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January 26, 1998

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Secretary
Federal Communications Commission
1919 M Street, Room 222
Washington, D.C. 20554

In the Matter of)
)
Federal-State Joint Board on)
Universal Service) **CC Docket No. 96-45**
) **(Report to Congress)**

Attention: Universal Service Branch

Enclosed is an original and four copies of comments prepared by John Staurulakis, Inc. (JSI) in response to the Public Notice, DA 98-2 (January 5, 1998), and the Order DA 98-63, released on January 14, 1998, in the above-referenced docket.

As provided in the January 5, 1998 Public Notice, we are also providing a diskette containing our comments to Ms. Todd.

Any questions concerning this filing may be directed to JSI.

Sincerely,


Bruce Schoonover, Sr.
Executive Vice President

Enclosures

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cc: Ms. Sheryl Todd, F.C.C. Universal Service Branch, 8th Floor, 2100 M Street, NW
International Transcription Service, 1231 20th Street, NW, Washington, D.C. 20036

Before the
FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of)
Federal-State Joint Board on Universal Service)

CC Docket No. 96-45
(Report to Congress)

**Comments of John Staurulakis, Inc.
In response to the January 5, 1998, Public Notice, DA-98-2,
related to the request of the Common Carrier Bureau
seeking comments for a report to Congress on
Universal Service under the Telecommunications Act of 1996**

John Staurulakis, Inc.

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Executive Vice President

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January 26, 1998

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Summary

JSI believes that the current bifurcated high-cost universal service support administrative rules; i.e., the 25 percent federal-75 percent intrastate responsibility, and the use of interstate and international revenues, without the benefit of intrastate revenues, as the basis for the contribution assessment, cannot be reconciled either with the provisions of the Act or with the FCC's own record.

The FCC's current administrative rules for bifurcated, high-cost, universal service support would result in the administrative burden of 50 state high-cost funds, and would discriminate against high-cost, less densely populated states: e.g., North Dakota could require a 35 percent surcharge on retail customer bills, while California would need only a 2 percent surcharge.

If the FCC were to establish a comprehensive system for universal service support and administration, the required surcharge could be uniform and nationwide, i.e., an overall 4 percent surcharge, nationwide, rather than a program that sees a 35 percent surcharge in a high-cost state but only 2 percent in a low-cost state. .

JSI believes the FCC should revise its universal service support program to:

- Include all retail telecommunications revenues – interstate, international, and intrastate – in the assessment base;
- Beginning January 1, 1999, for those LECs eligible to receive high-cost universal service support funding on the basis of forward-looking economic cost, authorize the USAC to collect, administer, audit, and distribute all universal service funding, based on a formula that determines the cost of supported services less the nationwide revenue benchmark, without regard to jurisdiction;

- Allow the majority of the financial benefit of universal service support to be used by states to ensure that intrastate services supported by the federal program are maintained at a reasonably comparable rate level, nationwide; and.
- Rely on state regulatory authorities to see that funds received from the federal program are used to promote and advance universal service.

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of)
Federal-State Joint Board on Universal Service)

CC Docket No. 96-45
(Report to Congress)

Comments of John Staurulakis, Inc.

John Staurulakis, Inc. (JSI) hereby files these comments in response to the January 5, 1998, Public Notice, DA-98-2, related to the request of the Common Carrier Bureau (Bureau) seeking comments for a report to Congress on Universal Service under the Telecommunications Act of 1996.

JSI is a consulting firm specializing in financial and regulatory services to more than two hundred Incumbent Local Exchange Carriers (ILECs) throughout the United States. JSI assists these ILECs in the preparation and submission of jurisdictional cost studies and Universal Service Fund (USF) data to the National Exchange Carrier Association (NECA), and routinely prepares and files tariffs with the Commission on behalf of a number of these ILECs. In that the Public Notice is seeking comments on issues affecting our clients in matters of cost recovery and assessments related to the universal service programs initiated by the Federal Communications Commission (Commission), JSI is an interested party in this proceeding.

In its December 5, 1998, Public Notice, the Bureau confirmed the Commission's intent to submit its report to Congress that "... provide a detailed description of the extent to which the Commission's interpretations in the following areas are consistent with the plain language of the Communications Act of 1934, 47 U.S.C. 151 et seq. (Act), as amended by the 1996 Act:

(1) the definitions of "information service," "local exchange carrier," "telecommunications," "telecommunications service," "telecommunications carrier," and "telephone exchange service" in section 3 of the Act, and the impact of the interpretation of those definitions on the provision of universal service to consumers in all areas of the Nation;

(2) the application of those definitions to mixed or hybrid services and the impact of such application on universal service, and the consistency of the Commission's application of those definitions, including with respect to Internet access for educational providers, libraries, and rural health care providers under section 254(h) of the Act;

(3) who is required to contribute to universal service under section 254(d) of the Act and related existing Federal universal service support mechanisms, and of any exemption of providers or exclusion of any service that includes telecommunications from such requirement or support mechanisms;

(4) who is eligible under sections 254(e), 254(h)(1), and 254(h)(2) of the Act to receive specific Federal universal service support for the provision of universal service, and the consistency with which the Commission has interpreted each of those provisions of section 254; and

(5) the Commission's decisions regarding the percentage of universal service support provided by Federal mechanisms and the revenue base from which such support is derived.”

JSI believes that the Commission’s interpretations, as embodied in its promulgated rules, are generally consistent with the plain language of the Communication Act of 1934, 47 USC 151, et seq. (Act) as amended by the 1996 (Act), for each of the first four areas for which the Bureau seeks comment. In addition, JSI fully endorses and supports the FCC’s unique treatment of rural telephone companies, for the foreseeable future, within the framework of its universal service support system.

With regard to the fifth area, however, JSI does not believe that the Commission's decisions regarding the percentage of universal service support provided by federal mechanisms and the revenue base from which such support is derived are at all in keeping with Congressional intent, and if implemented will, in fact, undermine the universal service principles specifically set forth by Congress to guide the Joint Board and the FCC in setting policies to preserve and advance universal service.”¹

¹ See Section 254(b) of the Telecommunications Act of 1996.

JSI contends that a plain reading of the Act, as well as the Commission's own experience, dictates that the federal high-cost universal service support mechanism should represent a comprehensive solution to universal service in high-cost-to-serve areas nationwide, should not be dependent for its success on the independent actions of fifty separate state regulatory bodies, and should ensure that the vast majority of the support mechanism's financial benefit be available in the intrastate jurisdictions to allow "...consumers in all regions of the Nation... [to] have access to telecommunications services and information services, including interexchange and advanced telecommunications services and information services, that are reasonable comparable to those provided in urban areas and that are available at rates that are reasonably comparable to rates charges for similar services in urban areas."²

**The FCC's Program of Federal, High Cost, Universal Service Support
Cannot Be Reconciled With the Intent of the Act**

In Section 254 of the Telecommunications Act of 1996, Congress set forth, among other things, the universal service principles it intended for the Joint Board and the FCC to follow in setting policy. Section 254(b) established universal service principles, among which include the following:

- Quality services should be available at just, reasonable, and affordable rates;
- Access to advanced telecommunications and information services should be provided in all regions of the nation;
- Consumers in all regions of the nation, including low-income consumers and those in rural, insular, and high-cost areas, should have access to telecommunications and information services, including interexchange and advanced services, that are reasonably comparable to those services provided in urban areas and that are available at rates reasonably comparable to rates charged for similar services in urban areas; and,

² See Section 254(b)(3) of the Act.

- There should be specific, predictable and sufficient federal and state mechanisms to preserve and advance universal service.

In its May 7, 1997 *Report and Order* on Universal Service, the FCC prescribed that the level of federal high-cost universal service support for non-rural LECs would be the result of the forward-looking economic cost of the supported services less a benchmark amount based on the nationwide average revenue per line, and multiplied by 25 percent.³ Further, as opposed to the schools and libraries and rural health care support mechanisms, the FCC decided that contributions required to support the high-cost universal service support mechanism would consist only of interstate and international retail revenues.

In implementing the Act's universal service provisions, JSI believes that in at least three respects, the FCC – unwittingly or not – violated the intent of Congress embodied in the universal service principles: First, by setting the federal share of financial support for the high-cost universal service support mechanism at 25 percent, the FCC undermined Congressional intent to create a “national” universal service program that affords “reasonably comparable” services and rates to all consumers, regardless of where they may live. Such an approach that would place 75 percent of the burden on individual states in effect creates 50 universal service programs. Moreover, it forces high-cost, low-density states, such as North Dakota and Montana which each have substantially less than a million access lines and virtually no urban centers, to account for the lion's share of universal service support for their rural citizens in exactly the same manner as low-cost, high-density states, such as New York and California which can spread these costs over millions of access lines and numerous metropolitan areas.

³ While we note that the FCC's 25 percent interstate 75 percent state-universal service support formula will not be applicable to rural telephone companies sooner than January 1, 2001, the precedent established for non-rural telephone companies beginning January 1, 1999 will ultimately affect rural companies. See May 7, 1997, *Report and Order*, on the Federal-State Joint Board on Universal Service, in CC Docket 96-45, (at para. 203-204).

JSI suggests that the FCC's decision to make the states responsible for 75 percent of "federal" universal service support is contrary to the provisions of Section 254(b) and serves to the distinct disadvantage of small and rural states that do not have the luxury of significant urban population bases on which to offset the costs of providing local service to high-cost rural customers. The 25-75 split represents a major departure from Congressional intent to create national policy and, rather than building on the federal-state partnership in promoting universal service, such a bifurcated approach actually represents a major point of contention between the states and the federal government.⁴

Second, in concert with its decision to fund only 25 percent of the cost of universal service, the FCC concluded that the funding derived through this new interstate support mechanism would not be available for use by states so that they could offset the need for high local rates. Clearly, this is wholly inconsistent with long-standing FCC policy, initiated in 1983.⁵

JSI notes that if the 25 percent interstate funding rule becomes effective on January 1, 1999, as proposed, it will result in the elimination of the availability of the portion of the approximately \$826 million, the 1998 level of USF, applicable to non-rural companies, and used by them to keep intrastate rates lower than they otherwise would be. In other words, states will not only be saddled with 75 percent of the costs of universal service, but they also will be confronted with the realization that historically available federal support will be eliminated for non-rural companies on January 1, 1999.⁶

⁴ In the Senate Commerce Committee's March 12, 1997 oversight hearings, FCC Chairman Reed Hundt noted that he had reversed his position on this issue because several states had complained that they had already established their own universal service programs and did not want to participate in a federal program. Sen. Byron Dorgan (D-ND) replied that he was not concerned with those states because universal service is a national policy, not a state-by-state policy. (see NTCA *Washington Report*, March 17, 1997).

⁵ As far back as 1984, both the FCC and the Joint Board signaled their recognition of the need for summary solutions to the need for adequate and specific support assistance for telephone companies serving high-cost areas. In the November 15, 1984 *Recommended Decision and Order* in CC Docket No. 80-286, the Joint Board noted that it had recommended and the FCC had adopted a high-cost assistance plan that "involves an additional interstate cost allocation for study areas with high (non-traffic-sensitive) local exchange costs. This is designed to reduce the intrastate cost allocation and keep local rates lower than they would otherwise be." emphasis added (see para. 48.)
⁶ *Report and Order*, see para. 268.

Third, and in opposition to the majority of state members of the Joint Board (as discussed later in these comments), the FCC proposed that high-cost universal service support be based on contributions from interstate and international retail revenues – and excluding intrastate – revenues. Thus, we contend, the Commission has decided on a formula that significantly understates the potential revenue base and undermines the “national” perspective for universal service, as articulated by Congress in Section 254(b).

Finally, JSI believes. FCC Commissioner Rachel Chong herself well illustrated the inherent conflict between the FCC’s Order and Congressional intent. In a separate, part-concurring and part-dissenting statement, Commissioner Chong stated:

“While I support our decision to decline to exercise the entirety of our authority as to some portions of the federal universal service program, I read the statute as standing for the proposition that Congress granted the Commission authority pursuant to Section 254 to set up a comprehensive federal universal service program As a result, I think it would be a better reading of Section 254 to allow the Commission to assess universal service contributions on the revenues (either interstate or intrastate) of interstate carriers, because it most accurately embraces the spirit of the national social programs (schools and libraries, rural health care, low income, rural, insular, high cost proposed or mandated in this section.” (emphasis added)

Options to Bifurcated Program

In response to the failure of the FCC's bifurcated approach to satisfy the specific goals of the Act, others in the industry have proposed diverse solutions. One such approach was produced by an Ad Hoc Staff Group of NARUC. During the NARUC Annual Convention in November 1997, an alternate distribution proposal for high-cost support was presented by Chairman Thomas Welch and Mr. Joel Shifman of the Maine Public Utilities Commission.⁷

In the proposal, Chairman Welch correctly demonstrates the inconsistencies in the bifurcated FCC proposal. The evidence presented in the proposal resulted from the use of a "blended" forward-looking cost model to investigate the state-by-state problems inherent in a 25-75 federal-state support mechanism. The primary difficulty is that under the bifurcated FCC program, there will be "high cost states that will be unable to internally generate the support necessary to maintain rates in high cost areas that are reasonably comparable to rates in urban areas."⁸ In fact, the requirements across states are dramatic. While California would have a state-based surcharge of 2 percent, North Dakota would need a state-based surcharge of 35 percent.⁹ This is in comparison to the 3 percent interstate surcharge proposed for interstate telecommunication revenues. The evidence presented is compelling: The bifurcated FCC approach will not achieve the goals defined by Congress regarding a national universal service policy.

⁷ See *High Cost Support: An Alternative Distribution Proposal*, the Ad Hoc Staff Group, for an *Ex Parte* Meeting, CC Docket No. 96-45, Federal-State Joint Board on Universal Service, November 18, 1997.

⁸ See *High Cost Support: An Alternative Distribution Proposal*, p. 9.

⁹ The Welch/NARUC analysis is based on compiling the results of the current BCPM and Hatfield models into a "blended or averaged" result. It is clear that the current models continue to be flawed and, therefore, produce erroneous results. JSI acknowledges these failings and, in fact, recognizes that the FCC has not yet determined if a FLEC-based high-cost universal service fund is appropriate for rural telephone companies. Nevertheless, regardless of the level of the funding, the Welch/NARUC analysis illustrates the relative magnitude of the differences that can be expected among states using a bifurcated universal service program as currently proposed by the FCC.

Chairman Welch presents an alternative program that tries to correct the problems associated with the bifurcated FCC proposal and reclaim the letter and spirit of Section 254 of the Act. Unfortunately, this approach continues to rely on the 25-75 ratio proposed by the FCC. As a result, while the alternative proposal may alleviate some of the pain inflicted by the political wounds suffered during the federal-state jurisdictional challenges, JSI believes that the Welch/NARUC proposal cannot achieve the goals intended by Congress.

Specifically, the alternative proposal departs from existing national administrative efficiencies under the current universal service fund and proposes the creation of universal service collection agencies in all states and territories. JSI believes that the national universal service goals would be best served by a national administration which would realize operational efficiencies that no one state could capture. Since the goal of social policy is to maximize the value of the program, it follows that administrative costs should be reduced to the greatest extent possible.

Moreover, the alternative approach fails to ensure that the “reasonably comparable” provisions of Section 254(b)(3) will be satisfied. Congress envisioned a trans-state program that ensures that all customers in the nation have reasonably comparable services at reasonably comparable rates. State regulatory authorities do not have oversight of rates in other states. Hence, a state cannot achieve reasonably comparable rates without either the cooperation of the other 49 states or a federal administrator. Without comprehensive federal administration, JSI believes, what former Chairman Hundt described as the balkanization of the universal service program will occur across the nation.¹⁰

¹⁰ In addition to the two flaws discussed here, JSI disagrees with the Welch proposal in many of its details. For instance, we do not agree to the primary principle of “fund minimization” adopted by the Welch/NARUC proposal. Congress clearly intended to establish a social policy goal of comparable and reasonable rates. To reach this goal, the new social policy may require additional funds. To this extent, the Welch/NARUC program restricts efforts for these new social policy goals established by Congress.

JSI Recommendations For a Federal Program, Consistent With the Act

JSI claims that it is in the national public interest to develop a federal program for universal service that will be able to achieve the objectives in Section 254 of the Act. Moreover, a Federal program based upon all telecommunication revenues would broaden the assessment base, thereby reducing obvious funding irregularities across states, and further the goal of competitive neutrality irrespective of jurisdictional traffic. JSI encourages the Commission to reconsider and revise its universal service policy to incorporate the following components, thereby creating a federal program consistent with the goals specified in the Act:

1. Establish a federal fund that is based upon total national telecommunications revenues – interstate, international, and intrastate.
2. Beginning January 1, 1999, for those LECs eligible to receive high-cost universal service support funding on the basis of forward-looking economic cost, authorize the Universal Service Administrative Company (USAC) to collect, administer, audit, and distribute all funds based on a formula that determines the cost of supported services less the nationwide benchmark revenue, without regard to jurisdiction.
3. Provide that the majority of revenues received by eligible telecommunication carriers be available to the states to ensure that intrastate services – e. g., basic local exchange service and intrastate access – are maintained at a reasonably comparable rate level, nationwide.
4. Rely on the state regulatory authorities to see that funds received from the federal program are used to promote and advance universal service.

By adopting these four principles, the Commission would establish a federal universal service program that is not only consistent with the goals of the Act, but would be consistent with the federal concept of administration that has successfully worked since 1984. Further, the existing universal service program administration has demonstrated that a federal organization can complement and enhance the goals that state regulators have established for the carriers under their jurisdiction.

It seems apparent that there would be considerable efficiencies in administration in having one organization administer the national universal service policy. If states wish to augment the federal program to further their specific policy objectives, the additional state administration would be minimal as compared to the state administration as proposed currently by the FCC. Also, the national administration of the program would allow state regulatory authorities to use their resources to focus on policy issues rather than collection, administration, auditing, and distribution.

Consistent with the Act, the federal program would allow eligible carriers to apply a majority of the funds received from the program to intrastate activities. This would ensure that the Commission satisfies the program goal, as intended by Congress, to provide for comparable services at comparable rates across the Nation.

Finally, using the total base of telecommunications revenues to support universal service is totally consistent with the goals of a national social policy. As has been mentioned, a balkanized approach would result in some states having a surcharge of more than 30 percent, while other states would see a 2 percent surcharge. Using the "blended" total fund amount presented by Chairman Welch, the federal program proposed herein would result in a total surcharge of just over 4 percent. (This percentage is compared with the 3 percent surcharge on

interstate revenues only under the current FCC proposal and with “blended” total fund amounts required for price-cap carriers.)

It is only logical that low-cost states would want to be removed from the federal program because they would be able to pool their vast resources and large populations to achieve state-specific goals with a surcharge lower than the national total base surcharge. However, allowing low-cost states this opportunity does not promote national policy, and it certainly does not comport with the goals and intentions of Congress as specified in the Act, and in comments reported in the following section. Opting out of a federal program for universal service is loosely similar to allowing all healthy persons to choose a low-cost health insurance plan. This may be an improvement for these persons, but it certainly does not benefit those in poor health – in fact, those in poor health would be required to pay higher insurance premiums. JSI claims that a federal program is the most cost-effective and efficient way to accomplish the goals of universal service.

JSI urges the Commission to reconsider its proposal, and revise it such that it is consistent and compatible with the goals and objectives specified in the Act.

**Further Evidence for a Federal Program:
The FCC Proposal Cannot Be Reconciled With the Existing Record**

As part of the universal service mandate it established in the Telecommunications Act of 1996 (Act), Congress went well beyond previous “social” policy commitments to guarantee “reasonable and affordable” communications to all Americans. Unlike its treatment of the Act’s predecessor, the 1934 Communications Act, Congress put real teeth into the law’s provisions and requirements regarding the federal commitment to national support mechanisms designed to make “comparable” services available at “just, reasonable, and affordable rates” in “all regions of the nation.” In addition to this well-articulated commitment to preserve and advance universal service in high-cost areas, Congress intended that the Federal Communications Commission

(FCC) design truly a federal program of support that would address today's "advanced" telecommunications services.

In its *Recommended Decision*, the Joint Board declined to make a recommendation regarding the funding base for high-cost assistance, a reluctance probably reflective of the conspicuous split – i.e., high-cost vs. low-cost (winners vs. losers), or high-density vs. low-density – among the states about the appropriateness of using intrastate revenues for universal service support. However, the Joint Board at the same time noted that the “role of complementary state and federal universal service mechanisms require further reflection.”¹¹ Thus, it would come as no surprise later in April when a majority of the state members of the Joint Board voted to recommend that all universal service mechanisms be funded through assessments on both interstate and intrastate revenues.¹² Chairman Hundt and the FCC, however, apparently had other priorities. Admittedly shaken by the states’ opposition and judicial intervention in the interconnection proceeding, as well as, the outcry from low-cost states in the universal service leg of the trilogy, Chairman Hundt had a change of heart, retreating from the position that the use of intrastate revenues in the federal program would feed the federal-state partnership (and allow states to use interstate revenues for their own universal service programs) and give both jurisdictions the advantage of a broader revenue base. Rather, the chairman had grown increasingly concerned about the threat of court challenges from individual states opposed to the federal use of intrastate revenues. As a result, at a NARUC Communications Committee meeting in February 1997, he commented that the objectives of the proposed support fund were too important to permit its implementation to be delayed by jurisdictional turf fights.

¹¹ See Federal-State Joint Board on Universal Service, *Recommended Decision*, November 7, 1996, at para. 822. The Joint Board recommended that the FCC seek further information and additional comments on the issue of whether both intrastate and interstate revenues should be assessed to fund the high-cost and low-income support mechanisms.

¹² FCC *Report and Order*, at para. 811. The FCC acknowledged that a majority of the state Joint Board members had filed a report on April 24, recommending that all universal service mechanisms be supported “through an assessment on the interstate and intrastate revenues of interstate telecommunications.” in “Majority Opinion of the Joint Board on the Funding of Universal Service, dated Apr. 24, 1997.”

The Eighth Circuit Court's November 1996 decision to stay several provisions of the Commission's interconnection order seemed to solidify Hundt's concern about the universal service funding issue. (In July, the court released its Opinion, in which it admonished the FCC for not respecting state jurisdictional authority over local ratemaking.) Chairman Hundt responded to the November stay, claiming that this was the first time that a court had ruled that the FCC does not have the authority to implement rules established by congressional statute. He also predicted that the court's decision would lead to the "balkanization" of national telecommunications policy.

However, JSI notes, the Eighth Circuit Court's Opinion released in July identified precisely the reason why the FCC should have pursued a national direction in its universal service order. In finding that the FCC had intruded into intrastate ratemaking, the court declared that the commission failed to meet the "one possible" justification for its pricing order. That justification evolved from the "impossibility" exception noted in the U.S. Supreme Court's 1986 *Louisiana Public Service Commission v. FCC* which interpreted that the FCC has grounds to preempt state regulation of intrastate telecommunications only when it is impossible to separate the interstate and intrastate components of the FCC's regulation, and state regulation would negate the FCC's lawful authority over interstate communications.

At NARUC's Washington, D.C. meeting in February, Hundt was ready to propose that, for high-cost assistance, the federal universal service fund tap only carriers' interstate revenues because "I perceive we don't have enough support among states for use of intrastate revenues." At the same time, however, he stuck to his guns in his position that support for the new universal service program for schools, libraries, and rural health care should be funded through assessments on both interstate and intrastate revenues of interstate telecom providers. But state members of the Joint Board told NARUC's Communications Committee they were concerned about the effects of Hundt's proposal on high-cost states. Joint Board member Sharon Nelson (WA) declared that the FCC's action created a conflict between jurisdictional disputes and the

Act's objective to ensure that access to services be universally available.¹³ In addition, FCC Commissioner Rachele Chong warned the NARUC Communications Committee that if the federal program relied on interstate revenues only, individual states would be left to their own devices for universal service; in other words, Chong said, each state will have to "pull its own universal service wagon, and some states will have a heavier wagon than others."¹⁴

In April 1997, Joint Board member Julia Johnson (FL) wrote Hundt, advising that both interstate and intrastate revenues should be assessed because, in a nutshell, universal service is universal service; i.e., the Joint Board defined universal service to include services that are both intrastate and interstate in nature, and states, in turn, would be allowed to assess revenues from both. Assessing both will discourage carriers from claiming interstate revenues as intrastate to avoid assessment; and, as competition develops, state and federal jurisdictional distinctions will become more difficult.¹⁵ Subsequently, Johnson joined with fellow Joint Board members Sharon Nelson and Martha Hogerty (MO) among the majority voting to fund universal service through both, saying that if support were funded solely by interstate revenues, "the assessment may be unreasonably high and one group of carriers will bear the lion's share of the burden.... The potential for arbitrage is substantially greater if only interstate revenues are assessed.... The industry and its pricing strategies may evolve in such a manner as to render the distinctions between interstate and intrastate moot."

Similar to the state Joint Board majority, a number of Senate Commerce Committee members disagreed with the Order, expressing their opposition to the FCC's misreading of the

¹³ See *Telecommunications Reports*, March 3, 1997, p. 3.

¹⁴ *Ibid.*, p. 26.

¹⁵ Earlier, Johnson joined with fellow Joint Board member Sharon Nelson in a statement accompanying the *Recommended Decision* in which they identified the changing nature of universal service: "An additional question which must be addressed to fully answer the question of revenue base, is the extent to which the states and the FCC share the responsibility for ensuring the preservation and advancement of universal service. This determination will have a significant impact on the size of the federal fund.... As the technology converges and carriers begin to enter each others' markets, it is unclear that the traditional distinctions between interstate and intrastate carriers will retain their current meaning." See *Recommended Decision*, "Separate Statement of Commissioner Julia Johnson and Chairman Sharon L. Nelson."

Act's universal service intent. At the committee's March 12, 1997 meeting, Sen. Jay Rockefeller (D-WV), among others, said "combined" funds using both intrastate and interstate revenues would be necessary for support to high-cost areas. Sen. Byron Dorgan (D-ND) was especially critical of Hundt's change of heart, declaring that it was imperative that both interstate and intrastate revenues be considered because it was the only way to fully fund universal service and thus avoid rate increases. Committee Chairman John McCain (R-AZ) echoed Dorgan's sentiments, saying he was extremely concerned that not using both revenues as a base "would raise local rates significantly."

Regarding Hundt's apprehensions about the demands of low-cost states, Sen. Dorgan told Hundt that he should "override the concerns of 10 states that have questioned whether the FCC can assess intrastate revenues," because universal service "needs to be a product of national policy." In response, Hundt reminded Dorgan that the FCC had wanted to set "national" policy on interconnection pricing, but was stayed by a federal court: "It's very difficult to have a state-by-state competition policy and a national policy on universal service." Conceding Hundt's point that it may be difficult, Dorgan noted nonetheless, "it's necessary."¹⁶

In a subsequent interview with *Telecommunications Reports*, Chairman Hundt reiterated his fears of state reprisals. Professing that the FCC's universal service order would be a "permanent, long-term plan," he noted nonetheless that "there are changes afoot because of competition, particularly at the state level." In the interview, Hundt also said that relying on intrastate revenues would make the plan "imperial" and "Washington-centric." He also claimed that the FCC should not take an approach that would raise basic, dialtone rates in 40 states to

¹⁶ On March 3, 1997, Sen. Dorgan led a group of 25 U.S. senators writing to Chairman Hundt of their anxiety about the Joint Board's universal service recommendation. With the purpose of reminding the FCC of Congress's goals set forth in the Act, the senators wrote, "In providing for competition, especially in rural areas, it is clear in the Act that Congress rejected a 'one-size-fits-all' approach. Thus, it is important that the Commission structure universal service support mechanisms appropriately to reflect the unique circumstances of rural, high-cost areas." The senators went on to say that Congress intended for both the FCC and the states to have "primary roles" in assuring access at affordable rate, but that proposals that the states make primary determination "should not suggest that the Commission and the federal universal service support mechanisms have a limited role in assuring universal service.... There must be a federal foundation of support."

help 10 states. At the same time, he acknowledged that the Commission had to create an adequate fund that will address both short- and long-term needs.

At oversight hearings in June 1997, members of the Senate Commerce Committee again criticized the FCC's failure to create an adequate, national policy for universal service. Sen. Slade Gorton (R-WA), for one, asked Hundt why the order called for interstate revenues only to be assessed for universal service contributions and why the federal commitment would be limited to 25 percent. When Hundt again pointed to the threat of court challenges and to the "historic" allotment of interstate revenues for universal service contributions, several committee members argued that Congress had articulated provisions that envision a "substantial" federal commitment to universal service that should "far outweigh" the states' commitment.

In July 1997, NTCA sought reconsideration of parts of the Order, saying that the decision to limit federal support to 25 percent was "an exercise in arbitrariness" that conflicts with the Act's requirement that support be "sufficient, explicit, and predictable." In a September letter to the FCC, Sen. Conrad Burns (R-MT) explained his arguments against the 25-75 split and maintained his contention that the FCC should develop a national high-cost fund based on both interstate and intrastate revenues. Since Congress had clearly mandated a national policy, Conrad emphasized that such a fund should provide 100 percent of the support required to keep rural rates affordable. And, during confirmation hearings in October for new FCC Chairman William Kennard, Sen. Ted Stevens (R-AK) criticized the provisions in the universal order minimizing the federal commitment, charging that "these interpretations clearly contradict the law."

Clearly, JSI believes, those parts of the FCC's Universal Service Order relating to the revenues to be assessed and the federal share of universal service support funding conflict with Congressional intent; are ill-advised; and will, if carried out by the FCC, penalize customers in rural, high-cost areas because of where they live. In the short term, the Commission's proposals regarding the funding for universal service support mechanisms will lead to significant adverse

effects on rural telephone subscribers and communities; in the long term, these policies could have draconian consequences on rural economic development in general and on the future prospects of rural America itself.

Summary

JSI believes that the current bifurcated high-cost universal service support administrative rules: i.e., the 25 percent federal-75 percent intrastate responsibility, and the use of interstate and international revenues, without the benefit of intrastate revenues, as the basis for the contribution assessment, cannot be reconciled either with the provisions of the Act or with the FCC's own record.

The FCC's current administrative rules for bifurcated, high-cost, universal service support would result in the administrative burden of 50 state high-cost funds, and would discriminate against high-cost, less densely populated states: e.g., North Dakota could require a 35 percent surcharge on retail customer bills, while California would need only a 2 percent surcharge.

If the FCC were to establish a comprehensive system for universal service support and administration, the required surcharge could be uniform and nationwide, i.e., an overall 4 percent surcharge, nationwide, rather than a program that sees a 35 percent surcharge in a high-cost state but only 2 percent in a low-cost state.

JSI believes the FCC should revise its universal service support program to:

- Include all retail telecommunications revenues – interstate, international, and intrastate – in the assessment base:

- Beginning January 1, 1999, for those LECs eligible to receive high-cost universal service support funding on the basis of forward-looking economic cost, authorize the Universal Service Administrative Company (USAC) to collect, administer, audit, and distribute all funds based on a formula that determines the cost of supported services less the nationwide benchmark revenue, without regard to jurisdiction
- Allow the majority of the financial benefit of universal service support to be used by states to ensure that intrastate services supported by the federal program are maintained at a reasonably comparable rate level, nationwide:
- Rely on state regulatory authorities to see that funds received from the federal program are used to promote and advance universal service.

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CC Docket No. 96-45

Respectfully submitted,

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