Arizona Corporation Commission
1200 W. Washington
Phoenix, AZ 85007
(602)542-4143 fax (602)542-0765

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To:	Richard D. Smith FCC-CCB, Acctg. Policy Div.	**From:**	Commissioner –Chairman Jim Irvin (602) 542-4143
Fax:	202-418-7361	**Pages:**	7 (including cover sheet)
Phone:	202-418-7392	**Date:**	10/29/98
Re:	Referral Issues CC Docket No. 96-45	**CC:**	

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• **Comments:**

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ARIZONA CORPORATION COMMISSION

October 29, 1998

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TO: Members of the Federal-State Joint Board on Universal Service

Re: Universal Service
CC Docket 96-45
Referral Issues

Dear Federal-State Joint Board Members:

As Chairman of the Arizona Corporation Commission ("Arizona Commission" or "ACC"), I am pleased to submit these comments on the ACC's behalf. In June of this year, I spoke to you about the issue of unserved and underserved consumers – a problem which exists not only in Arizona, but in many other States as well. These consumers are unable to obtain telephone service in many instances because they cannot afford to pay the up front line extension or construction charges associated with extending facilities to their homes. The Arizona Commission respectfully requests that you keep these consumers in mind and Chairman Kennard's eighth universal service objective[1] when you formulate your recommended decision in this Docket. The Arizona Commission submits the following additional comments for your consideration on the referral issues.

Issue 1. **An appropriate methodology for determining support amounts, including a method for distributing support among the States and, if applicable, the share of total support to be provided by federal mechanisms. If the Commission were to maintain the current 25/75 division as a baseline, the Commission also requests the Joint Board's recommendation on the circumstances under which a State or carrier would qualify to receive more than 25 percent from the federal support mechanisms.**

[1] On February 9, 1998 Chairman Kennard gave a speech before the National Association of State Consumer Advocates in which he identified eight universal service principles. Principle eight provides that Federal and State universal service support mechanisms should promote service to historically underserved areas – Native American nations, for example.

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Of the proposals submitted, only the Arizona Commission's proposal adequately addresses the issue of unserved and underserved customers.[2] While the Arizona Commission's proposal is not a comprehensive alternative to the current 25/75 percent plan, it is designed to supplement the plan ultimately selected by the Joint Board and FCC, since none of the proposals currently under consideration, including the 25/75 percent split, adequately address this issue.[3] The costs to serve known unserved and underserved consumers have not been considered or included in any of the federal universal service costing models or proposals.[4] We believe that it is important to recognize and include these costs as part of any federal high cost funding mechanism. Moreover, because the traditional funding mechanism has not been effective in bringing service to these consumers, the ACC's proposal also requests that the existing incentive or distribution mechanism be reexamined and that the Joint Board and FCC consider providing up front incentives to carriers in the future to put the necessary facilities in place to serve these consumers.[5]

While the Arizona Commission is currently addressing this issue as part of its own State universal service funding mechanism, it believes that this issue is fundamental to the whole notion and concept of universal service and must be addressed at the Federal level as well. Together, State and Federal efforts could make considerable inroads into solving this problem. The result of these State and Federal efforts will have a concrete and immediate impact on the lives of individual consumers. Furthermore, with appropriate guidelines in place, a program of this nature would not result in unduly burdening the overall Federal funding mechanism. It is important to note that under the Arizona Commission's proposal, many of the costs would be one-time charges to assist in getting the necessary facilities in place. Finally, we are also not suggesting that this problem be solved all at once. A gradual plan which assists the States in their efforts to address this problem would be of considerable benefit. We view this issue as going to the core of Section 254's mandate to ensure the availability of basic telephone service in both high cost and low cost areas alike. The dual objectives of Sections 254(b)(1) and (c) are to

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[2] The Arizona Commission recommended in its proposal that the Federal fund contribute toward line extension or construction charges in the case of low-income consumers. State funding mechanisms could contribute toward these charges also.

[3] We believe this matter is appropriate for consideration in the referral phase since the degree of the FCC's responsibility to ensure universal service is at issue. Bringing basic telephone service to consumers is one of the primary purposes of the Federal universal service fund as contemplated under Section 254 of the Federal Act.

[4] For example, both the BCPM 3.1 and the HAI 5.0 models base their cost calculations solely on the number and estimated locations of current local phone service customers. Neither model makes an attempt to account for residents who are not currently local service customers.

[5] The Arizona Commission recognizes that guidelines would have to be established for the program it proposes and suggests that the Joint Board undertake this in a companion proceeding.

ensure comparability of rates between high and low cost areas[6] and service availability to the greatest extent possible.

The Arizona Commission has not had time to review in any detail all of the other proposals filed with the Joint Board. However, we urge you to consider the following factors when deciding upon a comprehensive high cost program, and the FCC's role under Section 254.

First, the support mechanism must strike an appropriate balance between the interests of high cost and low cost States without sacrificing any of the objectives set out in Section 254(b) of the Federal Act. The interests of low cost States must give way to the extent necessary to accomplish the universal service objectives of the Federal Act. The interests of high cost States must be balanced against the objectives of cost minimization and accountability.

Second, the alternative adopted should be sufficient, along with State funds, to ensure that the Section 254 objectives are being met in each State.[7] If a Federal baseline amount is used, then the Arizona Commission believes that a procedure must be available for States to obtain additional funding if necessary. One approach might be to use the concept of "affordability" as the basis for determining additional need.[8] Other parties have suggested use of the "hold harmless" approach, where carriers or States adversely affected by the 25/75 percent split would be kept at the same funding levels as they are now at under the existing Federal high cost fund. The difficulty with this approach is determining when a carrier or State is adversely affected and should receive more than the Federal baseline amount. An approach which makes it too difficult for a State to establish need, will end up thwarting the important objectives of the Federal Act.

Finally, the FCC should give the States more input or oversight into ensuring that Federal funds are being used for their intended purpose. One way to accomplish this would be through the use of block grants to the individual States, as

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[6] The Arizona Commission supports the Ad Hoc Plan to the extent it provides for the elimination of distinctions based upon size or classification (rural or non-rural) of carriers. These distinctions serve no legitimate purpose and operate to the disadvantage of States such as Arizona, which have one large carrier serving many of the high cost areas of the State.

[7] Section 254(c) of the Federal Act establishes a Federal-State partnership: [t]here should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service." Chairman Kennard also recognized the importance of this partnership in his eight principles on universal service.

[8] Several State Commissions have adopted universal service plans which act to "buy down" local service rates to "affordable" levels when necessary. This approach appears to be working fairly well and may be a concept worthy of some examination at the Federal level.

proposed in the Ad Hoc Plan. Another means would be to provide for the submission of carrier plans to the State Commission which would establish a continuing need for the funds and outline a program detailing how the funds obtained are to be used to further the universal service objectives of the Federal Act.

Fourth, the Joint Board and FCC should not adopt any methodology without concrete and empirical data on the plan's ultimate impact upon States and carriers. The Joint Board and FCC should take whatever time is necessary to examine the issues raised and to devise an appropriate methodology which meets the objectives of the Federal Act.

Issue 2(a) To the extent that Federal universal service reform removes subsidies that are currently implicit in interstate access charges, whether interstate access charges should be reduced concomitantly to reflect this transition from implicit to explicit support, and whether other approaches would be consistent with the statutory goal of making federal universal service support explicit. The Commission also requests a recommendation on how it can avoid "windfalls" to carriers if federal funds are applied to the intrastate jurisdiction before States reform intrastate rate structures and support mechanisms.

The Commission should handle the realignment of Federal access charges independent and outside of the context of its Federal universal service proceeding. Federal universal service distributions should be based upon above average costs and/or affordability determinations as provided in Section 254 of the Federal Act and should be used to reduce local service rates rather than implicit subsidies in Federal access charges.

The issue of implicit subsidies in both Federal and State rates is an extremely complicated one, which could in and of itself take considerable time to address. The FCC should not further complicate this proceeding, which is difficult enough, with issues which themselves are deserving of a separate proceeding. If the FCC attempts to address all of these issues in this proceeding, the result will most certainly be gridlock.

Issue 2(b) Whether and to what extent federal universal service policy should support State efforts to make intrastate support mechanisms explicit. The Commission recognizes that section 254(k) envisions separate State and Federal measures related to the recovery of joint and common costs, but nevertheless welcomes the Joint Board's input on how section 254(k) may relate to the Commission's role in making intrastate support systems explicit.

The Arizona Commission believes that it is the State's responsibility to make intrastate support systems explicit. The FCC should not make Federal universal service funding dependent upon a State's actions in this regard. The Federal Act does not support such a result or the FCC's involvement in such issues.

Nonetheless, to the extent local rates are "not affordable", the ACC believes that this would implicate the provisions of Section 254 and States should be able to petition the FCC for additional support, using an "affordability" or "hold-harmless" standard discussed in Issue 1 of these remarks.

Issue 2(c) The relationship between the jurisdiction to which funds are applied and the appropriate revenue base upon which the Commission should assess and recover providers' universal service contributions and, if support for federal mechanisms continues to be collected solely in the interstate jurisdiction, whether the application of federal support to costs incurred in the intrastate jurisdiction would create or further implicit subsidies, barriers to entry, a lack of competitive neutrality, or other undesirable economic consequences.

The Federal Act authorizes the FCC to assess interstate revenues only for purposes of the Federal funding mechanism. The FCC should not base its assessments for the Federal funding mechanism on intrastate revenues or a combined revenue base. This action would discourage States from establishing their own universal service funds. Moreover, this would unduly burden carriers, which operate in States such as Arizona, that have established State funds and already draw upon intrastate revenues.

The only instance in which the assessment of intrastate revenues may be appropriate is if a State elected not to establish its own funding mechanism, desiring instead that the FCC administer a combined program on both its and the FCC's behalf.

Issue 3. To what extent, and in what manner, is it reasonable for providers to recover universal service contributions through rates, surcharges, or other means.

For purposes of the Federal funding mechanism, the Joint Board and FCC may provide that carrier contributions can be recovered through either end-user rates or end-user surcharges. To the extent contributions are recovered through rates, carriers have more discretion as to how and if they are recovered. The Arizona Commission's funding mechanism provides for the use of a surcharge.

On behalf of the Arizona Corporation Commission, I appreciate the opportunity to address these important issues and to provide comment for your consideration. Please do not hesitate to call me at 602-542-4143 or my Assistant, Mark A. DiNunzio at 602-542-3622 if you have any questions regarding these comments.

Very truly yours

Jim Irvin
Commissioner-Chairman
Arizona Corporation Commission

JMA/MAS/ms

cc: The Honorable John McCain