BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

REC'D TN REGULATORY AUTH.

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OFFICE OF THE EXECUTIVE SECRETARY

IN RE: PETITION TO CONVENE A CONTESTED CASE PROCEEDING TO ESTABLISH "PERMANENT PRICES' FOR INTERCONNECTIONS AND UNBUNDLED NETWORK ELEMENTS	)))	Docket No. 97-01262

CONSUMER ADVOCATE DIVISION'S RESPONSE IN OPPOSITION TO BELLSOUTH'S PETITION FOR RECONSIDERATION AND CLARIFICATION

Comes the Consumer Advocate Division of the Office of the Attorney General for the State of Tennessee and hereby responds in opposition to BellSouth Telecommunications, Inc.'s Petition for Reconsideration and Clarification. The Consumer Advocate Division urges the Tennessee Regulatory Authority ("TRA") to deny BellSouth's Petition for Reconsideration and Clarification.

The Consumer Advocate Division did not file direct proof on most the issues raised by BellSouth in its Petition for Reconsideration. The Consumer Advocate Division, however, did file proof on the issue of "Depreciation " raised by BellSouth. The Consumer Advocate Division, therefore, wishes to address that issue in this response.

Not surprisingly, BellSouth asks the Authority to adopt depreciation lives determined by BellSouth rather than the lives determined by the FCC and the Tennessee Public Service Commission (which were the lives chosen by the Authority in this proceeding). BellSouth Petition at 3. The Consumer Advocate Division would point out, however, that the lives put forward by BellSouth represent input only from BellSouth. Furthermore, that input from

BellSouth comes at a time when BellSouth knows that it is to its advantage to use shorter lives than had previously been used.

The lives determined by the FCC and the Tennessee Public Service commission, on the other hand, represent input from disinterested parties who were trying to determine the actual lives of assets. There was no advantage to either the FCC or the Public Service Commission to shade the numbers one way or another. Accordingly, the TRA should reject BellSouth's request that the TRA change its decision to use depreciation lives determined by the FCC and the Tennessee Public Service Commission.

ARGUMENT

Following is a summary of Bellsouth's arguments on depreciation; the Consumer Advocate Division will respond to each of these arguments in turn:

1. BellSouth Position: The Authority's decision to adopt 1993 depreciation lives is totally inconsistent with the forward-looking methodology which the Authority purports to adopt.
2. BellSouth Position: Even the FCC has acknowledged the need to examine historical depreciation regulatory practices in today's environment.
3. BellSouth Position: The depreciation lives proposed by BellSouth are by far the most reasonable and appropriate proposal before the Authority.
   a. The proposed lives used in BellSouth's cost studies are based on BellSouth's 1995 and 1996 Depreciation Studies, which provide detailed explanation of methodology, data analysis that support the asset lives and other depreciation parameters presented in the studies.

b. Although the Authority did not "review" BellSouth's Depreciation Studies, (Interim Order at 13), the Authority does not and cannot dispute that these studies contain thousands of pages of data and analysis supporting BellSouth's appropriate lives.

4. BellSouth Position: That the depreciations lives proposed by BellSouth have not been "adopted by the Authority" is irrelevant. By virtue of the Authority's December 9, 1998 Order approving BellSouth's application for a price regulation plan, BellSouth has the legal prerogative to establish its own deprecation rates.

5. BellSouth Position: Although the Authority found that "Tennessee-specific depreciation lives, salvage values, and other inputs" should be used in calculating deprecation rates (Interim Order at 13), this finding ignores the unrefuted evidence in the record that depreciation lives generally do not vary from state to state.

6. BellSouth Position: The Authority's conclusion that the depreciation lives prescribed for BellSouth in 1993 "are too brief" ignores the FCC's preliminary conclusion that existing regulatory depreciation lives are in reality too long, at least for certain accounts.

1. "The Authority's decision to adopt 1993 depreciation lives is totally inconsistent with the forward-looking methodology which the Authority purports to adopt."

The use of the 1993 depreciation lives is not inconsistent with the forward-looking methodology adopted in this proceeding. The depreciation lives used in the network elements cost of service study should be "forward looking" but that does not mean that they should not reflect the expected lives of the assets actually used in the provision of service.

The lives from the 1993 three way depreciation agreement are, by definition, forward looking. In developing the projected lives for the 1993 deprecation settlement, the objective was to "look forward" and determine the expected time that a newly installed asset would remain in service. Proper depreciation rates are those that allow an enterprise to recover its cost of the assets while they are use. Thus, rates are to be designed to match the cost recovery period with the actual use of the asset. That was the objective of the Tennessee Regulatory Staff and the FCC Staff 1993: to "look forward" and determine the time an asset would be in service . As a result, they selected lives that are determined on a truly forward looking basis.

2. "Even the FCC has acknowledged the need to examine historical depreciation regulatory practices in today's environment."

BellSouth cites the FCC's October 14, 1998 order in CC Docket 98-137 in arguing that the Authority should reconsider its decision on depreciation lives in this proceeding. A copy of this Order is attached as Exhibit A. While the FCC has proposed to review its depreciation practices, it is not yet prepared to eliminate the process that it uses to set depreciation rates as implied by BellSouth in this proceeding. [1] In paragraph 7 the Commission states:

> 7. As soon as robust competition exists in the local exchange markets, we believe our depreciation process should be eliminated because it will be unnecessary. In a robustly competitive market, both the incumbent LECs and their competitors should charge prices that are at or near their costs, including depreciation, in order to attract customers and maximize their profits. **In such a**

[1] In this case BellSouth proposes to base its depreciation lives on depreciation studies that have not been reviewed by either the FCC or the Tennessee Regulatory Authority.

> **market, a carrier's ability to raise its depreciation rates would be constrained by its need to compete against other carriers, rather than by government regulatory constraints. Unfortunately, the local exchange market today is not such a market**. In this Notice, we seek comment on conditions under which carriers could set their own depreciation rates without compromising the Commission's oversight, even in the absence of full competition. In addition, we offer a number of proposals to streamline these depreciation rules by eliminating all unnecessary regulatory requirements. We therefore initiate this proceeding to modify those rules. In addition to our more specific requests for comment below, we invite commenters to submit information on the costs and benefits of the rules at issue in this proceeding and of our proposed modifications. (Emphasis added, footnotes deleted.)

In its order the FCC recognizes that it would be premature to allow incumbent LECs to select, without review, their own depreciation rates for use in studies such as this. In particular, the FCC noted that competition is not yet a sufficient constraint on LECs. In addition, it should be kept in mind that the charges for services subject to this proceeding are for services to be provided to Bell's future competitors.

It is also significant to note the FCC's position on the depreciation lives of digital switches as set forth in this order. The FCC did not propose to simply shorten the lives of the digital switches but instead proposed to <u>extend</u> the range from the present 16 to 18 years to a range of 13 to 18 years. As explained in the paragraph 11 of the order, the FCC proposal would permit a carrier that "can support a life estimate between 13 and 16 years to select a new life estimate without an out-of-range filing." As stated, the proposal does not relieve the carrier of supporting the life it uses but would simply eliminate the necessity to make an out-of-range filing:

> 11. We expect that the retirement rates for digital switching will continue to increase and therefore we propose to expand the range for digital switching equipment from a range of 16 to 18 years to a wider range of **13 to 18 years**. Our proposal will permit a carrier that can support life estimates between 13 and 16

years to select a new life estimate without an out-of-range filing.

Even if adopted, the FCC's proposal does not indicate that the 17 year life used by the Authority in the present case is incorrect. As shown above, the 17 year life is still within the proposed 13 to 18 year range. Thus, the FCC simply proposes to extend the lower limit of the range but does not indicate that any change is necessary or that the Authority erred.

3. "The depreciation lives proposed by BellSouth are by far the most reasonable and appropriate proposal before the Authority."

- **a. The proposed lives used in BellSouth's cost studies are based on BellSouth's 1995 and 1996 Depreciation Studies, which provide detailed explanation of methodology, data analysis that support the asset lives and other depreciation parameters presented in the studies.**
- **b. Although the Authority did not "review" BellSouth's Depreciation Studies, (Interim Order at 13), the Authority does not and cannot dispute that these studies contain thousands of pages of data and analysis supporting BellSouth's appropriate lives."**

Admittedly, BellSouth did file thousands of highly redundant pages, the majority containing information relative to the areas the company serves it other states. Saying the same thing nine times, on nine separate pages, about nine different service areas does add physical weight but does not increase the weight of the evidence.

Furthermore, the alleged depreciation studies proposed by BellSouth have not been submitted to the Authority or to the FCC for the normal review process. Instead, BellSouth submitted the proposed studies that do not calculate depreciation in accordance with what BellSouth considers "outdated guidelines imposed upon by the FCC[2]." Accordingly, the Authority was correct to reject the lives as proposed by BellSouth based on the proposed studies that have not been subject to analysis and scrutiny normally afforded such filings.

4. "That the depreciations lives proposed by BellSouth have not been "adopted by the Authority" is irrelevant. By virtue of the Authority's December 9, 1998 Order approving BellSouth's application for a price regulation plan, BellSouth has the legal prerogative to establish its own deprecation rates."

While the statute provides that a telephone company operating under price regulation in accordance with Tenn. Code Ann. § 65-5-209 is not required to obtain Authority approval to change depreciation rates, this proceeding was intended to determine the rates to be paid for unbundled network elements. Thus, BellSouth did not ask that its depreciation rates as they might apply to matters outside this proceeding be changed and the Authority did not so establish or so modify the company's depreciation rates.

In this proceeding, the Authority was faced with determining the appropriate lives and net salvage factor inputs used in the pricing models advocated for use in setting permanent prices. The models being proposed in this proceeding use an annuity calculation to allow Bell to recover the cost of hypothetical investments in new equipment over its useful life. For example, assume that the model assumes that a $1,000,000 switch is to be installed and that it will remain

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[2]BellSouth Telecommunications, Inc.'s Petition for Reconsideration and Clarification, page 5.

in service 17 years. The model will compute a rate that will allow the company to recover, in equal payment, the investment plus a return component on an asset over its life. Thus, the model does not call for a depreciation rate input. The model calls for projected life and net salvage. Thus, the Authority did not approve or adopt any actual depreciation rates in this proceeding.

The lives and net salvage factors adopted by the Authority were previously reviewed and approved by both the FCC and the Tennessee Public Service Commission. BellSouth's proposed lives and net salvage factors, however, have had not been subject to such a review. Accordingly, the TRA should reject BellSouth's proposed depreciation lives.

5. "Although the Authority found that "Tennessee-specific depreciation lives, salvage values, and other inputs" should be used in calculating deprecation rates, (Interim Order at 13), this finding ignores the unrefuted evidence in the record that depreciation lives generally do not vary from state to state."

While the depreciation lives, salvage, and other inputs used in calculating depreciation rates may not vary much from state to state, they do vary. The Authority is responsible for setting rates for services in Tennessee, not other states. As a result, the Authority is correct in its decision to adopt lives, salvage, and other inputs specific to Tennessee.

6. "The Authority's conclusion that the depreciation lives prescribed for BellSouth in 1993 "are too brief" ignores the FCC's preliminary conclusion that existing regulatory depreciation lives are in reality too long, at least for certain accounts."

This statement in BellSouth's petition indicates that the FCC had found major problems with it's prescribed depreciation lives. A review of the order indicates differently. In paragraph 11 of the October 14, 1998 Order in CC Docket 98-137 the Commission states:

> We have reviewed recent industry data and have concluded that, except for the digital switching equipment account, **we have no evidence indicating that the current ranges are either too long or too short.** (Emphasis added, footnotes deleted.)

The FCC's preliminary conclusion is not that existing regulatory depreciation lives are too long. The FCC has preliminarily concluded that there is no problem for most accounts.

CONCLUSION

For the foregoing reasons, the Authority should deny BellSouth's Petition for reconsideration and Clarification.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Vance L. Broemel, hereby certify that I have served a copy of the foregoing Response in Opposition, either by hand-delivery, by FAX, or by U. S. Mail, on this 19 day of February 1999 to the following

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

In the Matter of	)	
	)	
1998 Biennial Regulatory Review --	)	CC Docket No. 98-137
Review of Depreciation Requirements	)	
for Incumbent Local Exchange Carriers	)	

NOTICE OF PROPOSED RULEMAKING

Adopted: July 22, 1998 Released: October 14, 1998

Comment Date: November 23, 1998
Reply Comment Date: December 8, 1998

By the Commission: Commissioner Furchtgott-Roth issuing a statement.

I. INTRODUCTION

1. The Communications Act, as amended, ("the Act"),[1] seeks to develop efficient competition by opening all telecommunications markets through a pro-competitive, deregulatory national policy framework. To that end, Section 11 of the Act requires the Commission, in every even-numbered year beginning in 1998, to review its regulations applicable to providers of telecommunications service to determine whether the regulations are no longer necessary in the public interest as a result of meaningful economic competition between providers of such service and whether such regulations should be repealed or modified.[2]

2. Our depreciation prescription process,[3] as a central feature of traditional common carrier policy, is a prime candidate for this biennial regulatory review.[4] When the Commission

1 47 U.S.C. § 161.

2 *Id.*

3 *See* 47 C.F.R. § 43.43.

4 We note that SBC Communications, Inc. ("SBC") recently has proposed that the Commission, as part of its biennial review, decline to continue to prescribe depreciation rates and lives for price cap carriers. *See* Petition for Section 11 Biennial Review, filed by SBC Communications, Inc. et. al., May 8, 1998 at 9-10 ("SBC Petition"); see also Letter, dated March 13, 1998, from Robin Gleason, Director - Regulatory Finance, Ameritech, to Kenneth P. Moran, FCC (suggesting elimination of Commission prescription of depreciation rates for price cap carriers);

used cost-of-service or rate-of-return regulation, it required incumbent local exchange carriers ("LECs") to set prices based on costs, including depreciation expenses.[5] Historically, each carrier seeking to change its depreciation rates has submitted a depreciation rate study that was reviewed by both the Commission staff and the representatives of the state public utility commission for the jurisdiction covered by the study. This depreciation prescription process required carriers to submit extensive data for each plant category to support the projection life, survivor curve, and future net salvage estimates underlying their proposed depreciation rates. These data requirements often necessitated voluminous submissions, with up to 25 pages of analysis for each of 34 plant categories.

3. Over the years, the Commission has taken steps to streamline the depreciation process. In 1980, the Commission departed from its previous practice of relying largely on historical experience to project equipment lives and began increasingly relying on company plans, technological developments and other future-oriented analyses.[6] Because of the adoption of these and other reforms, incumbent LECs' reserve ratios[7] increased from a low of 18.6 percent of total plant in 1980 to 49 percent in 1997. In 1993, the Commission issued the *Depreciation Simplification Order*.[8] In that Order, the Commission adopted a simplified depreciation prescription process for AT&T.[9] With regard to the incumbent price cap LECs, that Order

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Letter, dated Feb. 19, 1998 from Porter E. Childers, Executive Director - Legal and Regulatory Affairs, United States Telephone Association, to Kenneth P. Moran, FCC, Attachment at 1 (suggesting replacement of detailed depreciation and amortization requirements with GAAP).

[5] The Commission has raised issues in another pending rulemaking that may affect the depreciation process and alter the manner in which the incumbent LECs recover their plant investment. Access Charge Reform, *Notice of Proposed Rulemaking, Third Report and Order, and Notice of Inquiry*, 11 FCC Rcd 21354, 21464-66 (1996).

[6] We note that, since the Commission's Depreciation Reform Proceeding in 1980, the life and salvage factors prescribed by the Commission are forward-looking factors that are based primarily on analysis of incumbent LEC investment plans and on judgments regarding the technological obsolescence and economic viability of the assets, rather than a focus on the historical equipment life trends. See Amendment of Part 31 (Uniform System of Accounts for Class A and Class B Telephone Companies), *Report and Order*, 83 FCC 2d 267 (1980). *See also* Report on Telephone Industry Depreciation, Tax and Capital/Expense Policy at p. 8 (April 15, 1987). ("We determined that by paying closer attention to company plans, technological developments, and other future-oriented analyses, more realistic forecasts could be made, and we have since adopted those recommendations.")

[7] A carrier's reserve ratio is its accumulated depreciation divided by its gross plant investment.

[8] Simplification of the Depreciation Prescription Process, *Report and Order*, 8 FCC Rcd 8025 (1993) ("*Depreciation Simplification Order*").

[9] *Id.* at 8063. AT&T was allowed to select its own life and salvage factors, without being limited by any Commission specified ranges. It was required to file data to support its proposed life and salvage factors but the reporting requirements were reduced to 5 pages per account, from the previously required 25 pages per account.

provided for the establishment of ranges for the underlying life and salvage factors that those carriers could use to compute their depreciation rates. In the *Second Depreciation Simplification Order*, the Commission provided incumbent price cap LECs increased flexibility to set depreciation rates by identifying life and salvage factor ranges for 22 plant categories.[10] In the *Third Depreciation Simplification Order*, the Commission adopted values for the ranges for eight additional plant categories and simplified procedures for the remaining categories.[11] Incumbent price cap LECs that proposed life and salvage factors within the Commission-approved ranges no longer need to file detailed support for those rates. A carrier could, of course, propose a rate outside the range but it would have to provide cost support to justify it. As a result of these changes, the Commission reduced the typical carrier's filing requirements by 75 percent when its depreciation proposals are within the prescribed ranges.[12]

4. In this Notice of Proposed Rulemaking ("Notice"), we propose to reduce or streamline further our depreciation prescription process by permitting summary filings and eliminating the prescription of depreciation rates for incumbent LECs, provided that the carrier uses depreciation factors that are within the ranges adopted by the Commission, expanding the prescribed range for the digital switching plant account, and eliminating salvage from the depreciation process. We also seek comment on whether we should permit carriers to set their own depreciation rates if they are willing to waive the automatic low-end adjustment. These proposed modifications are designed to minimize the reporting burden on carriers and to provide incumbent LECs with a greater flexibility to adjust their depreciation rates while allowing the Commission to maintain adequate oversight.[13]

See also Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier, *Order*, 11 FCC Rcd 3271 (1995). Section 43.43 of the Commission's rules, 47 C.F.R. § 43.43, only requires "dominant" carriers to comply with our depreciation prescription process. AT&T has not been subject to the depreciation prescription process since it was declared non-dominant in October of 1995.

[10] Simplification of the Depreciation Prescription Process, *Second Report and Order*, 9 FCC Rcd 3206, 3208 (1994) ("*Second Depreciation Simplification Order*").

[11] Simplification of the Depreciation Prescription Process, *Third Report and Order*, 10 FCC Rcd 8442, 8444 (1995) ("*Third Depreciation Simplification Order*").

[12] The 1993 rule changes to the depreciation prescription process has reduced the filing requirements from 660 pages to approximately 170 pages. Under the current rules, a carrier that is proposing projection life or salvage factors within the range need only file an average of five pages per plant category, rather than the up to 25 pages per plant category that were required before the rules were simplified in 1993.

[13] *See* 47 U.S.C. § 220.

II. BACKGROUND

5. Depreciation is the loss in service value of an asset due to the factors which cause retirement of the asset.[14] Depreciation is the largest single operating expense that incumbent LECs incur, amounting to nearly $20 billion annually.[15] Under our current rules, the Commission prescribes depreciation rates for dominant incumbent LECs[16] with annual operating revenues of $112 million or more.[17] These carriers are subject to Section 220 of the Act[18] and must compute their depreciation rates by a formula[19] that uses the carrier's accumulated depreciation balance[20] and forecasts of two parameters: future net salvage ("FNS")[21] and average remaining life ("ARL")[22] for each plant account.

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[14] *See* National Association of Regulatory Commissioners, Public Utility Depreciation Practices at 13 (1996) ("*NARUC Depreciation Manual*").

[15] ARMIS USOA Report 43-02, Table B-2, Row 110.

[16] *See* 47 C.F.R. § 43.43. *See also* Amendment of Sections 43.42 and 43.43 of the Commission's Rules and Regulations to Increase the Revenue Threshold for Filing Pension and Depreciation Reports, *Report and Order*, 3 FCC Rcd 6908 (1988).

[17] The revenue threshold was adjusted by an index for inflation and was set at $112 million for 1996. *See* Implementation of the Telecommunications Act of 1996: Reform of Filing Requirements and Carrier Classifications, *Order and Notice of Proposed Rulemaking*, 11 FCC Rcd 11716, 11745-47 (1996) ("*Interim Indexing Order*"); Public Notice, Annual Adjustment of Revenue Threshold, DA 98-795 (rel. Apr. 24, 1998).

[18] 47 U.S.C. § 220.

[19] *See* Simplification of the Depreciation Prescription Process, *Notice of Proposed Rulemaking*, 8 FCC Rcd 146, 147 (1992) ("*Depreciation Simplification NPRM*"). Depreciation is calculated using the formula:

$$\text{Depreciation Rate} = \frac{100\% - \text{accumulated depreciation }\% - \text{future net salvage }\%}{\text{average remaining life}}$$

[20] Accumulated depreciation is the amount of plant investment that has been depreciated. In theory, upon retirement of plant, the accumulated depreciation will be equal to the cost of the plant less any net salvage. The accumulated depreciation component in the formula allows the rate to correct for any over or under depreciation accruals resulting from errors in prior life and salvage estimates. *See Id.* at 147 at n. 3.

[21] The FNS is the estimated gross salvage of the plant less any estimated cost of removal. Gross salvage is the amount a carrier receives from disposing of retired plant. Cost of removal is the cost the carrier incurs in retiring plant through the removal and disposition of the plant. *Id.* at 147.

[22] The ARL is the average of the future life expectancies of all items in a particular plant account. The ARL is determined by two basic factors: a projection life and a survivor curve. The projection life is the average life expectancy

6. Although price caps regulation largely eliminated the direct link between costs and prices, a carrier's depreciation remains significant, even under current price cap rules, in the following situations: (1) a calculation of a low-end adjustment;[23] (2) a recalculation of the productivity factor;[24] (3) an exogenous cost determination;[25] (4) a calculation of the Base Factor Portion that is used to determine how much a carrier can recover through End User Common Line charges;[26] or (5) the cost support a carrier would have to provide if it proposed an Actual Price Index ("API") higher than its Price Cap Index ("PCI").[27] In addition to these price cap effects, changes in depreciation expense may also affect prices or federal support payments through new mechanisms created to implement the Telecommunications Act of 1996.[28] For example, the Commission required incumbent LECs to use depreciation factors within the FCC authorized ranges when calculating forward-looking economic costs for universal service high cost loop support purposes.[29] Also, state commissions have required incumbent LECs to use interstate depreciation rates or life and salvage factors developed during the Commission's depreciation prescription process when calculating rates for interconnection[30] or unbundled

of new additions to plant; the survivor curve is the expected retirement pattern of plant. *Id.*

23 Price Cap Performance Review for Local Exchange Carriers, *First Report and Order*, 10 FCC Rcd 8961, 9036-37 (1995). Under price cap regulation, incumbent LECs that report annual interstate earnings below 10.25 percent may adjust their PCIs upward, targeted to earn 10.25 percent -- the lower formula adjustment mark. *See also LEC Price Cap Order*, 5 FCC Rcd at 6806-07 and 47 C.F.R. § 61.45(d)(1)(vii).

24 Price Cap Performance Review of Local Exchange Carriers, *Fourth Report and Order in CC Docket 94-1 and Second Report in CC Docket No. 96-262*, 12 FCC Rcd 16642, 16670 (1997) ("*Fourth Price Cap Review*").

25 Policy and Rules Concerning Rates for Dominant Carriers, *Second Report and Order*, 5 FCC Rcd 6786, 6809 (1990) ("*LEC Price Cap Order*").

26 In general, carriers project the Base Factor Portion revenue requirement using either historical cost trends or cost models based on projected budget data. *See* 1997 Annual Access Tariff Filings, *Order Designating Issues for Investigation, Memorandum Opinion and Order on Reconsideration*, 12 FCC Rcd 11417, 11429-30 and Appendix B (1997).

27 *See* Section 61.49 (e) of the Commission's rules, 47 C.F.R. § 61.49 (e).

28 Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) ("1996 Act") amending the Act.

29 Federal-State Joint Board on Universal Service, *Report and Order*, CC Docket No. 96-45, 12 FCC Rcd 8776, at ¶ 250 (rel. May 8, 1997) ("*Universal Service Order*"), as corrected by Federal-State Joint Board on Universal Service, *Errata*, 12 FCC Rcd 8776 (rel. June 4, 1997), appeal pending in Texas Office of Public Utility Counsel v. FCC and USA, No. 97-60421 (5th Cir. 1997).

30 *See* Application of Bell Atlantic-Delaware, Inc. for Approval of its Statement of Terms and Conditions Under Section 252(f) of the Telecommunications Act of 1996, Findings and Recommendations of the Hearing Examiners, PSC Docket No. 96-324 at p. 40 (Apr. 7, 1997) ("The FCC prescribed lives are forward-looking and appropriate to use in

network elements.[31] Finally, depreciation may play a role in a takings claim under the Fifth Amendment.[32]

III. DISCUSSION

7. As soon as robust competition exists in the local exchange markets, we believe our depreciation process should be eliminated because it will be unnecessary. In a robustly competitive market, both the incumbent LECs and their competitors should charge prices that are at or near their costs, including depreciation, in order to attract customers and maximize their profits. In such a market, a carrier's ability to raise its depreciation rates would be constrained by its need to compete against other carriers, rather than by government regulatory constraints. Unfortunately, the local exchange market today is not such a market.[33] In this Notice, we seek comment on conditions under which carriers could set their own depreciation rates without compromising the Commission's oversight, even in the absence of full competition. In addition, we offer a number of proposals to streamline these depreciation rules by eliminating all unnecessary regulatory requirements. We therefore initiate this proceeding to modify those rules. In addition to our more specific requests for comment below, we invite commenters to submit information on the costs and benefits of the rules at issue in this proceeding and of our proposed modifications.

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a TELRIC model."), adopted in Interlocutory Order No. 4488 (Apr. 29, 1997); Public Utility Commission of Texas, FTA96 § 252 Arbitration Panel, PUC Docket Nos. 16189, 16196, 16226, 16285 and 16290, Arbitration Award at p. 33 (November 7, 1996) (requires Southwestern to use the average service lives and salvage factors prescribed by the FCC); Order Approving Interconnection Agreement (Dec. 19, 1996); Texas State Statutes, Article 1446(c)(o).

31 *See* Consolidated Petitions of New England Telephone and Telegraph Company d/b/a NYNEX, Teleport Communications Group, Inc., Brooks Fiber Communications, AT&T Communications of New England, Inc., MCI Communications Company, and Sprint Communications Company, L.P., pursuant to Section 252(b) of the Telecommunications Act of 1996, for arbitration of interconnection agreements between NYNEX and the aforementioned companies, Commonwealth of Massachusetts, Department of Public Utilities, D.P.U. 96-73/74, 96/75, 96-80/81, 96-83, 96-94 - Phase 4, at p. 56 (December 4, 1996) ("We find, based on this record, that the projection lives prescribed by the FCC in its last represcription of NYNEX's depreciation rates are the kind of forward-looking projection lives required in a TELRIC study." The Massachusetts Commission directed that these lives be incorporated into NYNEX's compliance filing when calculating the rates for unbundled network elements using the NYNEX TELRIC model).

32 U.S. Const. amend. V.

33 Trends in Telephone Service, Table 8.1 (Industry Analysis Div. July 1998) In 1996, the incumbent LECs had 99 percent of the local exchange market, as measured by revenues. Even assuming that the competitive LECs have grown signigificantly, we expect that 1997 data will show the incumbent LECs' market share of not less than 97 percent.

8. BellSouth suggests that the Commission allow carriers to set their own depreciation rates on the condition that they not seek an automatic low-end adjustment.[34] This condition appears to address the low-end adjustment situation. We seek comment on BellSouth's proposal.[35] We also seek comment on what additional conditions could be imposed to eliminate our need for depreciation prescription in the other contexts upon which we rely on it.[36] If we can identify conditions that would eliminate the need for us to prescribe depreciation in the remaining situations we have identified, we propose to allow carriers to set their own depreciation rates.

9. In the event that we continue to set some depreciation rates for some carriers, we tentatively conclude that the depreciation prescription requirements for incumbent LECs subject to the depreciation prescription process should be further streamlined by doing the following: (1) reducing the supporting documentation required for carriers selecting depreciation factors from within the prescribed ranges; (2) eliminating depreciation prescription for carriers that select depreciation factors within the ranges; (3) expanding the range of lives for digital electronic switching equipment; and (4) eliminating net salvage from the depreciation prescription process.

10. **Filing and Prescription Procedures:** Under current procedures, carriers are required to file an average of five pages of information per account to support the selection of new depreciation factors for represcription of depreciation rates when those factors fall within the ranges prescribed by the Commission. Because there are 34 plant accounts, a typical filing would contain approximately 170 pages. The approval of the rates proposed in such filings has typically been pro forma as long as carriers selected depreciation factors from within the ranges. In this Notice, we propose to reduce filings to four summary exhibits[37] and the electronic data files used to generate them, provided carriers select depreciation factors from within the ranges and certify that their selections are consistent with their operations. We further propose that, if a carrier selects depreciation factors from within the ranges for all of its accounts, the Commission would permit the rates to go into effect without a prescription order. We believe that our proposal to eliminate Commission prescription of depreciation rates under these conditions will

[34] Presentation from Kathleen B. Levitz, BellSouth, to Ruth Milkman, FCC (Apr. 8, 1998).

[35] *Id.*

[36] *See* ¶ 6, *supra* (identifying a number of situations where depreciation remains significant, including calculation of a low-end adjustment.)

[37] The four summary exhibits are a comparison of existing and proposed depreciation rates; a comparison of existing and proposed annual depreciation expenses; a book and theoretical reserve summary; and the depreciation factors.

save time and resources for both the Commission and incumbent LECs. We seek comment on this proposal and on SBC's proposal that the Commission remove itself completely from the prescription of depreciation rates for price cap carriers.[38]

11. **Equipment Life Ranges:** When it adopted the life and salvage factor ranges, the Commission stated that it would review them periodically and revise them as necessary.[39] Accounting and other evidence strongly suggests the prescribed digital switching equipment lives should be lowered. Since the early 1990s, retirement rates for digital switching have nearly doubled and are now at approximately three percent.[40] This reflects an accelerating rate of replacement of major components of digital switches with newer, more powerful components. For example, incumbent LECs are replacing switch processors, line modules, and switch memory devices in order to enhance the call handling capability of switches and to provide improved and enhanced telecommunications services such as enhanced caller ID and enhanced CENTREX and to provide substantial improvements to network maintenance and administration. Incumbent LECs contend that "this increase in the retirement rate is not a temporary aberration, but the beginning of much higher rates."[41] We expect that the retirement rates for digital switching will continue to increase and therefore we propose to expand the range for digital switching equipment from a range of 16 to 18 years to a wider range of 13 to 18 years. Our proposal will permit a carrier that can support life estimates between 13 and 16 years to select a new life estimate without an out-of-range filing. We request comment on this proposal. We have reviewed recent industry data and have concluded that, except for the digital switching equipment account, we have no evidence indicating that the current ranges are either too long or too short.[42] We ask whether the ranges for any of the accounts other than digital switching require revision. Commenters proposing range changes should propose specific new ranges and should provide justifications for their proposals.

12. Pursuant to Sections 0.457 and 0.459 of the Commission's rules, carriers sometimes request confidential treatment for information provided about various types of

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38 SBC Petition at 9-10.

39 *Depreciation Simplification Order*, 8 FCC Rcd at 8058.

40 The retirement rates for the largest incumbent LECs have increased from 1.5 percent for 1990-92 to 2.9 percent for 1995-97. *See* ARMIS Report 43-02, Table B-1, Row 2212.

41 L. Vanston, R. Hodges and A. Poitras, Transforming the Local Exchange Network at 144 (2d ed. 1997).

42 For example, ARMIS data shows that retirement rates (i.e., annual retirements divided by average plant balances) for telephone plant are approximately the same level as they were ten years ago.

equipment, including digital switching.[43] In these requests, carriers have expressed concern that public disclosure of their detailed cost support would reveal proprietary information that could adversely affect their dealings with competitors and equipment vendors. We therefore request comment about whether the Commission's existing confidentiality procedures are adequate or whether additional safeguards need to be adopted to protect information that carriers regard as confidential.[44]

13. **Proposed Treatment for Salvage and Cost of Removal:** Salvage and cost of removal are two components that are currently considered in calculating depreciation rates. Salvage is the estimated scrap value or other proceeds a carrier will receive when it sells equipment retired from service, and cost of removal is the estimated cost a carrier will incur to dismantle and remove equipment retired from service. Because both salvage and cost of removal are estimates of future amounts related to the retirement of equipment, the two estimates are netted to a single amount (net salvage) in the calculation of depreciation rates. Although it is referred to as net salvage in our depreciation formula, cost of removal has traditionally exceeded salvage, which results in a negative net salvage amount. To illustrate net salvage, assume an asset costs $1,350, has an estimated life of 5 years, is expected to sell for $50 scrap value upon retirement, and is expected to cost $200 to remove from service. In this illustration the asset has a net salvage value of - $150, i.e., $50 salvage minus $200 cost of removal. Under these circumstances, a carrier would record depreciation expense of $1,500 over 5 years at $300 per year. The $1,500 charged to depreciation expense over the life of the equipment represents the original cost of $1,350 plus the $150 net cost to retire the equipment.

14. Estimating future gross salvage and cost of removal can be inordinately complex, time consuming, and speculative. To estimate what they will receive for equipment when it is retired and sold, carriers must project whether the equipment will be salable as useful equipment or as scrap many years in the future and what the price for commodities, such as copper,[45] may be. Also, estimating cost of removal requires carriers to project what portion of equipment will

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[43] 47 C.F.R. §§ 0.457 and 0.459.

[44] Section 0.457 of the Commission's rules, 47 C.F.R. § 0.457, establishes categories of information, including "trade secrets and commercial or financial information" which the Commission may, under specified circumstances, withhold from public disclosure. Section 0.459 of the Commission's rules, 47 C.F.R. § 0.459, specifies that carriers may identify, as proprietary, information for which they request confidentiality and file it under separate cover. If the Bureau Chief grants the request, it is not subject to public disclosure. If proprietary treatment is denied, information that was voluntarily submitted will normally be returned to the carrier and information that the carrier was required to submit will normally be subject to public disclosure. If the carrier's request for confidentiality is denied, it may appeal the denial to the Commission and subsequently to the court.

[45] The primary salvage value for the cable accounts, for example, is attributable to the copper conductors within the cables.

actually have to be removed, how many labor hours removal will typically take, and what the cost of that labor will be many years in the future. Consequently, the estimation of net salvage is a complex and inexact process that imposes substantial burdens on both the carriers and the state and federal commissions. The current process also requires the Commission to establish and review ranges for salvage and requires carriers to provide more extensive cost support if they propose salvage factors that are outside of the ranges prescribed by the Commission. Given the speculative nature of the estimates and the burdens associated with their calculation, we tentatively conclude that the prescription of net salvage no longer serves a regulatory purpose and that eliminating that factor from the depreciation prescription formula would significantly reduce the regulatory burden of the depreciation prescription process. Accordingly, we propose to eliminate the future net salvage factor from the depreciation formula and to record salvage and cost of removal as a current expense in the period incurred.[46] Alternatively, we could make the elimination of salvage from the depreciation formula optional, allowing each incumbent LEC the option to treat net salvage as either a current expense or a component of depreciation. We seek comment on these proposals.

15. In commenting on the proposed removal of net salvage from the depreciation process, commenters should address the effect this change could have on the current depreciation rates, whether new rates should be prescribed, whether the elimination of salvage would require adjustment of depreciation reserves, and what accounting changes would be necessary to effectuate the change.

16. We tentatively conclude that, if we remove net salvage from the depreciation process, we should create a new account, Account 6566, Net cost of removal, to record both salvage receipts and removal costs incurred. We also tentatively conclude that we should revise Sections 32.3100, Accumulated depreciation, and 32.2000, Instructions for telecommunications plant accounts, to eliminate the provisions that salvage and cost of removal be recorded in the depreciation reserve account. We request comment on the tentative conclusions. We also request comment on whether we should require carriers to keep subsidiary record categories in Account 6566 for salvage and cost of removal.

17. **Reporting Requirements for Mid-Sized LECs:** In separate proceedings on ARMIS and Accounting Biennial Review, we propose to create a category of mid-sized incumbent LECs that would be subject to a lighter regulatory burden than would be imposed on

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[46] In the example discussed in paragraph 12, the carrier would incur annual depreciation expenses of $270 per year for each year of the asset's five-year life. In addition, in the fifth year, the carrier would record the actual net salvage cost as a current expense. Assuming that the forecast was correct, the carrier would incur net salvage of $150 in the fifth year, in addition to the $270 in depreciation expense scheduled for that year. If, as frequently occurs, the forecast was erroneous and the carrier incurred net salvage expense of only $75, it would take that amount as a current expense.

large incumbent LECs.[47] Similarly, we propose in this proceeding, in addition to the streamlined processes proposed for all carriers, that mid-sized incumbent LECs not be required to file annual theoretical reserve studies.[48] Because we would continue to receive theoretical reserve studies from the largest incumbent LECs, which represent over 90 percent of the industry, this proposal would relieve these mid-sized companies of this regulatory burden without seriously encumbering our ability to monitor our depreciation prescription process.[49] To avoid unnecessary complexity, we tentatively conclude that we should apply the definition of mid-sized LEC that is adopted in the ARMIS proceeding[50] to our depreciation prescription requirements. We request comments on this proposal.

18. **Low-End Adjustment:** One of the reasons the Commission has retained some control over depreciation rates is because of carriers' ability to seek a low-end adjustment. Without such controls, carriers could manipulate depreciation expense to reduce their return and

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[47] *See* 1998 Biennial Regulatory Review -- Review of ARMIS Reporting Requirements, *Notice of Proposed Rulemaking*, CC Docket No. 98-117, FCC 98-152 (July 17, 1998) ("*ARMIS NPRM*"); 1998 Biennial Regulatory Review -- Review of Accounting and Cost Allocation Requirements, United States Telephone Association Petition for Rulemaking, *Notice of Proposed Rulemaking*, CC Docket No. 98-81, ASD File No. 98-64, FCC 98-108 (June 17, 1998) ("*Accounting Reform NPRM*").

[48] One means of determining the effectiveness of the Commission's depreciation prescription process and the level of any depreciation reserve deficiency is a comparison of a carrier's book depreciation reserve with its "theoretical" depreciation reserve. The carrier's book reserve is provided explicitly in its Part 32 accounts and is a matter of record. The theoretical reserve is computed and submitted to the Commission by July 1, each year. The Commission has relied on this type of analysis numerous times over the past twenty years as it has reformed the depreciation process by revising depreciation methodology and ordering carriers to amortize reserve imbalances. *See* Amortization of Depreciation Reserve Imbalances of Local Exchange Carriers, *Notice of Proposed Rulemaking*, 2 FCC Rcd 6473 (1987) ("*Amortization NPRM*"). The latest analysis completed indicates that as of January 1, 1997, the carriers' book depreciation reserve and the theoretical depreciation reserve is approximately the same. Therefore, there is no apparent depreciation reserve imbalance.

[49] Section 43.43 of the Commission's rules, 47 C.F.R. § 43.43, requires dominant "communications common carriers" with annual operating revenues exceed the indexed revenue threshold, currently $112 million, to file reports of proposed changes in depreciation. Companies with annual operating revenues below this amount are not currently subject to the depreciation process and continue to be exempt from any revised requirements.

[50] *ARMIS NPRM* at 7. In that proceeding, we propose to streamline the depreciation prescription process for certain mid-sized incumbent LECs based on the aggregate revenues of the incumbent LEC and any LEC that it controls, is controlled by, or is under common control with another LEC. If the aggregate revenues of these affiliated incumbent LECs are less than $7 billion, then each LEC within that group would be eligible to not file annual theoretical reserve studies. Incumbent LECs with individual annual operating revenues below the indexed revenue threshold would continue to be exempt from the Commission's depreciation prescription process.

obtain a price increase through the low-end adjustment.[51] We seek comment on whether we should permit carriers to set their own depreciation rates, as proposed by several incumbent LECs, or alternatively, whether such carriers should be permitted to do so only on the condition that they become ineligible for a low-end adjustment.

19. **Conclusion:** Prior to the 1996 Act, Section 220(b) of the Act required that the Commission prescribe depreciation rates for subject carriers.[52] The 1996 Act amended Section 220(b) such that prescription of depreciation rates is now within the Commission's discretion. Although we recognize that, for price cap carriers, depreciation generally no longer serves its original purpose of setting prices, it affects many other aspects of our regulation of the incumbent LECs.[53] We tentatively conclude that the elimination of depreciation regulation at this time would have an adverse impact in several critical areas, including the calculation of universal service high cost loop support, takings claims, and the low-end adjustment. We tentatively conclude that, if adopted, our proposal would eliminate all unnecessary depreciation prescription requirements and retain only those essential to the sound administration of the universal service high cost loop support and the achievement of the Commission's other regulatory goals. We seek comment on this tentative conclusion and solicit comment on SBC's alternative proposal that depreciation rates for price cap carriers should be based on "economic analysis consistent with the procedures called for by Generally Accepted Accounting Principles ("GAAP")."[54] We also seek comment on how we should determine when sufficient competition exists to allow us to eliminate the depreciation prescription process.

IV. PROCEDURAL ISSUES

A. *Ex Parte* Presentations

20. This is a permit but disclose rulemaking proceeding. *Ex parte* presentations are permitted, except during the Sunshine Agenda period, provided that they are disclosed as provided in the Commission's rules. See generally 47 C.F.R. §§ 1.1202, 1.1203, and 1.1206.

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[51] If a carrier's earnings were low enough so that it almost qualified for a low-end adjustment, it could, by shortening its lives and salvage factors, increase its annual depreciation expense. Because depreciation expense is one of the costs that is deducted from revenues to determine earnings, increased depreciation expense would result in reduced profits and could qualify the carrier for a low-end adjustment that it would not qualify for absent the change in depreciation.

[52] 47 U.S.C. § 220 (b).

[53] *See* ¶ 6, *supra*.

[54] SBC Petition at 9.

B. Regulatory Flexibility Analysis

21. The Regulatory Flexibility Act ("RFA")[55] requires that an initial regulatory flexibility analysis be prepared for notice-and-comment rulemaking proceedings, unless the agency certifies that "the rule will not, if promulgated, have a significant economic impact on a substantial number of small entities."[56] The RFA generally defines "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."[57] In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.[58] A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration ("SBA").[59]

22. This Notice proposes to eliminate the prescription of depreciation rates for incumbent LECs in most cases, expand the prescribed range for the digital switching plant account, and eliminate salvage from the depreciation process. This Notice also asks whether we should permit carriers to set their own depreciation rates if they are willing to waive their right to a low-end adjustment. The Notice proposes to further reduce the reporting requirements for certain mid-sized incumbent LECs by eliminating their obligation to file an annual theoretical reserve study. Neither the Commission nor SBA has developed a definition of "small entity" specifically applicable to LECs. The closest definition under SBA rules is that for establishments providing "Telephone Communications, Except Radiotelephone," which is Standard Industrial Classification ("SIC") code 4813. Under this definition, a small entity is one that, including affiliates of the entity, employs no more than 1,500 persons.[60]

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[55] The RFA, *see* 5 U.S.C. § 601 *et. seq.*, has been amended by the Contract With America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) ("CWAAA"). Title II of the CWAAA is the Small Business Regulatory Enforcement Fairness Act of 1996 ("SBREFA").

[56] 5 U.S.C. § 605(b).

[57] *Id.* § 601(6).

[58] *Id.* § 601(3) (incorporating by reference the definition of "small business concern" in Small Business Act, 15 U.S.C. § 632). Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register."

[59] Small Business Act, 15 U.S.C. § 632.

[60] 13 C.F.R. § 121.201, SIC code 4813.

23. We certify that the proposals in this Notice, if adopted, will not have a significant economic impact on a substantial number of small entities. Pursuant to long-standing rules, incumbent LECs with annual operating revenues exceeding the indexed revenue threshold must comply with the Commission's depreciation prescription process. This Notice proposes to reduce certain of these depreciation requirements. These changes should be easy and inexpensive for incumbent LECs to implement and will not require costly or burdensome procedures. We therefore expect that the potential impact of the proposal rules, if such are adopted, is beneficial and does not amount to a possible significant economic impact on affected entities. If commenters believe that the proposals discussed in the Notice require additional RFA analysis, they should include a discussion of these issues in their comments.

24. The Commission's Office of Public Affairs, Reference Operations Division, will send a copy of this Notice, including this initial certification, to the Chief Counsel for Advocacy of the Small Business Administration.[61] A copy will also be published in the Federal Register.

C. Paperwork Reduction Act

25. As part of our continuing effort to reduce paperwork burdens, we invite the general public to take this opportunity to comment on information collections contained in this Notice of Proposed Rulemaking, as required by the Paperwork Reduction Act of 1995, Pub. L. No. 104-13. Public and agency comments are due at the same time as other comments on this Notice of Proposed Rulemaking. Comments should address: (a) whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (b) the accuracy of the Commission's burden estimates; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

[61] 5 U.S.C. § 605(b).

D. Comment Filing Procedures

26. Pursuant to Sections 1.415 and 1.419 of the Commission's rules, 47 C.F.R. §§ 1.415, 1.419, interested parties may file comments on or before November 23, 1998, and reply comments on or before December 8, 1998. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies.[62]

27. Comments filed through the ECFS can be sent as an electronic file via the Internet to <http://www.fcc.gov/e-file/ecfs.html>. Generally, only one copy of an electronic submission must be filed. If multiple docket or rulemaking numbers appear in the caption of this proceeding, however, commenters must transmit one electronic copy of the comments to each docket or rulemaking number referenced in the caption. In completing the transmittal screen, commenters should include their full name, Postal Service mailing address, and the applicable docket or rulemaking number. Parties may also submit an electronic comment by 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.

28. Parties who choose to file by paper must file an original and four copies of each filing. If more than one docket or rulemaking number appear in the caption of this proceeding, commenters must submit two additional copies for each additional docket or rulemaking number. All filings must be sent to the Commission's Secretary, Magalie Roman Salas, Office of the Secretary, Federal Communications Commission, 1919 M St. N.W., Room 222, Washington, D.C. 20554.

29. Parties who choose to file by paper should also submit their comments on diskette. These diskettes should be submitted to: Ernestine Creech, Accounting Safeguards Division, 2000 L Street, N.W., Suite 257, Washington, D.C. 20036. Such a submission should be on a 3.5 inch diskette formatted in an IBM compatible format using WordPerfect 5.1 for Windows or compatible software. The diskette should be accompanied by a cover letter and should be submitted in "read only" mode. The diskette should be clearly labelled with the commenter's name, proceeding (including the lead docket number in this case CC Docket No. 98-137, type of pleading (comment or reply comment), date of submission, and the name of the electronic file on the diskette. The label should also include the following phrase "Disk Copy - Not an Original." Each diskette should contain only one party's pleadings, preferably in a single electronic file. In addition, commenters must send diskette copies to the Commission's copy

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[62] *See* Electronic Filing of Documents in Rulemaking Proceedings, 63 Fed. Reg. 24,121 (1998).

contractor, International Transcription Service, Inc., 1231 20th Street, N.W., Washington, D.C. 20037.

30. Written comments by the public on the proposed and/or modified information collections are due on or before November 23, 1998. Written comments must be submitted by the Office of Management and Budget (OMB) on the proposed and/or modified information collections on or before 60 days after date of publication in the Federal Register. In addition to filing comments with the Secretary, a copy of any comments on the information collections contained herein should be submitted to Judy Boley, Federal Communications Commission, Room 234, 1919 M Street, N.W., Washington, DC 20554, or via the Internet to jboley@fcc.gov and to Timothy Fain, OMB Desk Officer, 10236 NEOB, 725 - 17th Street, N.W., Washington, DC 20503 or via the Internet to fain_t@al.eop.gov.

V. ORDERING CLAUSES

31. Accordingly, IT IS ORDERED that, pursuant to Sections 1, 4, 11, 201-205, 215, 218, 220 and 403 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, 161, 201-205, 215, 218, 220 and 403 that NOTICE IS HEREBY GIVEN of proposed amendments to Parts 32 and 43 of the Commission's rules, 47 C.F.R. Parts 32 and 43, as described in this NOTICE OF PROPOSED RULEMAKING.

32. IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, SHALL SEND a copy of this NOTICE OF PROPOSED RULEMAKING, including the Initial Regulatory Flexibility Certification, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

Separate Statement of Commissioner Harold W. Furchtgott-Roth

In re: Notice of Proposed Rulemaking

1998 Biennial Regulatory Review -- NPRM to Propose Ways to Eliminate Unnecessary Regulations and Functions Associated with Our Depreciation Prescription Process.

I support adoption of this NPRM. In my view, any reduction of unnecessary regulatory burdens is beneficial. To that extent, this item is good and I am all for it. As I have pointed out in statements on other biennial review items, this item should not, however, be mistaken for complete compliance with Section 11 of the Communications Act.

There is another issue at hand for this NPRM, however, concerning the costs and benefits of our regulations. In an earlier biennial review NPRM, 1998 Biennial Regulatory Review -- Elimination of Part 41 Telegraph and Telephone Franks, CC Docket No. 98-119, Notice of Proposed Rulemaking (released July 21, 1998) ("Franks NPRM"), the Commission included the following paragraph:

> In this Notice, we tentatively conclude that no Part 41 regulation is necessary and we accordingly propose to eliminate Part 41, in toto. If any commenters consider that some form of regulation is required to govern the provision of franks and certain section 201(b) reports, we encourage them to suggest alternatives that are less burdensome than those currently set out in Part 41. *Such commenters, to the extent that they wish to retain Part 41 regulation, should present a cost-benefit analysis addressing the costs of compliance, including direct costs and burdens on companies, regulators, customers and taxpayers, as well as any indirect costs. The statute affords the Commission wide discretion in determining the contours of the public interest. We also note that many costs and benefits of regulation may be difficult, if not impossible to quantify. As a general matter, however, we will not maintain a regulation pursuant to the section 11 public interest analysis where we determine that the costs of the regulation exceed the benefits. We seek comment on this approach.* Overall, we seek comment on any and all analysis and conclusions contained in this Notice. *Id.* Para. 19 (emphasis added).

With simple modifications to reflect the different rule section at issue, I proposed to include the same language in this NPRM. Yet my colleagues would not support my proposal. Instead, they agreed to include the following sentence: "In addition to our more specific requests for comment below, we invite commenters to submit information on the costs and benefits of the rules at issue in this proceeding and of our proposed modifications."

Although I generally support the new language and appreciate my colleagues' willingness to include it, I do not understand what has changed in the two months since the Franks NPRM, cited above, that would cause my colleagues to support -- after considerable discussion -- the prior language in July but not now.

More fundamentally and importantly, I do not understand why my colleagues oppose the statement that, "as a general matter," the Commission "will not maintain a regulation pursuant to the section 11 public interest analysis where we determine that the costs of the regulation exceed the benefits." *Id.* Opposing this language gives the impression, hopefully false, that the Commission would be willing to maintain a rule for which the benefits fall short of the costs.

Of course, I recognize that some costs and benefits are difficult to quantify. I was willing, therefore, to support the statement in the Franks NPRM, quoted above, that "[w]e also note that many costs and benefits of regulation may be difficult, if not impossible to quantify." *Id.* With this caveat, we unanimously adopted the cost-benefit language in the Franks NPRM.

What has changed since July? I do not know. Nor do I understand, especially having acknowledged the empirical challenges of cost-benefit analyses, why the FCC would consider keeping rules that confer fewer benefits than burdens on industry and consumers.

As for the scope of the Commission's Section 11 review, I have explained previously that the FCC is not planning to "review all regulations issued under this Act . . . that apply to the operations or activities of any provider of telecommunications service," as required under Subsection 11(a) in 1998 (emphasis added). *See generally* 1998 Biennial Regulatory Review -- Review of Computer III and ONA Safeguards and Requirements, 13 FCC Rcd 6040 (released Jan. 30, 1998). Nor has the Commission issued general principles to guide our public interest analysis and decision-making process across the wide range of FCC regulations.

In one important respect, however, the FCC's current efforts are more ambitious and difficult than I believe are required by the Communications Act. Subsection 11(a) --"Biennial Review" -- requires only that the Commission "determine whether any such regulation is no longer necessary in the public interest" (emphasis added). It is pursuant to Subsection 11(b) --"Effect of Determination" -- that regulations determined to be no longer in the public interest must be repealed or modified. Thus, the repeal or modification of our rules, which requires notice and comment rule making proceedings, need not be accomplished during the year of the biennial review. Yet the Commission plans to complete roughly thirty such proceedings this year.

I encourage parties to participate in these thirty rule making proceedings. I also suggest that parties submit to the Commission -- either informally or as a formal filing -- specific suggestions of rules we might determine this year to be no longer necessary in the public interest as well as ideas for a thorough review of all our rules pursuant to Subsection 11(a).