service purchased pursuant to section 251(c)(4) will receive the full amount of universal service support previously provided to the incumbent LEC for that customer.[222] That section, however, does not provide a corresponding reduction in the amount of support received by the incumbent LEC. Accordingly, we amend section 54.307(a)(4) to clarify that, when a competitive eligible telecommunications carrier receives support for a customer pursuant to section 54.307(a)(4), the incumbent LEC will lose the support it previously received that was attributable to that customer.

F. Corporate Operations Expenses

1. Background

85. In the *Order*, the Commission adopted a formula to limit the amount of corporate operations expenses that a carrier may recover through the existing high cost loop support mechanisms.[223] This formula was developed to "ensure that carriers use universal service support only to offer better service to their customers through prudent facility investment and maintenance consistent with their obligations under section 254(k)."[224] Based on comments in both the Docket No. 96-45 and the preceding universal service docket, Docket No. 80-286, the Commission decided to "limit universal service support for corporate operations expense to a reasonable per-line amount, recognizing that small study areas, based on the number of lines, may experience greater amounts of corporate operations expense per line than larger study areas."[225] The maximum allowable corporate operations expense formula was based on a staff analysis of data submitted by NECA.[226]

86. In the *July 10 Order*, the Commission made two modifications to this

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[222] 47 C.F.R. § 54.307(a)(4).

[223] *Order*, 12 FCC Rcd at 8930-32. Corporate operations expenses include all of the expenses listed in sections 32.6710 through 32.6712 and sections 32.6720 through 32.6728 of the Commission's rules. 47 C.F.R. §§ 32.6710-32.6712; 47 C.F.R. §§ 32.6720-32.6728. Those categories of expenses include: executive; planning; general; administrative; accounting; finance; external relations; human resources; information management; legal; procurement; research and development; and other general and administrative expenses. *Id.*

[224] *See Order*, 12 FCC Rcd at 8930-31.

[225] *See Order*, 12 FCC Rcd at 8930-31.

[226] This formula, allowing corporate operations expense per line to depend upon the number of access lines, was based on a linear spline regression model that forces two line segments with different slopes to intersect. The model had declining costs per line as access lines increase to 10,000 and constant costs per line for companies with more than 10,000 lines.

formula.[227] First, the Commission established a floor on the monthly corporate operations expense cap at $9,505, to allow carriers with relatively few working loops to receive sufficient support to recover initial or fixed corporate operations expenses.[228] The second change addressed a feature of the original formula under which the cap on support for corporate operations expense for carriers whose working loops are within a certain range did not increase with the number of working loops. The revision added another component to the model to ensure that the cap on support for corporate operations expenses does not decrease as the number of working loops increases. Based on these changes on the original model, the formula was defined in the following manner:

> for study areas with 6,000 or fewer working loops the amount per working loop shall be [$27.12 - (0.002 x the number of working loops)] x 1.15 or [1.15 x $8,266/the number of working loops], whichever is greater;
>
> for study areas with more than 6,000 but fewer than 17,988 working loops, the amount per working loop shall be ($72,024/the number of working loops + 3.12) x 1.15;
>
> for study areas with 17,988 or more working loops, the amount per working loop shall be $7.12 x 1.15.[229]

2. Pleadings

87. Several parties representing the interests of small incumbent LECs submitted petitions requesting that the Commission reconsider its decision to place a limit on the recovery of corporate operations expenses.[230] Additionally, three parties filed petitions for

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[227] *July 10 Order*, 12 FCC Rcd at 10102-05.

[228] When the $9,505 monthly figure is converted to an annual figure, the annual minimum corporate expense cap is $114,071.

[229] 47 C.F.R. § 36.621.

[230] Alaska Telephone Association petition at 4; Fidelity Telephone Co. petition at 3-4; GVNW petition at 10-12; RTC petition at 19-20; USTA petition at 10; Western Alliance petition at 8-9. At least one petitioner raised issues that were addressed in the Commission's *July 10 Order*. GVNW petition at 9-10 (stating that the absolute amount of corporate operations expenses declines as the company size increases from 6,850 loops to 10,000 loops and that at 12,900 loops the allowance returns to that of a 6,700 loop company). We note that petitions for reconsideration were due on July 17, 1997, and that the Commission's Order on Reconsideration was released to the public on July 10, 1997. Thus, some petitions for reconsideration raised issues that were addressed several days earlier in the *Order on Reconsideration*.

reconsideration after the Commission modified the corporate operations expenses limitation in its *July 10 Order*.[231] Specifically, these parties argue that, contrary to the Commission's finding in the *Order*, corporate operations expenses are part of providing universal service,[232] and are not discretionary.[233] Additionally, the petitioners assert that this policy ignores Congress's intent to limit burdens on small, rural, and insular carriers and, in fact, disproportionately burdens smaller incumbent LECs;[234] that the decision not to allow a transition period is inconsistent with prior Commission determinations;[235] that reductions in support will lead to increases in price for local service and therefore universal service support is not "sufficient";[236] that, because of increased regulatory activity stemming from the 1996 Act, corporate operations expenses are increasing, not decreasing;[237] that reasonableness of corporate operations expenses cannot be judged by statistical analysis, but must be judged according to each incumbent LEC's "own specific history and environment";[238] that federal

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[231] Rural Telephone Coalition petition to July 10 Order; Western Alliance petition to July 10 Order; U S West petition to July 10 Order.

[232] Alaska Telephone Association petition at 4; USTA petition at 10; Western Alliance petition at 8-9 (citing Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, *Recommended Decision and Order*, 5 FCC Rcd 7578, 7579 (1990) and Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, *Report and Order*, 6 FCC Rcd 2936 (1991)); *accord* Virgin Islands Telephone Company reply at 7-8; *see also* RTC petition to July 10 Order at 2-3, 4 (stating that the Commission's reasoning that corporate operations expenses result from managerial priorities is insufficient because this is true of all spending, including purchase of network plant and facilities and stating that nothing in section 254 limits support to physical facilities).

[233] Western Alliance petition to July 10 Order at 6-7 (stating that only accounts 6722(a) and (b) are discretionary); RTC petition to July 10 Order at 3-4 (stating that compliance with cost separation studies, revenue requirement and settlement calculations, special Commission data requests external audits, and service cost filings are not discretionary).

[234] Alaska Telephone Association at 4-5; GVNW petition at 10-11; Western Alliance at 10; Virgin Islands Tel. Co. July 10 reply at 8-9 (citing 47 U.S.C. § 254(b)(3)'s reference to insular areas)

[235] Fidelity petition at 3, 5 (stating that the Commission found that rural LECs require ample time to adjust to any changes in support calculations and favoring a three year transition period).

[236] Fidelity petition at 4; *see also* Virgin Islands Tel. Co. at 9; Virgin Islands July 10 reply at 10 (citing 47 U.S.C. § 254(b)(5)'s directive that support be "specific, predictable, and sufficient").

[237] Fidelity petition at 4; RTC petition at 19; Western Alliance petition at 8-9; *see also* TCA reply at 4-5 (referencing inflation in addition to increases caused by regulatory changes and citing FCC's budget increase of 21 percent to implement the 1996 Act); Virgin Islands July 10 reply at 8.

[238] Western Alliance petition at 10; Western Alliance petition to July 10 Order at 8; RTC petition to July 10 Order at 4, 8-9 (asserting that the Commission should presume all expenses are reasonable and should conduct an investigation to identify individual expenses that it believes to be unreasonable).

regulatory expenses should not be included within the limitation to ensure that small companies will be able to adequately participate in the federal regulatory process;[239] and that the Commission has contradicted its stated intention to provide universal service support to rural LECs based on embedded costs and to defer using proxy models for rural carriers until January 1, 2001.[240] RTC argues that the Commission did not satisfy the requirements of the Regulatory Flexibility Act to consider alternatives to the cap.[241] RTC asserts that the Commission should not assume that up to 35 percent of all recipients are incurring expenses beyond a "range of reasonableness."[242]

88. In addition to challenging the decision to limit corporate operations expenses, several petitioners criticize specific portions of the method used to calculate the formula. For example, GVNW states that it is not clear whether the corporate operations expenses rule includes amounts from Accounts 6710 and 6720 or whether it includes "that portion assigned to loop cost in NECA's USF Algorithm (AL19)."[243] Western Alliance asserts that the *Order* contained no discussion or reasoned explanation of "(a) how or why the 115 percent ceiling was selected; (b) why a regression analysis using a spline function technique was accurate and appropriate; or (c) how or why the 1995 NECA data was representative."[244] Western Alliance also asserts that the data for LECs with more than 15,000 loops appear to fit the Commission's regression line relatively closely, but the data for LECs with fewer than 15,000 loops, and particularly for those with fewer than 5,000 loops, are widely scattered about the line.[245] Several petitioners suggest the Commission adopt a minimum cap of $300,000 to protect smaller carriers.[246] Some petitioners also favor such a minimum cap that does not

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[239] ITC petition at 7-9.

[240] TCA reply at 5; *see also* RTC petition to July 10 Order at 6 (arguing that the formula is a proxy model and that this proxy does not meet the criteria the Commission has adopted for the forward-looking cost models for non-rural carriers).

[241] RTC petition to July 10 Order at 8, n.11 *citing* 5 U.S.C. § 603.

[242] RTC petition to July 10 Order at 6 (asserting that approximately 200 companies, or 35 percent of all cost companies, will receive less support under the July 10 formula).

[243] GVNW petition at 9.

[244] Western Alliance petition at 9.

[245] Western Alliance petition to July 10 Order at 8.

[246] GVNW petition at 9-10 (proposing a minimum allowance of $300,000); USTA petition at 10-11 (advocating a $300,000 minimum and a limit of two standard deviations); *contra* Virgin Islands Tel. Co. reply to July 10 Order at 11 (does not favor $300,000 minimum because it will not provide relief to mid-sized companies such as Virgin Islands Tel. Co.).

vary by line count because they argue that it would more accurately reflect how corporate operations expenses are incurred.[247]

89. TCA and Virgin Islands Tel. Co. generally support the petitions for reconsideration.[248] Virgin Islands Tel. Co. asserts that the Commission's decision to adopt a nationwide cap violates the Act's requirement that the Commission ensure that rates in rural, insular, and high cost areas are comparable to those in urban areas.[249] Virgin Islands Tel. Co. asserts that the limitation on recovery of corporate operations expenses violates the Act's requirement that universal service support be "sufficient."[250] Virgin Islands Tel. Co. also asserts that the Commission's decision not to grant study area waivers for corporate operations expenses in excess of 115 percent of the national average absent "exceptional circumstances" based on its finding that such expenses are "not necessary for the provision of universal service" has effectively rendered relief through a study area waiver "unobtainable."[251] TCA and RTC argue that the Commission improperly invoked section 254(k) in support of its decision to limit corporate operations expenses.[252] TCA asserts that the Commission incorrectly relied on the comments of interexchange carriers suggesting that no common costs should be assigned to the loop to support the Commission's implied finding that carriers are subsidizing competitive services by recovering an excessive level of corporate operations expenses from high cost loop support mechanisms.[253]

90. Several petitioners challenge the procedural bases of both the *Order* and the *July 10 Order* under which the Commission's decided to limit corporate operations expenses. In particular, Western Alliance alleges that the Joint Board made no recommendation with

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[247] RTC Petition of July 10 Order at 6 (stating that management salaries do not vary by size); Western Alliance petition to July 10 Order at 4 (arguing that the minimum monthly allowance of $9,505.90 is insufficient to retain employees such as telephone managers and accountants for rural LECs).

[248] TCA reply at 1-4; Virgin Islands Telephone Corporation reply at 7-12.

[249] Virgin Islands reply at 7, 8-9 *citing* 47 U.S.C. § 254(b)(3).

[250] Virgin Islands Tel. Co. reply at 10.

[251] Virgin Islands Tel. Co. July 10 reply at 12-13 (asserting that the heavier waiver burden is inconsistent with the 1996 Act); *accord* RTC petition to July 10 Order at 8. *See also Order*, 12 FCC Rcd at 8932.

[252] RTC petition at 20 (asserting that the Commission did not properly consider whether current levels of corporate operations expenditures are inconsistent with section 254(k)); TCA reply at 4 (asserting that section 254(k) has nothing to do with properly allocating part 32 expenses); *accord* RTC July 10 Petition at 4. Section 254(k) states, in part: "A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition."

[253] TCA reply at 4.

respect to changing the recovery of corporate operations expenses.[254] Western Alliance also argues that this decision is a "vestige" of Docket No. 80-286, which Congress did not view as an appropriate foundation on which to base the proceedings for implementing the universal service provisions of the 1996 Act.[255] Western Alliance alleges that the Commission has not met the standard imposed by the Court of Appeals for the D.C. Circuit by supplying "reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored."[256] RTC contends that the Commission gave insufficient notice before adopting the limitation on corporate operations expense. Specifically, RTC contends that the Commission should have allowed all interested parties to comment on the formula, underlying data, assumptions, and outputs, that there was no notice in Docket No. 96-45, and that the notice in Docket No. 80-286 consisted of only four sentences.[257] TCA asserts that, because 1996 expenses have already been incurred, rural LECs have no opportunity to reduce costs to levels that are consistent with the cap adopted by the Commission.[258]

91. AT&T, Comcast/Vanguard, GCI, and MCI oppose the petitioners' requests that the Commission reconsider limiting recovery of corporate operations expenses and urge the Commission to maintain the limitation.[259] AT&T agrees with the Commission that these expenses are not directly related to the provision of subscriber loops.[260] Comcast/Vanguard and GCI question whether rural LECs should receive universal service support -- which they note is funded by, among others, LEC competitors -- for expenses such as lobbying and the costs of moving into a competitive environment.[261] MCI states that none of the petitioners

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[254] Western Alliance petition at 9.

[255] Western Alliance petition to July 10 Order at 5-6.

[256] Western Alliance at 9 *quoting Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970); *accord* Virgin Islands Tel. Co. reply at 10-11 (arguing that the Commission provided insufficient reasoning to justify its decision to limit corporate operations expenses and the decision to limit expenses to those within 115 percent of the formula); Virgin Islands Tel. Co. July 10 reply at 12.

[257] RTC petition to July 10 Order at 5, 7.

[258] TCA reply at 5.

[259] AT&T opposition at 13; Comcast/Vanguard opposition at 9; General Communications opposition at 4-5; MCI opposition at 13. GCI also filed an opposition to the petitions to the July 10 Order. *See* GCI July 10 opposition.

[260] AT&T opposition at 13.

[261] Comcast/Vanguard opposition at 8-9; General Communications opposition at 4-5 (describing expenses such as advertising and improving customer service that are included in corporate operations expenses and will be incurred by incumbent LECs in a more competitive environment); *contra* RTC reply at 8-9 (arguing that limiting recovery of corporate operations expenses will hamper ability of small incumbent LECs to perform the

offered any evidence to rebut the Commission's findings that corporate operations expenses are discretionary and not inherent to the provision of universal service.[262]

3. Discussion

a. Imposition of a Limitation

92. In light of these challenges to the Commission's decision to limit recovery of corporate operations expenses, we take this opportunity to explain more fully the bases for this decision.[263] Expenditures for corporate operations in many instances may be discretionary, in contrast, for example, to expenditures to maintain existing plant and equipment.[264] Corporate operations expenses include, for example, travel, lodging and other expenses associated with attending industry conventions and corporate meetings. Although participation in such activities may be prudent, the levels of these expenditures are subject to managerial discretion. Carriers currently have little incentive to minimize these expenses because the current mechanism for providing support in high cost areas allows carriers to recover a large percentage of their corporate operations expenses. For companies with fewer than 200,000 lines, for example, the expenses attributed to the high cost expense adjustment are covered in full for companies with costs in excess of 150 percent of the national average.[265] Smaller carriers possess even fewer incentives to minimize corporate operations expenses because the Commission has a limited ability to ensure, through audits, that smaller companies properly assign corporate operations expenses to appropriate accounts and that these expenses do not exceed reasonable levels. The Commission, and frequently state commissions, cannot justify auditing smaller carriers because the Commission's audit staff is small, there are many hundreds of small telephone companies, and the costs of full-scale audits are in many instances likely to exceed any expenses found to be improper. We, therefore, conclude that imposing a cap that is relatively generous to small carriers, but still imposes a limitation, is a reasonable method of encouraging carriers to assign corporate operations expenses to the proper accounts and discouraging carriers from incurring excessive expenditures. Under this approach, we provide carriers with an incentive to control their

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planning necessary to facilitate competition).

[262] MCI opposition at 13.

[263] *See, e.g.,* Western Alliance at 9.

[264] NYDPS further comments at 6 n.1; *see also* AT&T further comments at 24, att. A (suggesting that recovery of all administrative expenses be excluded), NECA further comments at 19 (stating that, if the Commission is concerned about excessive levels of general and administrative expenses, it may wish to consider using statistical measures, such as the two standard deviation test proposed by NECA in the 80-286 proceeding).

[265] *See* 47 C.F.R. § 36.631(c).

corporate operations expenses without requiring carriers to incur the costs associated with a full Commission audit. As the Commission stated in its *Order* and as explained further below, carriers that contend that the limitation provides insufficient support may request a waiver from the Commission.[266] Therefore, only carriers whose expenses exceed the cap and who contend that the capped amount is insufficient will be required to provide additional justification for their expenditures. We, therefore, conclude that a cap on federal support for corporate operations expenses is a reasonable method of preventing the recovery of improperly assigned or excessive expenses from federal funds while minimizing the administrative burden on the Commission and on all carriers, including smaller carriers.

93. We disagree with petitioners who assert that, because some corporate operations expenses are not discretionary, we should not impose any limit on the recovery of corporate operations expenses.[267] We recognize that the expenses cited by petitioners and commenters may be necessary for the operation of a company, and that such expenditures are in some circumstances required by state or federal law or regulation.[268] Most companies, however, fulfill all such state and federal requirements while incurring corporate operations expenses that are well below the limitation imposed by the Commission.[269] No party has provided detailed data explaining the significant differences in corporate operations expenses for companies of similar sizes.[270] Further, we are not excluding recovery of corporate operations expenses from universal service support, but instead are imposing a reasonable limit. We reject ITC's request to exclude all federal regulatory expenses from the limitation because, although some expenditures may be necessary to participate in the federal regulatory process,

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[266] *Order*, 12 FCC Rcd at 8932.

[267] *Accord* Opposition by Comcast/Vanguard at 9; General Communications at 4-5; and MCI at 13; *contra, e.g.*, RTC Reply at 1-2, 8-9.

[268] *See, e.g.*, RTC petition to July 10 Order at 3-4 (stating that compliance with cost separation studies, revenue requirement and settlement calculations, special Commission data requests external audits, and service cost filings are not discretionary).

[269] The methodology used to calculate the cap ensures that more than a majority of carriers subject to this cap incur corporate operations expenses well below the cap, *see infra*, and we are not aware of any carrier that is currently unable to fulfill all of its state and federal requirements within current levels of expenditure.

[270] Although several Alaskan companies did provide more detailed breakdowns of their corporate operations expenses, these companies did not explain with specificity why their expenses differ from the expenses of similarly sized companies. *See* letter from Paula Eller, President, Yukon Telephone Company to William F. Caton, Acting Secretary, FCC (Sept. 17, 1997) (providing additional information for Yukon Telephone Company, Mukluk Telephone Company, Interior Telephone Company, Mantanuska Telephone Association, and Arctic Slope Telephone Association Cooperative).

we see no reason to permit the unlimited recovery of such expenses.[271] Moreover, individual companies that are required to incur unusually high corporate operations expenses, such as Alaskan or insular telephone companies, have the right to apply for a waiver with the Commission to demonstrate the necessity of these expenses for the provision of the supported services.[272]

b. Adjustments to Limitation Formula

94. In the *July 10 Order*, the Commission specified a minimum allowable corporate operations cost in order to ensure that carriers with small numbers of working loops would receive sufficient support to recover initial or fixed corporate operations expenses.[273] This monthly cost minimum was estimated from a regression of total corporate operations expenses on the number of working loops.[274] After performing this analysis, the Commission adopted a minimum monthly recovery of $9,505, which results in a minimum recovery of $114,071 per year.[275] USTA and GVNW urge the Commission to increase this minimum recovery from $114,071 per year to $300,000 per year.[276] USTA additionally advocates adopting a limitation equal to the greater of either $300,000 per year or $34.82 per line per month.[277]

95. We reconsider, to a limited extent, the limitation on recovery of corporate operations expenses and adopt a new minimum cap of $300,000 per year as advocated by USTA and GVNW. Although we are fully confident in the formula that calculates the cap, we adopt a minimum cap of $300,000 out of an abundance of caution for the smallest carriers.[278] The increased minimum will reduce the need of the smallest carriers to seek a waiver of the cap. We intend to continue to monitor the effect of this limitation and the $300,000 minimum cap on smaller carriers. We note that, because the Commission has

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[271] *See* ITC petition at 7-9.

[272] *See, e.g.*, Alaska Tel. Ass'n petition at 4; TCA petition at 1-5; Virgin Islands Tel. Co. petition at 8; RTC petitions to July 10 Order at 2-4.

[273] *See July 10 Order*, 12 FCC Rcd at 10104.

[274] *July 10 Order*, 12 FCC Rcd at 10102-03.

[275] 47 C.F.R. § 36.621.

[276] GVNW petition at 9-10; USTA petition at 10-11.

[277] USTA indicates that this figure is "two standard deviations from zero." USTA does not provide the calculations which produced this figure. Letter from Porter E. Childers, Executive Director, Legal and Regulatory Affairs, USTA to William F. Caton, Acting Secretary, FCC (Oct. 6, 1997) (*USTA Oct. 6 ex parte*).

[278] *See* 5 U.S.C. §§ 601-612 (Regulatory Flexibility Act).

adopted an indexed cap for all high cost support, increases in the amount of support provided to some companies will reduce the amount of support provided to other companies. We find, however, that this change will result in a minimal increase in the total amount of universal service support provided to carriers.[279] We will continue to monitor this issue closely and will take steps to ensure that only necessary and prudent expenditures are supported. We do not adopt USTA's alternative proposal to increase recovery to $34.82 per line per month for all carriers because we believe the minimum cap of $300,000 provides adequate protection for the smallest carriers while imposing the smallest corresponding decrease in high cost loop support for carriers overall.[280]

96. Upon reconsideration, we make an additional change in the limitation formula to address a small discontinuity in the formula that causes the total allowable corporate operations expense to be slightly lower in the range from 17,988 and 17,997 lines than the amount computed at 17,987 lines.[281] To eliminate the anomaly caused by this discontinuity, we alter the second threshold for access lines from 17,988 lines to 18,006 lines. Finally, to make our rules easier to apply, we standardized general mathematical conventions in the formulas.[282]

c. Methodology Used to Calculate the Limitation

97. Western Alliance questions the methodology the Commission used to create the formula for the corporate operations expense limitation. Western Alliance asserts that the *Order* contained no discussion or reasoned explanation of: "(a) why a regression analysis using a spline function technique was accurate and appropriate; (b) how or why the 115 percent ceiling was selected; or (c) how or why the 1995 NECA data were representative."[283] We address these arguments in turn. As detailed further in the *July 10 Order*, the Commission used a linear spline to estimate average corporate operations cost per loop, based on the number of loops served. To produce this formula, we used statistical regression techniques that focused on the relationship between expenses per loop, rather than total expense. We adopted this approach in order to establish a model under which the cap on

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[279] *See* GVNW petition at 12 (indicating that a $300,000 minimum cap will result in an increase equal to approximately 0.2 percent of all high cost support).

[280] As noted, because of the indexed cap, increases in high cost loop support for some carriers will decrease such support levels for the remaining carriers.

[281] At 17,988 loops, total allowable corporate operations cost drops $79.30 from $147,365 to $147,285.70.

[282] For example, we distributed the 1.15 multiplier throughout the formulas and we no longer round 8.188 to 8.19 in section 36.631(a)(4)(ii)(C).

[283] Western Alliance petition at 9.

corporate operations expense per line would decline as the number of loops increases for a range of smaller companies so that economies of scale, pursuant to which expenses per loop decline as carrier size increases, would be taken into account by the formula.[284] Of the models studied, the linear spline was found to have the highest R^2, a measure indicating that this model provides the best fit with the data.[285] The relationship between corporate operations expense and lines served may reasonably be expected to change as carriers' size increases. The linear spline method used allows a different slope to be fitted for smaller carriers than for larger carriers. The Commission adopted the "knot," or the point at which the two line segments of the linear spline model meet, at 10,000 loops because that point allowed the best-fitting overall spline.[286]

98. Regarding the remaining issues raised by Western Alliance, the 115 percent ceiling that limits recovery of corporate operations expenses is consistent with other Commission rules regarding universal service support under Part 36 of our rules.[287] The Commission has consistently considered carriers whose loop costs exceed the national average loop cost by more than 15 percent worthy of special treatment.[288] In the present context, out of an abundance of caution, we have concluded that companies will be allowed to recover costs up to 15 percent above average costs, rather than limiting recovery of such expenses to

[284] *July 10 Order*, 12 FCC Rcd at 10115-18, App. B.

[285] The linear spline model, in this case, is two line segments joined together at a single point or knot. In general, the linear spline model allows the cap on corporate operations expense per line to decline as the number of loops increases for the smaller companies having fewer loops than the knot point. *See July 10 Order*, App. B. Regression analysis is a standard technique that quantifies relationships between input variables. In this case, the input variables are the number of lines a carrier serves and the levels of corporate operations expense per carrier. The R^2, a statistical measure for goodness of fit, for total operating costs using this model is 0.89. This implies that approximately 90% of the variation in total corporate operating costs is explained by the variations in the number of lines served. *See July 10 Order*, 12 FCC Rcd at 10115-18, App. B.

[286] *July 10 Order*, 12 FCC Rcd at 10115-18, App. B.

[287] *See* 47 C.F.R. § 36.631.

[288] Amendment of Part 67 of the Commission's Rules and Establishment of the Joint Board, CC Docket 80-286, *Decision and Order*, 96 FCC 2d 781 at para. 29 (1984) (adopting Joint Board's recommendation and analysis concluding that high cost support should be provided to companies whose costs are in excess of 115 percent of the national average); Amendment of Part 67 of the Commission's Rules and Establishment of the Joint Board, CC Docket 80-286, *Recommended Decision*, 48 Fed. Reg. 46,556, 46,567 (1983) (rejecting levels of both 110 percent and 120 percent, and concluding that the 115 percent level best balances the competing concerns of "insur[ing] universal availability of affordable telephone service and the need to limit the high cost amount to a level which can be recovered through a carrier's carrier access charges without resulting in economic inefficiency or uneconomic bypass.").

average costs.[289] We also find that, before receiving corporate operations expenses in excess of 115 percent of the average, companies should undergo additional scrutiny by submitting a waiver request to the Commission. Finally, the data used in the estimation are the actual corporate operations expenses that companies filed with NECA for the calculation of universal service support. We used the most current NECA data available at the time we performed these calculations.[290]

99. Western Alliance claims that the Commission's corporate operations expense formula affects smaller companies more significantly than larger companies.[291] It states that Figure 1 in the *July 10 Order* demonstrates that the data for LECs with more than 15,000 loops cluster more closely around the Commission's fitted line than the data for those LECs with fewer than 15,000 lines.[292] This observation, however, does not undermine the Commission's conclusion. Because corporate operations expense per line varies more for smaller companies than larger ones, any line that we might adopt would fit the data for larger companies more closely than it would fit the data for smaller ones. Moreover, as explained above, we have raised the minimum cap out of an abundance of caution to address concerns that, without modification, our formula may not afford sufficient recovery of corporate operations expenses for the smallest companies.

100. We reject GVNW's argument that it is not clear whether the corporate operations expense rule addresses amounts from Accounts 6710 and 6720 or whether it addresses "that portion assigned to loop cost in NECA's USF Algorithm (AL19)."[293] According to the *Order*, however, "[c]orporate operations expense are recorded in Account 6710 (Executive and planning) and Account 6720 (General and administrative)."[294] Hence, the limitation applies to accounts 6710 and 6720 and does not apply to NECA's USF

[289] When the Commission calculated the formula, it multiplied estimates of average costs by 1.15 to calculate the actual level of the cap. *July 10 Order*, 12 FCC Rcd at 10115-18, App. B. We note that this recovery is more generous than the Commission's initial proposal to eliminate recovery of all corporate operations expenses. *See infra* section IV.F.3.d.

[290] NECA files data each year on October 1. *See* NECA Universal Service Fund 1997 Submission of 1996 Study Results; 47 C.F.R. § 36.613.

[291] Western Alliance petition to July 10 Order at 8.

[292] *Id.*

[293] GVNW petition at 9.

[294] *See Order*, 12 FCC Rcd at 8930, n.735.

algorithm.[295]

101. RTC asserts that the Commission's formula is a proxy model and therefore should be subject to the criteria the Commission adopted for forward-looking cost proxy models in the *Order*.[296] Although the formula we adopted to limit recovery of corporate operations expenses is a model, it is not a model intended to estimate forward-looking economic costs. Therefore, most of the criteria adopted by the Commission concerning forward-looking cost proxy models are inapplicable to the corporate operations expense formula.[297] Further, RTC is incorrect to the extent that it is arguing that the underlying data and assumptions for the formula are unavailable to the public.[298] The data used to create the line were filed publicly with the Commission by NECA for calendar year 1995. The assumptions and method we used to compute the formula can be found in greatest detail in the *July 10 Order*.[299] The Commission has not, as TCA alleges, contradicted its decision to base universal service support for rural telephone companies on embedded costs until January 1, 2001.[300] The formula we have adopted imposes a limit on the recovery of embedded costs and is not a proxy model designed to calculate forward-looking economic costs.

102. We find that our limitation on recovery of corporate operations expenses will not jeopardize the affordability of local services.[301] Because, as discussed above, such expenditures and the level of such expenditures are in many cases discretionary, we believe that imposing some limits on corporate operations expenses serves the public interest.

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[295] "AL19" refers to line 19 of NECA's cost company loop cost algorithm. The portion of accounts 6710 and 6720 that are assigned to C&WF Category 1 and COE Category 4.13 are used as input values to line 19 of the algorithm. *See* NECA Universal Service Fund 1997 Submission of 1996 Study Results, section 3 at 3.

[296] *See* RTC Petition to July 10 Order at 5; *Order*, 12 FCC Rcd at 8912-16. These criteria, recommended by the Joint Board and adopted by the Commission, have been established to provide a guide in development and selection of proxy models, which are used to explain the behavior of forward-looking economic costs in capital investment. *Recommended Decision*, 12 FCC Rcd at 230-32; *Order*, 12 FCC Rcd at 8899 n. 573. "Forward-looking economic cost" is defined as the cost of producing services using the least cost, most efficient, and reasonable technology currently available for purchase with all inputs valued at current prices. *Id.*

[297] For example, criteria one requires the forward-looking economic cost models to assume the "least-cost, most-efficient, and reasonable technology for providing the supported services." *Order*, 12 FCC Rcd at 8913.

[298] *See* criteria 8 (requiring, *inter alia*, all underlying data, formulae, and computations to be available to interested parties). *Order*, 12 FCC Rcd at 8915.

[299] *July 10 Order*, 12 FCC Rcd at 10102-05; 10115-18, App. B.

[300] *See* TCA reply at 5.

[301] Fidelity petition at 4 (asserting that the limitation will cause increases in local rates).

Moreover, if carriers have prudent corporate operations expenses that exceed the cap, they may seek a waiver of that cap.[302]

103. Based on the changes described above, we modify the formula to limit the amount of corporation operations expenses per working loop that a carrier may recover as follows:

> for study areas with 6,000 or fewer working loops the amount per working loop shall be $31.188 - (.0023 x the number of working loops), or, ($25,000 ÷
> the number of working loops), whichever is greater;
>
> for study areas with more than 6,000 but fewer than 18,006 working loops, the amount per working loop shall be $3.588 + (82,827.60 ÷ the number of working loops); and
>
> for study areas with 18,006 or more working loops, the amount per working loop shall be $8.188.

We conclude that this modified formula will better serve our goal of ensuring that carriers use universal service support only to offer the supported services to their customers through prudent facility investment and maintenance consistent with their obligations under section 254(k).

d. Procedural Matters

104. We conclude that the limitation on corporate operations expenses was adopted in compliance with the Administrative Procedure Act (APA). The Commission gave the public ample notice regarding the possibility of limiting or excluding recovery of corporate operations expenses. In a Notice of Inquiry released in 1994, the Commission sought comment on whether we should exclude all recovery of corporate operations expenses. In a Notice of Proposed Rulemaking released in 1995, as the petitioners acknowledge, the Commission tentatively concluded that it should exclude recovery of all such expenses.[303] In the *Universal Service Notice*, the Commission specifically sought comment on whether any proposals in Docket No. 80-286 were worthy of consideration in Docket No. 96-45 and

[302] *See infra* section IV.F.3.d.

[303] *See* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, *Notice of Inquiry*, 9 FCC Rcd 7404 at 7416-17 (1994) (*1994 NOI*); Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket 80-286, *Notice of Proposed Rulemaking and Notice of Inquiry*, 10 FCC Rcd 12,309, 12,324 (*1995 Notice*).

specifically incorporated the record of that proceeding into the 96-45 docket.[304] Moreover, in its Public Notice seeking further comment, the Common Carrier Bureau asked what modifications should be made to the high cost support mechanism if it were retained with respect to rural areas.[305] In response to this Public Notice, several parties recommended that the Commission limit or exclude recovery of corporate operations expenses as it had previously proposed.[306]

105. Not only did the Commission provide notice of a potential limit on or exclusion of the recovery of corporate operations expenses, the approach adopted by the Commission takes into consideration the comments filed in response to these notices.[307] The Commission initially proposed disallowing all recovery for corporate operations expenses.[308] After considering the comments, however, the Commission concluded in the *Order* that it should limit such expenses to a reasonable level rather than excluding them altogether.[309] The approach taken is conceptually similar to the one NECA proposed in response to the *1995 Notice* and again in response to the Public Notice.[310] NECA proposed that high cost support recipients should recover only expenses that fall below a line that is two standard deviations above a regression line.[311] Our limitation is based on a regression line that takes into account the size of the company when calculating an acceptable range of recoverable corporate

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[304] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Notice of Proposed Rulemaking and Order Establishing Joint Board*, 11 FCC Rcd 18092, 18112 (1996) (*Universal Service Notice*).

[305] Common Carrier Bureau Seeks Further Comment on Specific Questions in Universal Service Notice of Proposed Rulemaking, CC Docket 96-45, *Public Notice*, 11 FCC Rcd 7750, 7754 (Comm. Carr. Bur. 1996) (*Further Comment Public Notice*).

[306] *See, e.g.*, AT&T further comments at 24, att. A (suggesting that recovery of all administrative expenses be excluded), NECA further comments at 19 (stating that, if the Commission is concerned about excessive levels of general and administrative expenses, it may wish to consider using statistical measures, such as the two standard deviation test proposed by NECA in its comments to the *1995 Notice*, to limit the amount of expenses allocated to the USF); NYDPS further comments at 6, n.1.

[307] *Cf.* TCA reply at 4 (asserting that the Commission's decision was based on an insufficient record).

[308] *1995 Notice*, 10 FCC Rcd at 12,324.

[309] *Order*, 12 FCC Rcd at 8931-32.

[310] *See* NECA further comments at 19 (stating that, if the Commission is concerned about excessive levels of general and administrative expenses, it may wish to consider using statistical measures, such as the two standard deviation test proposed by NECA in the 80-286 proceeding).

[311] NECA 1995 Notice comments, App. G1. NECA created three regression lines that regressed, respectively, administrative expenses per USF loop in accounts 6120, 6710, and 6720 against the natural logarithm of number of USF loops. *Id.* at 3.

operations expenses and, rather than allowing all expenses within two standard deviations of the line as proposed by NECA,[312] allows recovery of expenses that are up to 115 percent of the typical costs of companies of similar size. Thus, because the corporate operations expense cap was within the scope of the proposal to eliminate recovery of all corporate operations expenses and was supported by record evidence, the requirements of the APA were met.[313]

106. We conclude that we are not barred from adopting this limitation because, although the Joint Board did not make a recommendation about limiting the recovery of corporate operations expenses,[314] the Commission properly referred to the CC Docket No. 96-45 Joint Board the question of whether proposals originating with the CC Docket No. 80-286 Joint Board should be adopted.[315] We also conclude that Western Alliance incorrectly implies that the legislative history to the 1996 Act prohibits the Commission from adopting any proposal that was submitted in the record of the CC Docket No. 80-286 proceeding.[316] Although the Joint Explanatory Statement explained that Congress did not view the CC Docket No. 80-286 proceeding as an appropriate basis for implementing section 254(a),[317] nothing in the legislative history suggests that Congress, in enacting section 254, intended to preclude us from considering specific proposals from that docket in the separate proceeding undertaken to implement section 254. Indeed, the Commission, in the *Universal Service Notice*, sought comment on whether any proposals from the 80-286 docket were consistent with the 1996 Act so as to avoid duplication of previous Commission efforts.[318] As described above, several commenters proposed elimination or limitation of the recovery of corporate operations expenses in the 96-45 docket, and the Commission adopted this limitation as part of the 96-45 docket.

107. We also conclude that our adoption of a high standard for granting a waiver for

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[312] By adopting a two standard deviation approach, NECA's proposal reduced recovery of corporate operations expenses of approximately 5 percent of companies. NECA 1995 Notice comments, App. G1 at 4.

[313] *See Omnipoint Corp. v. FCC*, 78 F.2d 620, 632 (D.C. Cir. 1996) (citing *United Steelworkers of America, AFL-CIO-CIC v. Marshall*, 647 F.2d 1189 (D.C. Cir. 1981)); *see also, Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 547 (D.C. Cir. 1983).

[314] Western Alliance petition at 9.

[315] *Universal Service Notice*, 11 FCC Rcd at 18,112.

[316] *See* Western Alliance petition to July 10 Order at 5-6.

[317] Joint Explanatory Statement at 131.

[318] *Universal Service Notice*, 11 FCC Rcd at 18112.

corporate operations expense recovery is fully justified.[319] Because corporate operations expenses are in many cases completely within a company's discretion, they are more likely to be susceptible to abuse than other types of expenditures such as plant maintenance expenditures.[320] Accordingly, parties contending that they should recover unusually high amounts of such expenses should be required to meet a substantial burden. Additionally, because the limitation includes a buffer zone to accommodate companies that may have corporate operations expenses that are higher than average, but not extreme, we affirm our conclusion that the need for waivers should be limited to exceptional circumstances.

108. We also reject petitioners' suggestions that the limitation on recovery of corporate operations expenses should be phased in over a lengthy transition period.[321] Unlike other situations cited by the commenters, a transition period is not warranted in this instance. We conclude that we should not phase in a measure designed to prevent misallocation, manipulation, and abuse. Companies believing that they have reasonably incurred expenses in excess of the limitation may petition for a waiver from the Commission. We find that the availability of a waiver will sufficiently protect any company that legitimately incurred expenses in excess of the limitation, whether caused by activity mandated by the 1996 Act or for any other reason.[322]

109. Contrary to the position of some commenters, the Commission is fully authorized to adopt rules to implement section 254(k) in addition to codifying the statutory provision as it has already done.[323] In fact, in the *Section 254(k) Order*, we concluded that we would "from time to time, re-evaluate our rules to determine whether additional rule changes

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[319] *Order*, 12 FCC Rcd at 8932 (stating that the Commission will grant study area waivers only under "exceptional circumstances").

[320] *See supra* section IV.F.3.a and comments cited therein.

[321] *See, e.g.*, Fidelity petition at 3, 5.

[322] *See, e.g.*, Virgin Islands Tel. Co. July 10 reply at 8-9 (stating that corporate operations expenses in the Virgin Islands are higher than in other parts of the United States). We note, however, that staff analysis comparing 1995 data with 1996 data shows that corporate operations expenses for companies with more than 10,000 lines went down in 1996 and that such expenses increased by only 6 percent for companies with fewer than 10,000 lines. *Compare* NECA Universal Service Fund 1997 Submission of 1996 Study Results *with* NECA Universal Service Fund 1996 Submission of 1995 Study Results. *See also* NECA Universal Service Fund 1997 Submission of 1996 Study Results, section 10, nationwide totals (showing percent changes between 1995 and 1996).

[323] 47 U.S.C. § 254(k); Implementation of Section 254(k) of the Communications Act of 1934, as amended, *Order*, 12 FCC Rcd 6415 (May 8, 1997) (*Section 254(k) Order*).

are necessary to meet the requirements of section 254(k)."[324] The Commission concluded in the *Order* and the *July 10 Order* that some recipients of federal universal service support may be receiving funds beyond those necessary to provide the supported services.[325] Recovery of such expenditures may allow carriers to use these expenditures to subsidize competitive services in violation of section 254(k).[326] In addition to limiting support for corporate operations expense in order to control spending that may be in excess of that allowed by the Act,[327] the Commission correctly found that limiting corporate operations expenses would reduce the ability of incumbent LECs to subsidize competitive services with noncompetitive services by reducing the incumbent LECs' receipt of funds beyond those that may be necessary to provide the supported services. We therefore conclude that limiting recovery of corporate operations expenses is within the ambit of section 254(k).

V. SUPPORT FOR LOW-INCOME CONSUMERS

A. Obligation to Provide Toll-Limitation Services

1. Background

110. The Commission has defined toll-limitation services as toll blocking, which allows customers to block outgoing toll calls, and toll control, which allows customers to limit in advance their toll usage per month or billing cycle.[328] Toll-limitation services for qualifying low-income consumers are among the "core" or "designated" services that carriers must provide in order to be deemed "eligible telecommunications carriers."[329] In addition, once they are designated as eligible, all eligible telecommunications carriers must offer Lifeline and LinkUp services.[330] In the *Order*, the Commission agreed with the Joint Board's

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[324] *Section 254(k) Order*, 12 FCC Rcd at 6415.

[325] *Order*, 12 FCC Rcd at 8930-32; *July 10 Order*, 12 FCC Rcd at 10102-05.

[326] Section 254(k) states, in part: "A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition." 47 U.S.C. § 254(k).

[327] *See* 47 U.S.C. § 254(e) (requiring carriers that receive universal service support to "use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended").

[328] *Order*, 12 FCC Rcd at 8978-8979. *See also* 47 C.F.R. § 54.400(2).

[329] *Order*, 12 FCC Rcd at 8809.

[330] *See* 47 C.F.R. § 54.405.

recommendation[331] that Lifeline customers should receive toll-limitation services at no charge, in addition to the other services that will be supported by federal universal service support mechanisms for rural, insular, and high cost areas.[332] In reaching this conclusion, the Commission found that, by limiting in advance customers' toll usage per month or billing cycle, toll-limitation services assist customers in avoiding involuntary termination of local telecommunications services for non-payment of long-distance charges.[333] The Commission authorized state commissions to grant carriers that are technically incapable of providing toll-limitation services a transitional period during which they may receive universal service support for serving Lifeline consumers while upgrading their switches to provide these services.[334]

2. Pleadings

111. Several petitioners seek clarification of certain Commission rules requiring carriers to offer toll-limitation services to all qualifying low-income consumers. Our rules define toll limitation as "toll blocking and toll control."[335] These parties object to having to offer both toll blocking and toll control, and argue that offering either one of these services should be sufficient to qualify for universal service support.[336] RTC asserts that LECs generally do not have the "capability to determine, in real time, the accumulated toll billings of any subscriber" because, unlike IXCs, LECs cannot monitor toll usage as customers place toll calls.[337] Others parties contend that providing toll control, even if technically possible, would be difficult and expensive, and would not yield measurable benefits because parties could circumvent toll control protections simply by dialing around or using pre-paid calling cards.[338] Catholic Conference, in its opposition to USTA's and RTC's petitions, asserts that

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[331] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Recommended Decision*, 12 FCC Rcd 87, 285 (1996).

[332] *Order*, 12 FCC Rcd at 8980.

[333] *Order*, 12 FCC Rcd at 8980.

[334] *Order*, 12 FCC Rcd at 8982.

[335] USTA petition and Ameritech opposition *citing* 47 C.F.R. §§ 54.400(4) and 54.401(a)(3).

[336] *See* USTA petition at 4-6; Ameritech opposition at 4-6; AT&T opposition at 24; Bell Atlantic opposition at 11-12; BellSouth opposition at 10; and GTE opposition at 15.

[337] RTC petition at 24. *See also* AT&T opposition at 24-25.

[338] *See* USTA petition at 5-6; Ameritech opposition at 5-6; AT&T opposition at 24-25; GTE opposition at 16.

Lifeline consumers should have the choice of either toll blocking or toll control.[339]

112. The Florida Commission asks the Commission to clarify whether carriers offering Lifeline must offer Lifeline consumers toll-control services other than those identified in the *Order*.[340] The Florida Commission asks whether international toll-call-blocking and toll blocking that allows callers with a Personal Identification Number (PIN) to make toll calls, for example, must be provided free of charge to Lifeline consumers.[341] The Florida Commission points out that such toll-control services are not characterized by a pre-set spending limit, unlike the toll-blocking and toll-limitation services defined in the *Order*.[342] The Florida Commission seeks further clarification regarding whether toll control must limit incoming collect calls, noting that the Commission's rules require that toll blocking only block outgoing calls.[343] Finally, the Texas Commission requests clarification as to whether a carrier must provide Lifeline services in order to be designated an eligible telecommunications carrier.[344]

113. In response to the Florida Commission's petition, USTA asks the Commission to reject any suggestion that international toll-call-blocking and toll blocking that allows callers with a Personal Identification Number (PIN) to make toll calls must be provided free-of-charge to Lifeline consumers.[345] According to USTA, most LECs offer only toll blocking services that block calls beginning with 1+, 0+, 0, and 10XXX. Thus, USTA does not support any requirement to provide toll-limitation services other than those that block calls beginning with these numerical codes. USTA further rejects the suggestion that international

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[339] Catholic Conference opposition at 4-5.

[340] Florida Commission Oct. 9 petition at 5-6. On Oct. 9, 1997, Florida Commission filed a Petition for Declaratory Statement, Waiver, and Clarification and Request for Expedited Ruling. That portion of Florida Commission's petition that is styled as a petition for clarification was not timely filed within the period for filing petitions for reconsideration or clarification of the *Order*. *See* 47 U.S.C. § 405(a). *See also Virgin Islands Telephone Corp. v. FCC*, 989 F.2d 1231, 1237 (D.C. Cir. 1993); *Reuters Ltd. v. FCC*, 781 F.2d 946, 951-52 (D.C. Cir. 1986). Therefore, we consider that portion of its petition as informal comments.

[341] Florida Commission Oct. 9 petition at 5-6.

[342] The Commission defined "toll blocking" as a service that allows customers to block toll calls and "toll control" as a service that allows customers to limit in advance their toll usage per month or billing cycle. *Order*, 12 FCC Rcd at 8978-8979.

[343] Florida Commission Oct. 9 petition at 6.

[344] Texas Commission petition at 9-10.

[345] Letter from USTA to William F. Caton, FCC, dated November 5, 1997 (USTA November 5 ex parte) at 2.

toll-call-blocking should be provided free-of-charge on grounds that most LECs, in providing toll-blocking service, are not able to differentiate between interstate, intrastate, or international calls.

3. Discussion

114. We believe that low-income consumers eventually should have the choice of selecting either toll blocking or toll control to restrict their toll usage. We conclude, however, that giving consumers such an option is not viable at this time. Based on the record before us, we find that an overwhelming number of carriers are technically incapable of providing both toll-limitation services, particularly toll-control services, at this time.[346] Under our current rules, carriers technically incapable of providing both types of toll-limitation services must seek from their state commissions a time-limited waiver of their obligation to provide both toll blocking and toll control.[347] Given that a large number of carriers are technically incapable of providing both toll blocking and toll control at this time, we believe that requiring carriers to provide both would result in an unnecessarily burdensome process for state commissions required to act on a large number of waiver proceedings.[348]

115. In light of these concerns, we believe that requiring carriers to provide at least one type of toll-limitation service is sufficient to provide low-income consumers a means by which to control their toll usage and thereby maintain their ability to stay connected to the public switched telephone network. Weighing the burdens on the states and the need to have carriers designated in a short time frame against the goal of giving low-income consumers a full range of options for controlling toll usage, we define toll-limitation services as either toll blocking or toll control and require telecommunications carriers to offer only one, and not necessarily both, of those services at this time in order to be designated as eligible telecommunications carriers. We note, however, that if, for technical reasons, a carrier cannot provide any toll-limitation service at this time, the carrier must seek a time-limited waiver of this requirement to be designated as eligible for support during the period it takes to make the network changes needed to provide one of those toll-limitation services. In addition, if a carrier is capable of providing both toll blocking and toll control, it must offer qualifying low-income consumers a choice between toll blocking and toll control. Because we agree with Catholic Conference that all qualifying low income consumers ideally should be offered their choice of toll blocking or toll control, we plan to monitor and revisit this issue if we

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[346] *See* RTC petition at 24; USTA petition at 5-6; Ameritech opposition at 5-6; AT&T opposition at 24-25; GTE opposition at 16.

[347] 47 C.F.R. § 54.101(c).

[348] Because state commissions are to designate eligible telecommunications carriers by January 1, 1998, these waiver proceedings would need to be completed prior to or on that date.

determine that technological impediments to carriers' ability to offer toll limitation have been reduced or eliminated. We also encourage carriers to develop and investigate cost-effective ways to provide toll-control services.

116. We further conclude that carriers offering Lifeline service will not be required to provide toll-limitation services other than those specifically identified in the *Order*. The Commission defined toll blocking as a service that allows customers to block outgoing toll calls, and defined toll control as a service that allows customers to limit in advance their toll usage per month or billing cycle.[349] Therefore, carriers offering Lifeline service will not be required to offer, for example, international toll-call-blocking or toll blocking that allows callers with a Personal Identification Number (PIN) to make toll calls, as suggested by the Florida Commission. While we encourage carriers to offer Lifeline consumers, free of charge, toll-limitation services that include functions and capabilities beyond those described in the *Order*, we are persuaded by USTA that most carriers currently are technically incapable of providing these additional services. Furthermore, regarding the issue of whether toll control must limit collect calls, we conclude that, like toll blocking, toll control only must allow consumers to limit outgoing calls.

117. In response to the Texas Commission's request, we reiterate that toll-limitation services for qualifying low-income subscribers are included in the definition of the "core" or "designated" services that will receive universal service support. A carrier must provide these core services throughout its entire service area in order to be designated an eligible telecommunications carrier.[350] We further clarify that, compliance with the no disconnect rule[351] and the prohibition on deposit rule[352] are not specific preconditions to being designated an eligible telecommunications carrier. Once designated as an eligible telecommunications carrier, however, that carrier must offer all Lifeline and LinkUp services to qualifying low-income subscribers.[353]

B. Recovery of PICC

1. Background

[349] *Order*, 12 FCC Rcd at 8978-8979. *See also* 47 C.F.R. § 54.400(2).

[350] *See Order*, 12 FCC Rcd at 8821-8822.

[351] The no disconnect rule prohibits carriers from disconnecting customers who participate in the Lifeline program for nonpayment of toll charges. *See Order*, 12 FCC Rcd at 8983-8988.

[352] The prohibition on deposit rule provides that qualifying low-income consumers who elect toll blocking may not be required to pay service deposits. *See Order*, 12 FCC Rcd at 8988-8990.

[353] *See* 47 C.F.R. §§ 54.405, and 54.411.

118. On May 7, 1997, the Commission adopted the *Access Charge Reform Order* that, among other things, created a new flat per-line charge assessed upon an end user's presubscribed interexchange carrier (IXC).[354] This flat, presubscribed interexchange carrier charge (PICC) will enable incumbent local exchange carriers to recover non-traffic sensitive common line costs not recovered through subscriber line charges (SLCs).[355] The PICC for primary residential lines will be capped at $0.53 per month for the first year, beginning January 1, 1998.[356] Beginning January 1, 1999, the ceiling on the monthly PICC on primary residential lines will be adjusted for inflation and will increase by $0.50 per year until the sum of the SLC plus the flat-rated PICC is equal to the price cap LEC's permitted common line revenues per line.[357] The sum of the single-line SLC and the PICC shall never exceed the sum of the maximum allowable multi-line SLC and multi-line PICC.[358] The Commission stated that incumbent LECs may collect directly from any customer who does not presubscribe to long distance service from an IXC the PICC that would otherwise be assessed against the presubscribed IXC at the beginning of each billing cycle.[359] The Commission instituted this policy to eliminate the incentive for customers to access long-distance services solely through "dial-around" carriers in order to avoid paying long-distance rates that reflect the PICC.[360]

119. Customers who elect toll blocking do not have a presubscribed IXC and, pursuant to our access rules, may be required to pay the $0.53 PICC directly to incumbent LECs.[361] On September 4, 1997, the Commission released a *Second Further Notice of Proposed Rulemaking* that proposed to waive the PICC charge for Lifeline customers who elect toll blocking and thus do not presubscribe to an IXC.[362] The Commission tentatively

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[354] *Access Charge Reform Order* at paras. 91-105.

[355] *Access Charge Reform Order* at para. 91.

[356] *Access Charge Reform Order* at para. 94.

[357] *Access Charge Reform Order* at para. 94.

[358] *Access Charge Reform Order* at para. 94.

[359] *Access Charge Reform Order* at para. 92.

[360] *Access Charge Reform Order* at paras. 92-93.

[361] *Access Charge Reform Order* at para. 92.

[362] Federal-State Joint Board on Universal Service, Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge, CC Docket Nos. 96-45, 96-262, 94-1, 91-213, 95-72, *Second Further Notice of Proposed Rulemaking* (rel. Sept. 4, 1997)

concluded that the costs of the PICC in such cases should be recovered from the low-income program of the new federal universal service support mechanisms and sought comment on this tentative conclusion.[363]

2. Pleadings

120. Several petitioners and commenters support the Commission's tentative conclusion to waive the PICC for Lifeline consumers who elect toll blocking, and to recover the waived PICCs from the low-income program of the federal universal service support mechanisms.[364] These parties generally take the position that toll blocking enables consumers to control their toll usage and that requiring Lifeline consumers to pay the PICC would undermine the Commission's intent to make toll blocking available free-of-charge. SBC argues that support for PICCs of low-income consumers who elect toll blocking should be provided in addition to the maximum $7.00 per Lifeline customer benefit established in the *Order*.[365] Sprint supports the Commission's proposal to waive the PICC for Lifeline customers, but asserts that the waived charges should be supported by the low-income program on a conditional basis for at least one year.[366] Sprint argues that, because it is difficult to predict the competitive effects of requiring competitors of incumbent LECs to contribute to the support of incumbent LECs, the Commission should monitor waived PICCs until it can be more "confident that the benefits of such increased burden outweigh the costs."[367] AT&T suggests that, to ensure competitive neutrality, the Commission should clarify that eligible competitive carriers that provide Lifeline service, as well as eligible incumbent LECs, may recover the waived PICC for consumers who elect toll blocking from the federal low-income program.[368] SBC opposes this proposal and contends that, because only price cap LECs are permitted to recover PICCs directly from end users who do not have presubscribed IXCs and are subject to regulation regarding the recovery of separated common line costs, only price cap LECs should be permitted to recover waived PICCs from the

(*Second Further Notice*) at para. 5.

[363] *Second Further Notice* at para. 5.

[364] *See* Catholic Conference petition at 4-6; AT&T opposition at 25; BellSouth opposition at 10; Bell Atlantic comments to *Second Further Notice* at 1-2; MCI comments to *Second Further Notice* at 1-2; RTC comments to *Second Further Notice* at 3-4; SBC comments to *Second Further Notice* at 3; USTA comments to *Second Further Notice* at 2; US WEST comments to *Second Further Notice* at 2-3.

[365] SBC comments to *Second Further Notice* at 3-4.

[366] Sprint comments to *Second Further Notice* at 1-2.

[367] Sprint comments to *Second Further Notice* at 1-2.

[368] AT&T comments to *Second Further Notice* at 6.

support mechanisms.[369] In the alternative, SBC proposes that the Commission limit support to eligible carriers that normally impose a charge on a presubscribed IXC and that collect such charges from end-user customers when those customers have toll blocking.[370] SBC further proposes to set support amounts as the lesser of such charge or the then-current PICC cap.[371]

121. AT&T argues that the federal low-income program should support all PICCs for low-income consumers who elect toll blocking, even if the consumers presubscribe to an IXC.[372] AT&T asserts that in rare instances a low-income consumer who has selected a presubscribed IXC and subsequently elects toll blocking may nevertheless continue to have a presubscribed IXC.[373] AT&T contends that, because the IXC will not receive revenue from a customer who elects toll blocking, the IXC should not be required to pay the PICC for that customer.[374] Instead, AT&T argues that the PICC for such a customer should be recovered from the federal low-income program.[375] Bell Atlantic counters that such action is not necessary to eliminate the financial barriers to a Lifeline consumer's selection of toll blocking, and, therefore, the IXC should remain responsible for those PICCs.[376] SBC contends that support should be provided to Lifeline customers who are placed on toll blocking as a result of failure to pay toll charges. SBC argues that requiring such Lifeline customers to pay the PICC would contradict the Commission's stated intention of ensuring that toll blocking be provided free-of-charge.[377] In addition, although the Florida Commission supports the Commission's tentative conclusion to waive the PICC for low-income consumers who elect toll blocking, it suggests that LECs recover all waived PICCs directly from IXCs.[378] The Florida Commission contends that the PICC is primarily intended to recover non-traffic sensitive (NTS) costs that currently are recovered from IXCs through the usage-sensitive

[369] SBC comments to *Second Further Notice* at 5.

[370] SBC comments to *Second Further Notice* at 5-6.

[371] SBC comments to *Second Further Notice* at 5-6.

[372] AT&T comments to *Second Further Notice* at 5-6.

[373] AT&T comments to *Second Further Notice* at 5-6.

[374] AT&T comments to *Second Further Notice* at 5-6.

[375] AT&T comments to *Second Further Notice* at 5-6.

[376] Bell Atlantic comments to *Second Further Notice* at 1.

[377] SBC comments to *Second Further Notice* at 8.

[378] Florida Commission comments to *Second Further Notice* at 2-3.