

Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, DC 20554

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FEDERAL COMMUNICATIONS COMMISSION  
OFFICE OF THE SECRETARY

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. <u>96-45</u>
Universal Service	)	
	)	
Access Charge Reform	)	CC Docket No. 96-262

REPLY COMMENTS OF U S WEST, INC.

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## SUMMARY

Although most of the latest round of commentary in this docket was thoroughly predictable, there were two major exceptions. First, U S WEST went beyond the heartland of the commentary and pointed out that the Commission's proposals for implementation and the model itself are fatally flawed and contrary to the universal service goals of the 1996 Act. The second exception is even more notable; MCI in large part agreed with U S WEST on these fundamental points. To wit, MCI and U S WEST agree on the following:

- The Commission's implementation proposals fall far short of the Act's requirements.
- The Commission's decision not to go all the way with the universal service reform mandated in the Act, but rather to arbitrarily limit the fund size to well below the mandated level of sufficiency, is unlawful.
- The Commission's approach would unlawfully maintain implicit subsidies.
- The Commission's decisions were made in a fact-free environment and lack any evidentiary support.

Such agreement among traditional opponents is very persuasive and should be taken to heart by the Commission.

In addition, these reply comments observe that there was substantial support in the commentary for U S WEST's position that study area targeting is not only unwise but unlawful because it relies on implicit subsidies that are vanishing, thus leaving rural customers out in the cold.

Further, in these Reply Comments, U S WEST addresses the potential effect of the recent Fifth Circuit decision regarding the First Universal Service Order. In

essence, that decision confirmed the mandate to replace implicit support with explicit support -- a mandate ignored by the Commission in its proposals.

Finally, U S WEST addresses what must be done in the short term to support universal service while the Commission returns to the drawing board (as it must) to design a lawful long term universal service model.

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REPLY COMMENTS OF U S WEST, INC.

I. INTRODUCTION<sup>1</sup>

Even MCI WorldCom, Inc. (“MCI”) agrees with U S WEST, Inc. (“U S WEST”) that the Federal Communications Commission’s (“Commission”) artificial attempts to limit the fund size are unlawful and antithetical to the purposes of the 1996 Act, as noted in the following quotation taken from MCI’s comments:

But the Act requires the Commission to undertake comprehensive universal service reform of the sort proposed in the First Report and Order – defining and calculating the total universal service subsidy need, creating an explicit fund to meet that need . . .<sup>2</sup>

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<sup>1</sup> These Reply Comments are submitted for the record in the following proceedings: In the Matter of Federal-State Joint Board on Universal Service, Access Charge Reform, CC Docket Nos. 96-45 and 96-262, Seventh Report & Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45 Fourth Report & Order in CC Docket No. 96-262 and Further Notice of Proposed Rulemaking, FCC 99-119, rel. May 28, 1999 (“Implementation FNPRM”).

<sup>2</sup> MCI at 6 (emphasis added).

Thus, the “hold harmless” and “no increase in fund size” goals manufactured by the Commission are unlawful as is any model arising from them. Don’t take U S WEST’s word for it; ask MCI.<sup>3</sup>

With the significant exception of MCI, the comments in this proceeding generally stuck to the script that has become all too familiar in the never-ending three year saga of universal service. Commentors representing low-cost state commissions, urban state local exchange carriers (“LEC”) and carriers who do not serve rural local exchange customers called for a small fund “targeted” to the study area level.<sup>4</sup> Regulators from high-cost states and LECs serving larger numbers of rural consumers stressed the concepts of “sufficiency” and “comparability” as required in the 1999 Act and called for generally more funding specifically targeted to high-cost areas within a state.<sup>5</sup> Commentors representing “rural” LECs wished

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<sup>3</sup> Although U S WEST must applaud MCI’s frankness in this docket, it also must question its sincerity given that MCI here decries the model as unlawful and resulting in insufficient explicit support amounts, while it joins AT&T Corp. (“AT&T”) in the companion FNPRM in arguing for even lower inputs (and therefore support amounts) than the Commission has proposed. See Joint Comments of AT&T Corp. and MCI WorldCom, Inc., filed July 23, 1999, to the Further Notice of Proposed Rulemaking, CC Docket Nos. 96-45 and 97-160, FCC 99-120, rel. May 28, 1999 (“Inputs FNPRM”).

<sup>4</sup> See, e.g., AT&T at 12; Ameritech at 4-7; Bell Atlantic Telephone Companies (“Bell Atlantic”) at 5-6; People of the State of California and the California Public Utility Commission at 11 (“California”); New York State Department of Public Service at 5 (“New York”).

<sup>5</sup> See, e.g., GTE Service Corporation at 20-22 (“GTE”); U S WEST at 5, 8-15; Iowa Utilities Board at 1, 2-3; Non-Urban State Commissions (Arkansas, Maine, Montana, New Hampshire, North Dakota, Vermont, West Virginia and Wyoming State Regulatory Agencies) *passim*.

that none of this tumult would affect them.<sup>6</sup> Some new ideas did emerge from the comments, and we will note several of them later in these reply comments.

As noted, the one exception to the patterns of the past is in the comments of MCI. In U S WEST's Comments we sought to explain why the "solution" which the Commission presented in the Implementation FNPRM failed to meet the clear universal service directives contained in the Telecommunications Act of 1996.<sup>7</sup> While U S WEST and MCI may disagree on many issues, we appear to have a common opinion on the fundamental shortcomings of the proposed universal service plan. Among other things, MCI stated:

Fundamentally, the Order fails to achieve the requirements of the Telecommunications Act of 1996. (Page 2)

The partial universal service reform presented in the Order, which attempts to address a narrow universal service issue by adhering to the old regulatory paradigm, is antithetical to the comprehensive reform required by the Act. (Pages 2-3)

In the Further Notice, the Commission couches its request for input on what the values should be for these variables in terms of whether and how the values can be chosen to yield a small explicit fund, based on its finding that in today's market environment, with the lack of competition, the implicit universal service subsidies in above-cost rates are not threatened by erosion and therefore only a small fund is needed. (Pages 4-5)

The Commission has created a fact-free environment in which it believes it will be able to justify any course it chooses by manipulating the values for these input variables. (Page 6)

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<sup>6</sup> See, e.g., Rural Telephone Coalition at 6 ("RTC"); Virgin Islands Telephone Corporation at 4-5 ("Virgin Islands"); TDS Telecommunications Corporation at 3-4 ("TDS").

<sup>7</sup> U S WEST at Section II.A.

A “solution” that does not identify and calculate the total universal service funding need, but rather maintains unidentified and unmeasured levels of funding embedded in rates that are potentially subject to competitive erosion, harms the marketplace by unnecessarily maintaining a high level of government-induced uncertainty. (Page 6)

The Commission based key elements of the mechanism on the recommendations in the Joint Board’s Second Recommended Decision, but those recommendations were made without any supporting evidence in the record and the Commission has provided no other evidentiary support for those key elements. (Page 7)

We are not so naïve as to think that U S WEST and MCI have the same vision of what the ultimate universal service solution should look like, but we appear to be of a common mind that this plan just does not get there. For all of their corporate history MCI has had a single-minded vision to enter markets and compete. The cornerstone of the 1996 Act was the opening of local markets to competition. In our comments we stated our belief that Congress intended that this competition be efficient,<sup>8</sup> and that required the replacement of implicit subsidies with “specific, predictable and sufficient”<sup>9</sup> explicit support. As already discussed above, on page 6 of their comments MCI clearly echoes U S WEST’s position:

But the Act requires the Commission to undertake comprehensive universal service reform of the sort proposed in the First Report and Order – defining and calculating the total universal service subsidy need, creating an explicit fund to meet that need, and concurrently removing existing implicit universal service subsidies from interstate access charges. (Emphasis added.)

U S WEST agrees.

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<sup>8</sup> U S WEST at 5.

<sup>9</sup> Id. at 3.

In the remainder of our Reply Comments we will discuss several areas where we believe the Commission's plan falls short including the hold-harmless provisions and the level of universal service targeting. We will also comment on the impact of the recent 5<sup>th</sup> Circuit Court of Appeals ruling on the Commission's First Report and Order in this proceeding.<sup>10</sup> We believe that this ruling further supports the fact that the Commission's plan as expressed in its Implementation FNPRM fails to implement the clear directives of Congress and is therefore unlawful. Finally we will comment on several alternatives which have been presented for positive Commission action in the near term to address the needs of high-cost rural consumers.

## II. THE HOLD HARMLESS PROVISIONS

In our comments we stated the belief that the Commission's plan failed to achieve even a reasonable short-term solution because of two fundamental flaws:

The requirement that the new fund should not be "substantially larger" than the currently existing fund, and

That recipients should be "held harmless" for their current receipts from the fund.<sup>11</sup>

U S WEST believes that even if the fund is to be unlawfully constrained below that which is "sufficient," the Commission must at least attempt to move toward achieving the intent of the 1996 Act by allowing what funding is available to

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<sup>10</sup> Texas Office of Pub. Util. Counsel v. FCC, No. 97-60421, (5<sup>th</sup> Cir. July 30, 1999), affirmed in part, remanded in part, and reversed in part.

<sup>11</sup> U S WEST at 2.

flow to the highest-cost customers.<sup>12</sup> This outcome would still be insufficient and unlawful, but it would be preferable to the current Commission proposal. The hold harmless proposal makes this allocation impossible since current recipients and states are guaranteed what they presently receive, even if higher-cost customers remain unfunded in other states.

In the Implementation FNPRM the Commission asks whether hold-harmless provisions should be applied at the state level or the carrier level. Again the results are predictable. LECs overwhelmingly believe it should be applied at the carrier level because the carriers are the ones that actually incur the cost of service<sup>13</sup> while state regulators and most others believe it should be applied at the state level.<sup>14</sup> Missing in all of these comments, however, is the impact which hold harmless provisions, no matter at what level, will have on the ability of consumers in high-cost rural areas of Non-Rural LECs to enjoy affordable and advancing telecommunications services.

### III. THE TARGETING OF SUPPORT

If support is to go to those customers most in need, then some means must be found to identify those locations and determine the amount of support needed. This is not accomplished by “targeting” support to the study area. As U S WEST

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<sup>12</sup> U S WEST at 6. The concept of allowing limited funding to flow to the most needy customers was supported by other commentors. See, e.g., GTE at 20; MCI at 16; Sprint at 12; Non-Urban State Commissions at 20.

<sup>13</sup> See GTE at 36; BellSouth at 9; SBC at 9; Sprint Corporation at 5 (“Sprint”); United States Telephone Association at 4 (“USTA”).

<sup>14</sup> See California at 5; Public Service Commission of Wisconsin at 7 (“Wisconsin”).

explained in our comments, when support is provided based on study area averages, carriers will receive the same amount of support per customer whether they serve remote rural customers or customers in dense urban areas.<sup>15</sup>

By determining support requirements based on study area average costs, the Commission leaves large amounts of implicit universal service support in LECs' rates structures, both state and interstate.<sup>16</sup> Many commentators have noted averaging costs at the study area level to determine the amount of subsidy will result in a smaller fund size.<sup>17</sup> However this smaller fund size comes at the expense of the rural consumer.

An interesting perspective on the need for targeted high-cost support can be found in the comments of the state of Wisconsin. On page 6 they state

States that are primarily urban will not need to develop large state mechanisms, as they will have few rural areas to support. States with substantial high cost areas in addition to urban areas, will need larger state support mechanisms, and thus larger universal support assessments in those states. This may result in businesses choosing not to locate in Wisconsin (or other similarly-situated states) because its telecommunications services have a high universal service program assessment.

As Wisconsin so eloquently illustrates, what is at stake here is not so much the need to minimize the fund, but to support rural communities, as Congress intended. In addition to helping rural communities and consumers, however, the removal of implicit subsidy and its replacement with explicit subsidy is also directly

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<sup>15</sup> U S WEST at 13.

<sup>16</sup> *Id.* at 5.

<sup>17</sup> *See, e.g.*, AT&T at 7; Ameritech at 2; Bell Atlantic at 2; California at 3; New York at 5.

linked to the other objective of Congress, the facilitation of efficient local competition. On page 11 of their comments Sprint states:

To the extent that the universal service plan causes the subsidization of high cost areas by low cost areas to continue, the Commission must accept the reality that this type of subsidization will be eroded with the arrival of competition in the low cost areas – the only portion of the study area to which competitors will flock.

While averaging of costs over large areas reduces the perceived size of the high-cost support need, it does so by the continued reliance on implicit support which distorts the evolution of efficient competition. Returning to the comments of MCI:

These factors affect fund size because they represent greater or lesser cost averaging or, put another way, maintaining greater or lesser levels of implicit universal service support. (Page 18)

To facilitate competitive entry and support the needs of rural consumers Congress specifically sought the removal of implicit support and replacement with explicit support.

#### IV. THE FIFTH CIRCUIT CASE

On July 30, 1999 the United States Court of Appeals for the Fifth Circuit released its decision in its review of the Commission's initial Universal Service Order.<sup>18</sup> While the decision commented on many aspects of the Order, including the high-cost, schools and libraries and rural health care elements, the Court offered useful guidance in the area of the continued reliance on implicit support, which confirmed the invalidity of the Commission's current proposal.

The Court made it abundantly clear that the Commission's notion that the requirement that interstate universal service funding must be "explicit and sufficient" is based on statutory language of command, not exhortation. This is because Section 254(e) of the 1996 Act is stated in mandatory terms, unlike the more general principles which are found in Section 254(b) of the 1996 Act. Thus, the Commission is not free to enact rules which concretize an implicit subsidy for universal service without running afoul of the 1996 Act itself. Based on its finding that the Commission's rule that ILECs must recover their universal service fund obligations through carrier access charges constituted an implicit subsidy for universal service (a subsidy which discriminated against ILECs), the Court reversed this Commission rule and remanded it for further resolution consistent with the Court's opinion.

Similarly, the Commission's proposals to arbitrarily limit the fund to its current size and to postpone replacing implicit subsidies with explicit ones is also unlawful. U S WEST pointed this out in its prior comments, and the Fifth Circuit opinion serves as confirmation. Thus, the Commission must scrap its current approach in favor of a lawful one that, among other things, does not maintain implicit subsidies, and creates explicit subsidies sufficient to accomplish the 1996 Act's universal service goals.

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<sup>18</sup> Texas Office of Pub. Util. Counsel v. FCC, No. 97-60421, (5<sup>th</sup> Cir. July 30, 1999), affirmed in part, remanded in part, and reversed in part.

## V. WHAT THE COMMISSION CAN DO IN THE NEAR TERM

It has been over three years since the Commission began this journey to implement the universal service directives of the 1996 Act, and the end is clearly nowhere in sight. In our Reply Comments in the companion proceeding (Inputs FNPRM) we continue our arguments that the Commission's Synthesis Model is fatally flawed and significant changes would be required before it could be used to determine specific high-cost funding requirements. Unfortunately, the many outstanding issues are not likely to be resolved by the planned January 1, 2000 implementation date for the new explicit mechanism. Nonetheless, CLECs continue to win high-margin business customers and the base of implicit support for high-cost customers continues to erode. Clearly something must be done in the near term.<sup>19</sup> At a minimum, the Commission must institute some interim plan to provide additional support to the highest cost customers (for example, those costing \$100/month or more).

Several commentors offer suggestions for how this could be accomplished:

MCI (at 11) suggests the Commission consider the Super Benchmark plan proposed by U S WEST.<sup>20</sup> We are obviously flattered by this proposal, and believe that it would provide a workable way to direct what explicit support is available to those most clearly in need of support to maintain affordable service. Some form of

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<sup>19</sup> Consequently, RTC's request for a delay to resolve a perceived issue with the cap on loop support must be denied. This issue has nothing to do with the growing need for increased explicit non-rural support and should not hold up such support.

reasonable proxy model could be used as an interim tool to identify relative costs among geographic areas and to target support to the highest cost customers.

The Non-Urban State Commissions (at 14) offer a proposal to identify the gross amount of funding that would be necessary to maintain comparable rates between urban and rural areas as directed by the 1996 Act. Their methodology suggests that a fund of approximately \$3 billion may be necessary for this purpose. Although we do not fully understand the details of their proposal,<sup>21</sup> some methodology that would rough-size the necessary fund could be developed and the resulting fund distributed to benefit customers in the highest cost areas. This is similar to the plan outlined by U S WEST in our comments, but may be easier to implement in the short term as a transition plan.

The Non-Urban State Commissions (at 21) also offer an alternative interim plan to utilize the accounting costs currently reported by incumbent carriers. Their proposal would abolish the distinction which exists in the current USF program between customers with over 200,000 lines in a study area and those with fewer than 200,000 lines. Presently carriers below this line threshold receive a minimum of 60% of their costs above 115% of national average from the federal fund, while those with over 200,000 lines receive only 10% of their costs over 115% of the

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<sup>20</sup> See, e.g., Reply Comments of U S WEST Communications, Inc. on Proposals to Revise the Methodology for Determining Universal Service Support, CC Docket Nos. 96-45 and 97-160, filed May 29, 1998.

<sup>21</sup> For example, we disagree with the use of study area average costs. It should be noted that the Wyoming PSC dissented from the others on the use of study area average costs (*see* signature page for Stephen Oxley, Esq. of the Wyoming PSC).

national average. As explained in U S WEST's comments<sup>22</sup> the new market environment makes this distinction irrelevant, and maintaining this discrimination between rural customers of "non-rural" carriers and the rural customers of "rural" carriers risks the creation of telecommunications "haves" and "have-nots" in rural America. While not a permanent solution, a plan such as this might form a workable interim step.

## VI. CONCLUSION

The great weight of the persuasive commentary on the Commission's proposed rules concerning implementation manifestly demonstrate that the Commission's proposal constitutes an utter abandonment/complete disregard of the universal service provisions of the 1996 Act. The resulting support would not be sufficient, nor would it be fully explicit, nor would it be predictable. Moreover, given the need for the Commission to go back to the drawing board, there is an urgent need for an interim solution to the growing problem of the simultaneous erosion of implicit support and the inertia and inadequacy of current levels of explicit support. Consequently, U S WEST implores the Commission to immediately begin work on an interim solution, while abandoning its doomed

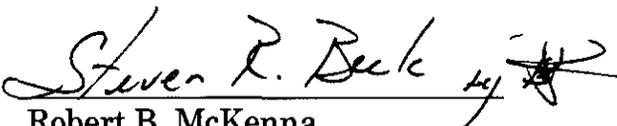
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<sup>22</sup> U S WEST at 16.

course regarding the permanent fund in favor of one actually and competently  
calculated to achieve the universal service aims of the 1996 Act.

Respectfully submitted,

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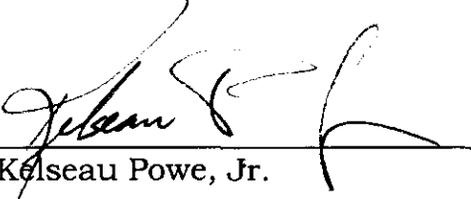
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August 6, 1999

**CERTIFICATE OF SERVICE**

I, Kelseau Powe, Jr., do hereby certify that on this 6<sup>th</sup> day of August, 1999, I have caused a copy of the foregoing **REPLY COMMENTS OF U S WEST, INC.** to be served, via first class United States mail, postage prepaid, upon the persons listed on the attached service list.

  
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