analysis to various extent. All of these parties recognize loop cost recovery as an important piece of the challenges involving access charge reform and universal service.

Public Counsel/AARP and TRACER, on the other hand, make convincing arguments that the loop has been and will continue to be a shared cost. As Public Counsel/AARP state, "The telecommunications network should be treated as an integrated, multi product enterprise delivering a wide range of services. All services should be required to pay for all facilities that they utilize. Recovery of a share of joint and common costs is not a subsidy. The loop is a shared cost."

The Commission again reaffirms its finding from Docket No. UT-950200, on page 85 of the Fifteenth Supplemental Order (April 11, 1996), that loop costs are shared and should be matched with all of the revenues derived from the use of the loop. As the Fifteenth Supplemental Order states:

> "Based on the decision in U-85-23, one should not expect local service to be expected to cover 100% of loop costs, because some loop costs had been assigned to other services. The issue here is much broader and should not be controlled by the assignment provided for in U-85-23."

The same analysis is true for all telecommunications companies that this rule will apply to. In the order quoted above we began a shift away from a one-size-fits-all approach to one more flexible that takes each company's circumstances and the necessary public policy into consideration when determining rate design (as we are in this rulemaking) and rate levels (as we would with any rate proposal). The prescription made in this rulemaking regarding terminating access charges allows us to be more flexible on the originating side where competition has an opportunity to develop. The more customer choice and competition between and among services and providers, the more flexibility we

will be able to ensure and the less oversight we may exercise without slighting our statutory responsibilities to protect the public interest.

3. "Below-Cost" Terminating

Mashell Telecom argued that the Commission's rule would price terminating access charges for some companies "below-cost." Mr. Haynes explained this during the adoption hearing by stating, "If it (the loop) is a common cost to originating then it's a common cost to terminating." He asserted that not assigning shared cost to terminating access would result in a price for that service which would be "below-cost."

U S WEST Communications argued that the Commission's rule may allow competitive companies to file below-cost terminating rates because of the ability to concur in another company's tariff (and forego performance of a cost study) as anticipated by subsection (5) of the rule.

The Commission believes that the concerns of both Mashell and U S WEST are misplaced. First, terminating access charges will not be "below-cost" because local interconnection services will not be "below-cost." Second, "below-cost" should be defined as anything below the price floor of Total Service Long Run Incremental Cost (TSLRIC). The rule prices terminating access charges above cost (e.g. above the price floor of TSLRIC). Subsection (2) goes on to state the allowable treatment of shared costs. The rule does not prescribe any amount of shared costs to be "allocated" to originating access, but the rule does allow for a company to propose recovery of shared (loop) costs through originating access. Even subsection (6) does not require recovery of shared (loop) costs through originating access - it merely allows companies to do so if they wish to remain revenue neutral. We believe this policy will allow prudent recovery of costs while allowing companies to price closer to cost (the price floor) in order to respond to competition by lowering prices to consumers.

U S WEST's argument is without merit because terminating access charges will be based on local interconnection services which are currently undergoing a generic cost and pricing proceeding in Docket No. UT-960369, et al. Once costs and prices are determined in that proceeding the issue of cost will have been thoroughly flushed out. Additionally, as U S WEST has argued in this proceeding and in others, the CLECs tend to compete in the low-cost urban and densely populated business areas. The Commission finds that CLECs' costs are probably lower than the ILECs they are likely to concur in. However if U S WEST believes its competitors are pricing any service "below-cost" it continues to have the right to file a complaint with this Commission, and CLECs may do the same with ILECs. The rule is reasonable, is consistent with current economic theory and public policy, and will promote competition by pricing a vital bottleneck element closer to cost.

4. Small Business Economic Impact Statement (SBEIS) - Issues

Kalama/Tenino, Mashell, and WITA all complained that the Small Business Economic Impact Statement's (SBEIS) representations are inaccurate and that the proposed mitigations are inadequate.

The Commission finds that the May 11, 1998, final version of the SBEIS (including appendices) accurately and adequately reflects and addresses small business circumstances and concerns. Commission Staff estimates vary from company suggestions, but Commission Staff suggestions are credible and reflect experience with companies' actual costs and opportunities in this industry. Every ILEC including the small companies have the opportunity in the universal service Docket No. UT-980311(a) to identify the cost of universal service in high-cost and rural areas.

To the extent these companies feel that "implicit subsidies" may be transferred from terminating to originating access, these companies have the right and the opportunity in that docket to file cost justification, benchmark support, and recommend the level of explicit support required in order to ensure that prices in rural and high-cost areas are reasonably comparable to those in urban areas. This universal service cost justification opportunity is also a means of mitigation available to small telecommunications companies who feel that implicit support for high-cost areas will put them at a disadvantage in a competitive environment. These companies may make their case with respect to alleged "lost revenues" and the high-cost nature of providing service in their areas, and the Commission will decide based on the merits in Docket No. UT-980311(a) what level of funding is appropriate from universal service subsidies vs. the other revenues realized from the panoply of services offered by each company.

5. Small Company Concurrence in Another Small Company Tariff

Whidbey Telephone Company argued at the adoption hearing that a small company identified in subsection (5) should be able to concur in the terminating access rate of another small company for greater representatives of the underlying costs among these companies.

The Commission agrees with Whidbey on this issue and has revised the rule in subsection (5) to address this concern.

E. Rate Design

1. Originating Access Charges Need Not Be Equal to Terminating Access Charges

GTE-NW and USWC (with the concurrence of other ILECs) argue generally that a “minute is a minute” and that terminating access should be priced at the same level as originating access, because it provides essentially the same functions. The companies argue that originating and terminating access should be priced at the same level; and that if both are reduced, the lost revenues should be recovered through the universal service fund as replacement of an implicit subsidy. Sprint/United and other ILECs advocate, that some of the lost revenues should be recovered through universal service funding and some through the mandated implementation of a uniform flat rated primary interexchange carrier charge (or PICC, pronounced “pixie”).

AT&T and MCI argue a similar point but urge that both originating and terminating access be priced at cost (or the price floor), with little regard or concern for any revenue loss that local companies might incur.

WorldCom recommends allowing a difference between originating and terminating access charges (now allowed under the rule in subsection (2)), and monitoring whether or not originating access charges fall as a result of competition and market-based pricing, as it would like to see happen. If originating access charge reductions are not experienced, WorldCom would recommend that the Commission take prescriptive action when necessary.

The rule is simple and straightforward about this issue. The rule prescribes a rate design for terminating access charges. The rule allows originating access charges to be the same as terminating access charges, if companies choose to price that way. The rule also allows companies to price originating access charges to recover additional contribution and to price those charges higher than cost in order to allow companies to manage their revenue streams and compete where necessary. The Commission agrees with WorldCom that competition may, or may not, reduce originating access charges.

The Commission, however, does not see a need to prescribe reductions to originating access charges. It is sufficient that we prescribe only the rate design for terminating access and allow competition and customer choices (i.e., “the Market”) to determine the sustainability of originating access charges. As circumstances warrant, companies will reevaluate their own rate structures and price levels, which is to be expected in a more competitive environment. We remain open to dealing with individual company responses and proposals on a case-by-case basis given the underlying circumstances of each. Terminating access is the only change that we must mandate in order to allow competition to move forward at this time.

2. Pricing Flexibility (vs. Prescription)

We have discussed at some length the comments of the parties and the response of the Commission regarding this issue (see sections **C. Revenue** and **D. Cost**

for that discussion). We adopt Commissioner Hemstad's comment during the adoption hearing, expressing the desire to be open to whatever pricing flexibility is appropriate in the newly emerging competitive market. Glenn Blackmon, Ph.D., Assistant Director of Telecommunications authored a short paper outlining options that he distributed at the time of the adoption hearing, which is included in the rulemaking file and which we have considered in making our decision.

In addition, the Commission refers the parties to prior Commission orders relating to this issue, especially Docket No. UT-950200 15th Supplemental Order, and Docket No. UT-941464, et al., 4th Supplemental Order.

3. Local Rate Increase Risk

The ILECs cautioned the Commission on the potential risk of proposals to increase local residential rates, especially in rural areas where competition (or customer choice) may not exist.

The IBA echoed the ILECs concerns with an interest in protecting small businesses from local rate increases that may be proposed as an unintended consequence of this rule.

Public Counsel/AARP also cautioned the Commission that rate rebalancing (i.e. proposing to lower competitive services' rates but to increase bottleneck services' rates, such as raising local rates in order to lower originating access charges) is, "not an imaginary threat ... LECs have consistently argued that access reform must be accomplished through rate rebalancing."

The Commission understands the parties' positions and the concerns stated about this rule by the incumbent companies, who fear the potential loss to competition of the benefits they now draw from their monopoly or near-monopoly status. We protect incumbent local companies by allowing an initial two-part terminating rate filing; we protect incumbent local companies by allowing the uncritical acceptance of revenue neutral filings, and we protect incumbent local companies by continuing to provide rate base-rate of return regulation in which their rates may continue to be set in a way to afford them the opportunity to earn an appropriate return.

This rule, in conjunction with other Commission activities such as universal service reform and implementation of local competition, will help to keep all rates lower than they otherwise would be without this rule. As Commissioner Gillis remarked during the adoption hearing, ".... what we're trying to do is to create a competitive environment where there is a fair playing field that companies will compete and produce lower prices, better service quality, and innovation."

4. Interstate Tariff Arbitrage

Sprint/United, U S WEST, and WITA (including other concurring ILECs) argue that to the extent lowering terminating access charges causes intrastate originating access charges to rise, IXC customers may falsify information in order to purchase the same services out of each ILEC's interstate tariff where the same service may be less expensive. This is generally the bypass argument that is described above under section **C. Revenue**, within a company's own jurisdictional tariffs. Rather than losing a customer and associated revenue to a competitor, the ILECs argue here that they may lose revenue if the customer purchases its interstate services at a lower price.

To the extent customers shop for a better deal it is in their interest to do so. Regulated companies will need to become more competitive. In this instance, however, falsifying information is not shopping. We do not have jurisdiction or control over the ILECs interstate tariffs. The FCC has jurisdiction, but the ILECs themselves do have the ability to propose changes to them. To the extent that ILECs need to adjust rate designs other than intrastate terminating access charges, they may do so. The Commission has only offered a revenue neutral opportunity to increase or restructure intrastate originating access charges. If an ILEC needs to lower other intrastate prices or increase interstate prices to better reflect cost recovery and market conditions the Commission recommends that ILECs make those proposals to the respective jurisdictions with such reasonable justification as each circumstance warrants.

F. Legal Authority and Process

U S WEST raised several points that it presented as legal impediments to the Commission taking the actions contemplated by the adoption of the rule through rulemaking, rather than by using adjudicative processes. First, U S WEST asserts that the proposed rule violates procedural due process rights of U S WEST and others, and is in excess of the Commission's authority to adopt rules because the proposed rule as published in the CR-102 does not authorize all companies subject to the rule to propose a revenue neutral filing.

The rule adopted (as amended at subsection (6) prior to its adoption) does allow all companies subject to the rule to propose a revenue neutral filing, thus these concerns are avoided. This change addresses the legal concerns expressed by U S WEST at pages 2-4, 9-10, and page 11 of its June 12, 1998, comments.

U S WEST also noted in its comments that the Commission has traditionally set rates for a company only after a notice and opportunity for a hearing, and entry of an order setting rates. U S WEST asserts that the Commission, by adoption of this rule, is setting rates for companies without using this traditional process. The company refers to the process the Commission used when it adopted rules setting the maximum charges for

Alternative Operator Service companies to charge customers, noting that the Commission did not take the position that the operation of the rule superseded the effective tariffs on file. WITA notes a similar concern, referring to the process the Commission used in the proceedings under Docket No. U-85-23, et al., and also notes that the Commission cannot compel a tariff filing through adoption of a rule.

The Commission is not setting explicit rates for any individual company by adoption of this rule, nor determining the cost support and sufficiency of the information presented by any company in support of a tariff or rate filing. By adoption of this rule, the Commission is prescribing a rate design that will require most, if not all, companies, to file revisions to their approved tariffs in order to have tariffs on file that comply with the rule. The Commission sees no difference in the process being used here and that used in the AOS rule situation: If companies do not voluntarily file revised tariffs that comply with these rules, the Commission will need to institute complaints against the non-complying tariffs. Because the rule allows for revenue-neutral filing by all companies, no rate reduction is mandated by the rule, and there is no loss of revenues as a result of the rule, versus the potential (speculated) impact of market forces.

Simply because the Commission in the past has used a different process such as a generic proceeding with many companies participating in an adjudicative setting does not bind the Commission to use the same process in every case. The rulemaking process is designed to be open to all persons, not simply companies that may have a particularized interest in the subject of the rulemaking or the funds to support participation in an adjudicative process. The rulemaking process allows broader participation than does an adjudicative setting. Case law in this state at the least encourages that agencies proceed by rulemaking, rather than application of a policy to a particular regulated party, when the policies the agency is implementing apply generally to members of the regulated industry. RCW 34.05.010(16), which defines a "rule," also suggests that the rulemaking process is preferable to an adjudicative proceeding when many parties are potentially affected.

We note that, consistent with the Commission's position, U S WEST states that the Commission may establish prospective rate designs by rule. In this rulemaking proceeding, the Commission is not establishing rate levels, but is directing a form of rate design, with direction about the types of costs that may be included in which rates. However the rule does not, for example, mandate that a particular company's rate for terminating access charges be set at any specific rate level expressed in dollars or cents. Under our rule, each company may reasonably justify its own unique rate within the stated parameters.

G. Other Proposals

1. Sprint Proposal

Sprint proposed that the Commission reduce access charges to interstate levels and replace lost revenues with increases from a state universal service fund and a flat rated PICC assessed on originating IXC's.

The rule we adopt is consistent in principle with Sprint's proposal. Sprint would have the Commission mandate a PICC for all ILECs. Sprint would have the Commission decide the level of universal service funding in this docket rather than in the universal service docket. Subsections (2) and (6) of the adopted rule allow flexibility for each ILEC to propose a PICC or other charge on originating access. The rule permits a flexible approach that will allow ILECs the opportunity to respond to market conditions on the originating side. The only mandated access charge rate design is on terminating access because it is the least susceptible to competition and customer choice. The Commission will deal with the cost of universal service and the associated level of necessary funding in the universal service Docket No. UT-980311. Therefore, the Commission rejects Sprint's proposal.

2. WITA Proposal

WITA's proposal is similar to the Sprint/United proposal discussed above, and is rejected for the same reasons.

3. U S WEST Proposal (Subsection (3) Universal Service)

U S WEST would have the Commission rewrite the rule to address U S WEST's legal authority issues.

The Commission rejects this proposal for the reasons explained in section **F. Legal Authority**, and for all of the economic and public policy reason stated throughout this order. U S WEST's proposal would undermine the Commission's investigation of the cost of universal service in UT-980311(a) by mandating a permanent revenue replacement mechanism that would be in direct opposition to the Legislature's directive and the national movement as reflected in actions of Congress, FCC, NARUC, Joint Boards, etc., toward basing universal service funding on the cost of providing basic service in high-cost areas.

H. SUMMARY OF REASONS FOR CHANGES TO NOTICED LANGUAGE:

Subsection (1) includes the clarifying amendment that "comparable local interconnection service" applies in each exchange in order to allow companies who compete to charge terminating access in parity with the applicable local interconnection agreement in each exchange, which may vary dependent upon which incumbent is interconnected with). This amendment was offered and advocated by TCG and ELI. We adopt it for the reasons advocated in its support.

Subsection (2) contains the previous definition of “cost” from subsection (1) of the noticed language, and clarifies that the cost of the local loop may be recovered through originating access but not terminating access. This amendment was necessary to clarify the rule’s intention, as pointed out in the written comments of Public Counsel, TRACER, and GTE-NW. The reasons are also described throughout the text of this order.

Subsection (3) remains unchanged except for adding the word “any” to the phrase, “recover any costs for support of universal . . . .” This clarification illustrates the Commission’s intention that not all universal support be recovered from interexchange carriers and their customers. The amendment will allow the costs for support of universal service to be allocated among all intrastate use, both toll and local, if necessary. This change is consistent with our decision that terminating access service should be in parity with local interconnection service. This amendment follows the written comments of AT&T and MCI, and is explained in greater detail above. The change allows the greatest degree of competitive neutrality that we can provide, given our current authority.[2]

This revision meets the intent of the original rule to create a placeholder for a comprehensive universal service funding program, which will be addressed in the Commission’s universal service study directed by the legislature and possible future legislation. The rule, with this amendment, enables us to move forward with procompetitive actions that are necessary to remove barriers to entry and to reduce anticompetitive and discriminatory rate structures.

Subsection (5) was amended expressly to exempt competitively classified carriers from the requirement of filing cost studies (consistent with reducing expensive regulatory burdens on effectively competitive companies). This section is relevant to competitive local companies only if all their local traffic is exchanged on a “bill and keep” basis; companies with explicit local interconnection rates would still be required to structure terminating access service at the interconnection levels. This amendment is consistent with the intention of the original rule and reduces regulatory burdens where effective competition exists. TCG and ELI commented in writing and orally, respectively in support of such a change.

Subsection (5) has also been amended to allow small businesses the opportunity to concur in the approved terminating rate of another small business. This revision will reduce regulatory burdens on small businesses and may be more representative than the original rule would have been. The Commission adopted this amendment to address concerns that Whidbey Telephone Company stated at the adoption hearing. This issue is also discussed in more detail above.

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[2] Although this allows the Commission to move forward, we remain mindful of the Legislature’s review and any potential legislative action that might occur in the next session.

Subsection (6) extends the revenue-neutral mitigation opportunity to all local exchange companies. This substantially reduces the regulatory burden of the rule on all companies. Any company will be permitted to implement the rule without reducing its revenues, as long as it meets the requirements of the rule (that is, it does not seek to shift terminating access revenues to any service other than originating access). The Commission will not require companies to meet an "earnings test" to shift revenues in this manner. The Commission adopted this amendment to address written comments, and also to clarify and confirm the Commission's intentions regarding the rule. The provision meets both the concerns of incumbent local exchange companies that their revenues could be impaired by the rule, and the concerns of Public Counsel and TRACER for protection against unwarranted local rate increase requests.

This amendment is a means to mitigate concerns of incumbent telecommunications companies. We wish to implement with as little disruption as possible the policies adopted through this rulemaking -- promoting competition, protecting captive customers against bottleneck economic power, allowing greater pricing flexibility to those that seek it where warranted, and eliminating discrimination and anticompetitive rate structures as promptly as possible. This revision is consistent with the original rule and facilitates the reduction of regulatory burdens where effective competition has an opportunity to develop. It also provides greater predictability for customers and guidance for telecommunications companies.

We agree with Public Counsel and TRACER, and believe that this revision meets the intent of the original rule and reduces regulatory burdens where effective competition has an opportunity to develop - it also provides greater predictability for customers and guidance for the companies.

III. IMPLEMENTATION

The Commission heard Commission Staff's comments regarding implementation of the rule during a time in which information continues to be gathered that may bear on the ultimate rates structure that may result. The Commission adopts the Commission Staff recommendation, presented at the time of adoption, as set out in this section as the Commission's policy statement regarding the implementation of the rule.

The rule provides for explicit recovery of universal service costs that have been determined by the Commission, but such costs have not yet been determined for some companies. The Commission is investigating the costs of universal service in Docket UT-980311(a). Some companies may wish to wait for the results of that investigation, which is scheduled to conclude late this year, before making any major shift in its terminating and originating access revenues. Commission Staff would support, and

the Commission would accept, an interim compliance filing that leaves existing terminating revenues in place if it:

(a) includes a cost-based terminating rate consistent with subsection (1) of the rule,

(b) includes an interim universal service rate that recovers the residual amount of terminating revenues,

(c) commits the company to revise the interim universal service rate to reflect the Commission's decision in Docket UT-980311(a) within 30 days after the final order in that docket, and

(d) is otherwise consistent with the requirements of this rule and in the public interest.

IV. ADOPTION OF THE TERMINATING ACCESS CHARGE RULE:

COMMISSION ACTION: After considering all of the information regarding this proposal, the Commission adopted the proposed rule with the changes described and discussed in the text of this order. The adopted rule is set out in Appendix A of this order.

STATEMENT OF ACTION; STATEMENT OF EFFECTIVE DATE: In reviewing the entire record, the Commission determines that WAC 480-120-540 should be adopted to read as set forth in Appendix A, as rule of the Washington Utilities and Transportation Commission, to take effect on the sixty-first day after the distribution date of the issue of the Washington State Register in which it appears.

This effective date is at least six weeks longer than the normal effective date of rules adopted pursuant to RCW 34.05.380(2), to allow companies time to prepare the necessary tariff filings needed in order to comply fully with the rule. Taking effect sixty days after publication of the rule will allow the companies ample time to prepare their filings and file them thirty days prior to the effective date of the rule. This timing will allow the companies' tariffs to become effective coincident with the effective date of the new rule.

Other phases of implementation are clear from the rule or other provisions of this order.

O R D E R

THE COMMISSION ORDERS That:

1. WAC 480-120-540, as set forth in Appendix A, is adopted as a rule of the Washington Utilities and Transportation Commission, to take effect on the sixty-first day after the distribution date of the issue of the Washington State Register in which it appears.

2. This order and the rule set out below, after being recorded in the register of the Washington Utilities and Transportation Commission, shall be forwarded to the Code Reviser for filing pursuant to chapters 80.01 and 34.05 RCW and chapter 1-21 WAC.

3. The Commission adopts Commission Staff memoranda, presented when the Commission considered filing a preproposal statement of inquiry, when it considered filing the formal notice of proposed rulemaking, and when it considered adoption of this proposal, in conjunction with the text of this order, as its Concise Explanatory Statement of the reasons for adoption, as required by RCW 34.05.025.

DATED at Olympia, Washington, this 23rd day of September 1998.

WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

ANNE LEVINSON, Chair

RICHARD HEMSTAD, Commissioner

WILLIAM R. GILLIS, Commissioner

Note: The following is added at Code Reviser request for statistical purposes:

Number of Sections Adopted in Order to Comply with Federal Statute: New 0, amended 0, repealed 0; Federal Rules or Standards: New 0, amended 0, repealed 0; or Recently Enacted State Statutes: New 0, amended 0, repealed 0.

Number of Sections Adopted at Request of a Nongovernmental Entity: New 0, amended 0, repealed 0.

Number of Sections Adopted on the Agency's own Initiative: New 1, amended 0, repealed 0.

Number of Sections Adopted in Order to Clarify, Streamline, or Reform Agency Procedures: New 0, amended 0, repealed 0.

Number of Sections Adopted using Negotiated Rule Making: New 0, amended 0, repealed 0; Pilot Rule Making: New 0, amended 0, repealed 0; or Other Alternative Rule Making: New 0, amended 0, repealed 0.

NEW SECTION

WAC 480-120-540 Terminating access charges. (1) Except for any universal service rate allowed pursuant to subsection (3) of this section, the rates charged by a local exchange company for terminating access shall not exceed the lowest rate charged by the local exchange company for the comparable local interconnection service (in each exchange), such as end office switching or tandem switching. If a local exchange company does not provide local interconnection service (or does so under a bill and keep arrangement), the rates charged for terminating access shall not exceed the cost of the terminating access service being provided.

(2) The cost of the terminating access shall be determined based on the total service long-run incremental cost of terminating access service plus a reasonable contribution to common or overhead costs. Local loop costs are considered "shared" or "joint" costs and shall not be included in the cost of terminating access. However, nothing in this rule prohibits recovery of local loop costs through originating access charges (including switched, special, and dedicated as defined in subsection (4)(a) of this section).

(3) If a local exchange company is authorized by the commission to recover any costs for support of universal access to basic telecommunications service through access charges, it shall recover such costs as an additional, explicit universal service rate element applied to terminating access service.

(4) Definitions.

(a) "Access charge" means a rate charged by a local exchange carrier to an interexchange carrier for the origination, transport, or termination of a call to or from a customer of the local exchange carrier. Such origination, transport, and termination may be accomplished either through switched access service or through special or dedicated access service.

(b) "Terminating access service" includes transport only to the extent that the transport service is bundled to the end office or tandem switching service. Dedicated transport unbundled from switching services is not subject to subsection (1) of this section.

(c) "Bill and keep" (also known as "mutual traffic exchange" or "payment in kind") is a compensation mechanism where traffic is exchanged among companies on a reciprocal basis. Each

company terminates the traffic originating from other companies in exchange for the right to terminate its traffic on that company's network.

(5) The requirement of subsection (1) of this section that any terminating rate be based on cost shall not apply to any local exchange company that is a small business, or to any local exchange company that is competitively classified, if it concurs in the terminating rate of any local exchange company that has filed a terminating rate that complies with the requirements of subsection (1) of this section. For the purposes of this subsection, "small business" has the same meaning as it does in RCW 19.85.020.

(6) Any local exchange company that is required to lower its terminating access rates to comply with this rule may file tariffs or price lists (as appropriate) to increase or restructure its originating access charges. The commission will approve the revision as long as it is consistent with this rule, in the public interest and the net effect is not an increase in revenues.

[]