

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

SOUTH CENTRAL RURAL TELEPHONE	)	
COOPERATIVE CORPORATION, INC.'S	)	CASE NO.
AVOIDED COST METHODOLOGY AND	)	2001-014
STUDY	)	

O R D E R

BACKGROUND

On January 17, 2001, South Central Rural Telephone Cooperative Corporation, Inc. ("South Central") filed a petition with supporting documentation, asking for approval of its avoided cost study and resulting wholesale discount rate. South Central's study, a copy of which is attached here to as Appendix A, produced a whole discount rate of 6.06 percent. South Central filed the petition pursuant to Administrative Case No. 355.<sup>1</sup> The filing, according to South Central, also conforms to the Commission's decision in Case No. 99-376.<sup>2</sup> In its Order in Case No. 99-376, the Commission allowed all companies exempted under Section 251(f)(1) of the Telecommunications Act of 1996 to defer filing avoided cost studies until further Order of the Commission and upon notice to the Commission of their intent to defer filing. On September 28, 1999, South Central filed notice of intent to defer until it received a bona fide request for interconnection from a competitive local exchange carrier. However, by filing this study, South Central

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<sup>1</sup> Administrative Case No. 355, An Inquiry Into Local Competition, Universal Service, and the Non-Traffic Sensitive Access Rate.

<sup>2</sup> Case No. 99-376, Approving Duo County's Avoided Cost Methodology and Study.

waives its right to continued deferral. The Commission reviews this study based upon its compliance with the methodology ordered in previous cost study decisions.

### THE STUDY

According to South Central, its cost study was prepared in accordance with the Commission's Order in Administrative Case No. 355 and conforms to the guidelines prescribed in Case No. 99-376 and the relevant Eighth Circuit Court of Appeals decision.<sup>3</sup> South Central argues that, to the extent the methodology used by the Commission to determine wholesale discount rates in previous filings does not comply with the Eighth Circuit's decision, the methodology must be revised. South Central states that because the Eighth Circuit found that the plain meaning of the Telecommunications Act of 1996 is that the wholesale discount rate should be based on costs that are actually avoided,<sup>4</sup> not those that could be avoided, indirect costs should not be included in the discount rate. Therefore, South Central does not include in its calculation any expenses assigned to indirect accounts.

South Central also argues that the expenses in the accounts Product Management - Account 6611, Sales - Account 6612, Product Advertising - Account 6613, and Customer Services - Account 6623 will not normally occur in a resale environment and therefore will be 100 percent avoided, while none of the expenses in Call Completion - Account 6621 and Number Services - Account 6622 will be avoided. South Central then applies these avoided cost percentages to the portion of each

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<sup>3</sup> Iowa Utilities Board, et al., v. Federal Communications Commission, 219 F.3d 744, 754-756 (2000).

<sup>4</sup> Id. at 755.

account representing local service and intraLATA toll expenses. South Central assigns a 50 percent avoided rate to uncollectibles and subtracts the result from directly avoided costs, and uses retail revenue subject to resale as the denominator in the computation of the wholesale discount rate. Finally, it submitted an analysis, by job function of Customer Service – Account 6623 that determined, on a composite basis, that 83.02 percent of the total account will be avoided.

### ADJUSTMENTS

In reviewing past avoided cost studies, the Commission has structured its methodology to generally conform to the outline proposed by the Federal Communications Commission (“FCC”) in its First Report and Order.<sup>5</sup> This methodology included recognition of the avoidance of indirect costs in proportion to the relationship of directly avoided costs to total direct costs. It is clear to the Commission that indirect or shared costs such as general overheads support all of the incumbent local exchange carriers’ (“ILEC”) functions including marketing, sales, billing and collection and other avoided retail functions.

Therefore, it is clear that the overall level of indirect expenses can be expected to decrease as a result of a lower level of overall operations in a wholesale environment. The Commission has taken the position that, in the absence of evidence by South Central, a certain portion of indirect cost would be actually avoided and therefore should be included in its calculations. Since South Central did not demonstrate with certainty

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<sup>5</sup> Implementation of the Local Competition Provisions in the Telecommunications Act of 1996 (CC Docket No. 96-98), and Interconnection Between Local Exchange Carriers and Mobile Radio Service Providers (CC Docket No. 96-185, First Report and Order, Released August 8, 1996).

that indirect costs will not be partially avoided, the Commission will include an allocation of indirect costs in its determination of the company's wholesale discount rate using South Central's percentages and partial account balances. The change would increase the wholesale discount rate to 7.54 percent.

South Central did not perform an account analysis to determine the avoided costs in Account 6613 – Product Advertising, Account 6621 – Call Completion and Account 6622 – Number Services. Instead it assigned a 100 percent avoided cost factor to the local and intraLATA expense included in these accounts. With regard to Customer Service - Account 6623, although South Central examined each function within the account and found that 83.02 percent of all charges to the account were expected to be avoided, South Central still applied a 100 percent avoided cost factor to the estimated local and intraLATA toll expenses included in the account. In Case No. 99-376, the Commission found that application of an avoided cost percentage determined on the basis of an entire account to only a portion of that account was inappropriate and rejected this methodology. If South Central's percentages were applied against the total account as required in Case No. 99-376, the wholesale discount rate would be 11.71 percent. The Commission will accept South Central's percentages and use the 100 percent and the 83.02 percent as determined by South Central and apply these percentages to the total account, consistent with the Commission's decision in Case No. 99-376. Substituting the 83.02 percent for the 100 percent for Customer Service and applying the 83.02 percent against the entire account results in a wholesale discount rate of 9.80 percent.

Finally, South Central assigned a 50 percent avoided cost percent to uncollectibles based upon the presumption that some delinquent customers will be lost to resellers. However, South Central opines that it is virtually impossible to determine which customers will switch. It also deducted the avoided costs it calculated for uncollectibles from the directly avoided cost. The correct methodology requires that uncollectible avoided costs are added, along with other indirect avoided costs, to the directly avoided costs. Pursuant to the Commission's decision in this case to include indirect costs in the wholesale discount rate computation, and in accordance with the Commission's treatment of uncollectible revenues in the rehearing in Case No. 99-376, uncollectible revenues will be treated as indirect costs. This change results in the final wholesale discount rate of 9.60 percent.

#### WHOLESALE DISCOUNT RATE

The Commission has determined that certain adjustments as discussed herein should be made to the avoided cost study as proposed by South Central to produce a wholesale discount rate of 9.60 percent (Appendix B). This discount will be offered to any competitive local exchange carrier reselling South Central's tariffed services.

IT IS THEREFORE ORDERED that the appropriate wholesale discount rate for South Central's retail services shall be 9.60 percent.

Done at Frankfort, Kentucky, this 19<sup>th</sup> day of April, 2001.

By the Commission

ATTEST:

  
Executive Director

APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2001-014 DATED APRIL 19, 2001

South Central  
Estimated Act Compliant Avoided Cost Study

Line	Account Description	Per Study 12/31/98	Estimated Local & IntraLATA Toll*	Avoided Costs	
				%	Total
<u>Direct Accounts</u>					
1	6611 Product Management	\$ -	\$ -	100.00%	\$ -
2	6612 Sales	\$ -	\$ -	100.00%	\$ -
3	6613 Product Advertising	\$ 16,299	\$ 8,309	100.00%	\$ 8,309
4	6621 Call Completion	\$ -	\$ -	0.00%	\$ -
5	6622 Number Service	\$ 159,133	\$ 101,766	0.00%	\$ -
6	6623 Customer Services	\$ 820,130	\$ 524,473	100.00%	\$ 524,473
7	Other	\$ 8,933,391	\$ 5,693,934		
8	Total Direct Cost	\$ 9,928,953	\$ 6,328,482		\$ 532,782
<u>Indirect Accounts</u>					
9	6711 Executive	\$ 286,176		0.00%	\$ -
10	6712 Planning	\$ 1,812		0.00%	\$ -
11	6721 Accounting & Finance	\$ 262,707		0.00%	\$ -
12	6722 External Relations	\$ 73,547		0.00%	\$ -
13	6723 Human Resources	\$ 79,087		0.00%	\$ -
14	6724 Information Management	\$ 98,343		0.00%	\$ -
15	6725 Legal	\$ 37,546		0.00%	\$ -
16	6726 Procurement	\$ 85,392		0.00%	\$ -
17	6727 Research & Development	\$ 12,223		0.00%	\$ -
18	6728 Other G&A	\$ 281,328		0.00%	\$ -
19	6121 Land and Buildings	\$ 250,320		0.00%	\$ -
20	6122 Furniture	\$ 4,147		0.00%	\$ -
21	6123 Office Equipment	\$ 43,902		0.00%	\$ -
22	6124 General Purpose Computer	\$ 86,684		0.00%	\$ -
23	5301 Uncollectible Revenue	\$ (39,374)		50.00%	\$ (19,687)
24	Indirect Avoided Cost				\$ (19,687)
25	Total Avoided Cost				\$ 513,095
26	Basic Local Service	\$ 7,406,880			
27	LD Network Services	\$ 1,056,015			
28	Revenues Subject to Resale	\$ 8,462,895			
29	Avoidable Discount				6.06%

\*These are estimated based on the cost of a similarly situated LEC.



APPENDIX B

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 2001-014 DATED APRIL 19, 2001



