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ANN BAVENDER*
ANNE GOODWIN CRUMP
VINCENT J. CURTIS, JR.
RICHARD J. ESTEVEZ
PAUL J. FELDMAN
RICHARD HILDRETH
FRANK R. JAZZO
ANDREW S. KERSTING
EUGENE M. LAWSON, JR.
SUSAN A. MARSHALL*
HARRY C. MARTIN
GEORGE PETRUTSAS
RAYMOND J. QUIANZON
LEONARD R. RAISH
JAMES P. RILEY
KATHLEEN VICTORY
HOWARD M. WEISS
ALISON J. SHAPIRO

* NOT ADMITTED IN VIRGINIA

FLETCHER, HEALD & HILDRETH, P.L.C.

ATTORNEYS AT LAW

11th FLOOR, 1300 NORTH 17th STREET

ARLINGTON, VIRGINIA 22209-3801

(703) 812-0400

TELECOPIER

(703) 812-0486

INTERNET

www.fhh-telcomlaw.com

FRANK U. FLETCHER
(1939-1985)
ROBERT L. HEALD
(1956-1983)
PAUL D.P. SPEARMAN
(1936-1962)
FRANK ROBERSON
(1936-1961)
RUSSELL ROWELL
(1948-1977)

EDWARD F. KENEHAN
(1960-1978)

CONSULTANT FOR INTERNATIONAL AND INTERGOVERNMENTAL AFFAIRS
SHELDON J. KRYS
U. S. AMBASSADOR (ret.)

OF COUNSEL
EDWARD A. CAINE*
MITCHELL LAZARUS*
EDWARD S. O'NEILL*
JOHN JOSEPH SMITH

WRITER'S DIRECT

703-812-0403
feldman@fhh-telcomlaw.com

February 22, 2000

VIA HAND-DELIVERY
Magalie Salas, Esq.
Secretary
Federal Communications Commission
Room TW-B204
445 12th Street, S.W.
Washington, D.C. 20554

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FEB 22 2000

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Re: CC Docket No. 96-45
CC Docket No. 97-160
Reply to Opposition to and Comments on Petition
for Reconsideration of Roseville Telephone Company

Dear Ms. Salas:

On behalf of Roseville Telephone Company, I enclose an original and four copies of its Reply to Opposition to and Comments on Petition for Reconsideration of Roseville Telephone Company. If there are any questions regarding this matter, please contact me.

Very truly yours,

Paul Feldman

Paul J. Feldman
Counsel for Roseville
Telephone Company

Enclosure
cc: Certificate of Service
Mr. Mike Campbell (w/encl.)
Mr. Greg Gierczak (w/encl.)
Mr. Glenn Brown (w/encl.)

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FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
Forward Looking Mechanism for High Cost Support for Non-Rural LECs	)	CC Docket No. 97-160

REPLY TO OPPOSITION TO AND COMMENTS ON PETITION FOR RECONSIDERATION OF ROSEVILLE TELEPHONE COMPANY

Paul J. Feldman, Esq.
Fletcher, Heald & Hildreth, P.L.C.
1300 N. 17th Street, 11th Floor
Arlington, Virginia 22209
(703) 812-0400

Glenn Brown
McLean & Brown
9011 East Cedar Waxwing Dr.
Chandler, Arizona 85248
(480) 895-0063

February 22, 2000

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

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Federal-State Joint Board on Universal Service	))	CC Docket No. 96-45
	)	
Forward Looking Mechanism for High Cost Support for Non-Rural LECs	)))	CC Docket No. 97-160

REPLY TO OPPOSITION TO AND COMMENTS ON PETITION FOR RECONSIDERATION OF ROSEVILLE TELEPHONE COMPANY

Roseville Telephone Company ("Roseville") hereby replies to the Comments on and Opposition to the Petition filed by Roseville on December 30, 1999 ("PFR") seeking reconsideration of a portion of the Tenth Report & Order[1] in the above-captioned proceeding.[2]

I. Introduction

It is important at the outset to clarify what Roseville is requesting in its PFR, and what it is not, because a misunderstanding of Roseville's request lies at the heart of challenges to its proposal. In its PFR, Roseville requested that the Commission change the dividing-point between "large" and "small" telephone companies solely for

[1] FCC 99-304, released November 2, 1999 (hereinafter *"Tenth R & O"*).

[2] The pleadings responded to herein are Comments filed by MCI Worldcom, Inc. ("MCI"), and an Opposition filed by the People of the State of California and the California Public Utilities Commission ("CPUC"). It should be noted that Roseville also filed a PFR regarding the portions of the Commission's Ninth Report and Order in CC Docket 96-45 which incorrectly included *interstate* Long Term Support in the hold-harmless provisions of its new explicit support mechanism for *intrastate* costs. Significantly, no parties filed oppositions to that PFR.

the purposes of the new explicit high-cost mechanisms mandated by the 1996 Act. The *Tenth R & O* utilized the "rural/non-rural" distinction as defined in Section 3(37) of the Communications Act.[3] Roseville proposed that the dividing-line be changed to use the over/under 200,000 line distinction used in the current Universal Service Fund (USF) calculus. <u>Roseville is not requesting to be considered a "rural" telephone company for purposes of Sections 251 or 252 of the Communications Act.</u>[4] What Roseville is requesting is that it (and four other similarly situated LECs) be treated, for federal high cost support purposes, under the provisions to be recommended by the Rural Task Force. Such an approach would treat Roseville in a manner consistent with companies more similar in size and cost structure to Roseville, than to non-rural BOCs hundreds of times its size. The result would be to protect Roseville's subscribers from substantial rate increases.

A critical problem that the Commission must manage is the transition from the current USF to the new explicit support mechanism. The USF essentially defines two types of study areas – "65%" study areas and "10%" study areas. A study area with less than 200,000 lines (such as that of Roseville) receives 65% of its high costs[5] from the USF, while a study area with over 200,000 lines receives only 10% of its high costs

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[3] In hindsight, the use of the terms "rural" and "non-rural", particularly in the context of universal service reform, is unfortunate. Such terms may create incorrect implications regarding the size and cost structure of a company based on the location of the company's service area. In addition, "non-rural" companies often serve rural areas, while some "rural" companies serve in urban areas.

[4] The Section 3(37) definition of rural telephone company is used primarily to determine a company's interconnection obligations and other relationships with competitive carriers. As will be discussed more fully below, Roseville is currently interconnected with eight competitive carriers serving customers in its territory.

[5] High costs are those loop costs which exceed 115% of the nationwide average loop costs. See 47 CFR Section 54 for a complete description of the USF rules.

from the fund. Virtually all RBOC and GTE study areas are of the 10% variety. To the extent that any of these areas are to receive "hold-harmless" support, the phase-out of this support will have less impact on end-users. In contrast, virtually all Section 3(37) "rural" study areas are 65% study areas. Since these receive proportionately six and one-half times more of their high costs from the USF than would a comparable 10% study area, the transition to the new explicit high-cost support mechanism will have significantly more impact on these companies and their customers. It was largely for this reason that the Universal Service Joint Board created the Rural Task Force ("RTF") to examine the applicability of the Synthesis Model and the non-rural support mechanism and transition plans to the smaller LECs.

In the PFR, Roseville discussed the different transitional problems faced by the "65%" (i.e., under 200,000 line) study areas, using the following chart:

	Study Area A	**Study Area B**	**Study Area C**
Lines	4,500,000	120,000	4,500
Section 3(37) Class	Non-Rural	Non-Rural	Rural
Cost/Line*	$35.00	$35.00	$35.00
Nat'l Average*	$25.00	$25.00	$25.00
Difference	$10.00	$10.00	$10.00
USF	$1.00	$6.50	$6.50
Per-Line Impact of 3-Year Phase-Out	$0.33	$2.16	$2.16

*Hypothetical values for illustration purposes. All figures are $/line/month.

This chart shows three hypothetical study areas with identical per-line costs, but with different numbers of lines. Notice that while Study Area B at 120,000 lines is classified as a Section 3(37) "non-rural" study area, since it serves less than 200,000 lines it receives the same proportional USF support as Study Area C, the Section 3(37) "rural" study area. More importantly, the customer impact of a three year phase-out of hold-harmless support is the same as for the "rural" study area, and six and one-half times that of the large "non-rural" area.

Roseville is not the only Section 3(37) non-rural study area that receives hold-harmless support yet serves less than 200,000 lines. The following chart shows the four other study areas that fall into this category, and the amount of USF that they currently receive.

Non-Rural Study Areas Under 200,000 Lines Receiving HH Support

		Hold Harmless Support	
	USF Loops	Annual	$/Line/Mo
Contel Of North Carolina dba GTE NC	128,838	$2,324,124	$3.01
GTE North Inc - Missouri	118,118	$428,604	$0.60
North State Telephone Company-NC	126,149	$2,414,388	$1.59
P R T C - Central	157,150	$35,831,868	$31.06
Roseville Telephone Company	117,860	$6,372,420	$5.70

Source: NECA 1Q2000 High-Cost Funding Report App 1 (annualized)

In sum, the transition to the new federal high cost support system is a complex task that can impose unnecessary harm on certain companies and their subscribers. One means for limiting such unnecessary harm is to make an appropriate distinction between the large companies that will be moving to the Synthesis Model, and the other companies, for whom federal support is to be determined through the RTF.

II. The Concerns of the CPUC are Not Relevant and are Misplaced.

The California Public Utilities Commission (CPUC) bases its opposition to Roseville's universal service proposal on the concern that if it is granted "rural" status, Roseville will somehow use this to seek "rural" status for the purposes of Section 251, and thus avoid its interconnection responsibilities with competing carriers. Opposition at note 3. The CPUC's concerns are greatly misplaced. First, in the PFR, Roseville is not seeking "rural" status pursuant to Section 251(f) of the Act. Rather, it is merely seeking to change the demarcation point between "large" and "small" LECs for the purposes of federal high-cost support. Second, Roseville is actively meeting its interconnection obligations, and currently interconnects with eight CLECs who are serving customers in Roseville's territory.[6] Roseville's PFR was not filed in order to shelter itself from competition. Third, the CPUC's expressed concern is inconsistent with the plain language of 251(f). Section 251(f)(1) deals with rural companies as defined by Section 3(37), and provides an exemption from certain interconnection obligations until the carrier (1) receives a bona fide request, and (2) the state PUC determines that such request is not unduly burdensome. Since Roseville does not meet the Section 3(37) definition of "rural", and Roseville is not requesting a change of its status, the CPUC's concerns regarding Section 251(f)(1) are misplaced. Section 251(f)(2) applies to "rural" carriers with "fewer than 2 percent of the Nation's subscriber

[6] The CLECs with which Roseville currently interconnects are AT&T, ICG, MCI, PacWest, Option One, Pacific Bell, Nextlink, and ELI.

lines". Because Roseville serves less than two percent of the Nation's access lines, it could petition for a modification or suspension of its interconnection obligations under Section 251(f)(2), if it wanted to, regardless of how the Commission rules on the instant PFR. In such a case, however, the CPUC is empowered to review the facts set forth in the petition, and make its own evaluation as to whether to grant the Section 251(f)(2) petition. Thus, the grant of the PFR will not alter Roseville's interconnection obligations, or force the CPUC to alter those obligations.

The CPUC also states that "Roseville's plea that it be treated like a rural carrier is incompatible with its request, granted by the CPUC, to be treated as a competitive carrier for state ratemaking purposes under the CPUC's New Regulatory Framework (NRF)". Opposition at page 4. This argument is not relevant to the issues in the PFR. Currently four California LECs operate under the NRF: Pacific Bell, GTE, Roseville and Citizens Utilities. Citizens Utilities, however, is classified under the Section 3(37) guidelines as a "rural" carrier. Thus even if Roseville were requesting "rural" designation, this would have no impact on its NRF status under California regulation. Similarly, a carrier's status under NRF should have no impact on federal policies for high-cost support. There is no necessary connection between the two.

On pages 3 and 4 of its Opposition, the CPUC argues that Congress did not intend that different regulatory distinctions be used for interconnection and universal service purposes:

> "...both the interconnection and universal service provisions of the Act refer to a rural telephone company, which evidences Congress' intent to treat such a company the same for both interconnection and universal service purposes."

Yet, while Section 214(e) does use the term "rural telephone company" in two sub-sections,[7] none of these sub-sections require the Commission to use the Section 3(37) rural/non-rural distinction for the purposes of determining which carriers are subject to the new Synthesis model high-cost support mechanism. Similarly, while Section 254 of the Act uses the word "rural" in four places,[8] the words "rural telephone company" appear nowhere in Section 254, and thus that Section does not mandate use of the Section 3(37) rural/non-rural distinction for the purposes of determining which carriers are subject to the new Synthesis model high-cost support mechanism. Indeed, nothing in the California Opposition contradicts the Commission's finding in the *Tenth R&O* on this issue: "Although the Commission used the rural telephone company definition to distinguish between rural and non-rural carriers for purposes of calculating universal service support, there is no statutory requirement that it do so." Thus, lacking any statutory barrier to doing so, the Commission should grant Roseville's request to re-

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[7] 214(e)(2) provides that a state "may" designate more than one "Eligible Telecommunications Carriers" in rural telephone company area, and "shall" do so in all other areas. 214(e)(5) defines the "service area" for universal service support obligations for a rural telephone company to be its study area.

[8] The contexts where the word "rural" appears in Section 254 are as follows:

- 254(b)(3) ACCESS IN RURAL AND HIGH COST AREAS – 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...that are reasonably comparable to those provided in urban areas...at rates that are reasonably comparable.
- 254(g) INTEREXCHANGE AND INTERSTATE SERVICES – The rates for interexchange telecommunications services to subscribers in rural and high cost areas shall be no higher than rates in urban areas.
- 254(h)(1)(A) HEALTH CARE PROVIDERS FOR RURAL AREAS – Services to rural health care providers should receive support so that costs of are comparable to similar services in urban areas.
- Section 254(h)(5)(b)(vi) further defines a "health care provider" to include "rural health clinics".

define the break-point for implementation of the new explicit high-cost mechanism, in order to assure a smoother transition process and minimize the impact on customers.

Finally, Roseville is puzzled by the CPUC's discussion of rate shock in page 6 of its Opposition. No one likes to see customers' rates go up, particularly as competition expands in the local telephone market. From time-to-time, in order to meet obligations to invest to serve customers, and to have earnings adequate to meet the needs of shareholders, regulated telephone companies such as Roseville must file for rate increases with their state regulator. This Roseville did in 1995. The CPUC awarded a rate increase less than that which had been proposed by Roseville,[9] and in doing so explicitly balanced Roseville's financial needs against the potential for harmful rate shock that the CPUC thought could arise from granting the entire proposed rate increase. Yet, when Roseville follows the CPUC's lead and expresses concern about the rate shock that would result from the loss of federal high-cost support, the CPUC appears to trivialize that concern.

III. MCI Worldcom's Objections are Misplaced.

On page 2 of its Comments, MCI Worldcom states:

> "Roseville has presented no evidence that the cost model is incorrect in this case. The only justification it attempts to give for treatment as a rural carrier is that it is smaller than most of the other non-rural carriers and thus cannot achieve the economies of scale that those carriers can achieve."

[9] It is worth noting that one of the ways in which the CPUC was able to minimize the impact on consumers was to use the explicit federal support to offset costs which ratepayers would otherwise have to pay. If this support is abruptly eliminated (as the CPUC's comments in this proceeding as well as the earlier request of the Joint Board for suggestions on the phase-out of hold harmless support would appear to suggest) then, by the CPUC's own rules and earlier logic, Roseville's customers could potentially face a rate increase of $5.70 per line per month. Even if the phase-out of Hold Harmless support is spread over three years, the impact could be a rate increase of almost $2 per line per month, in each of the next three years.

However, Roseville's PFR is not based on arguments on the accuracy or inaccuracy of the Synthesis Model.[10] As discussed in the Introduction, Roseville's main concern is with the impact that the phase-out of hold-harmless support will have on Roseville and its customers. Since Roseville serves less than 200,000 lines, it receives 65% of its loop costs over 115% of the nationwide average. As demonstrated above, this makes Roseville similar to the rural LECs, and quite different from most non-rural LECs which receive only 10% of costs over 115%.

MCI Worldcom also cites average density data in an attempt to show that Roseville is more comparable to non-rural LECs than to rural LECs:

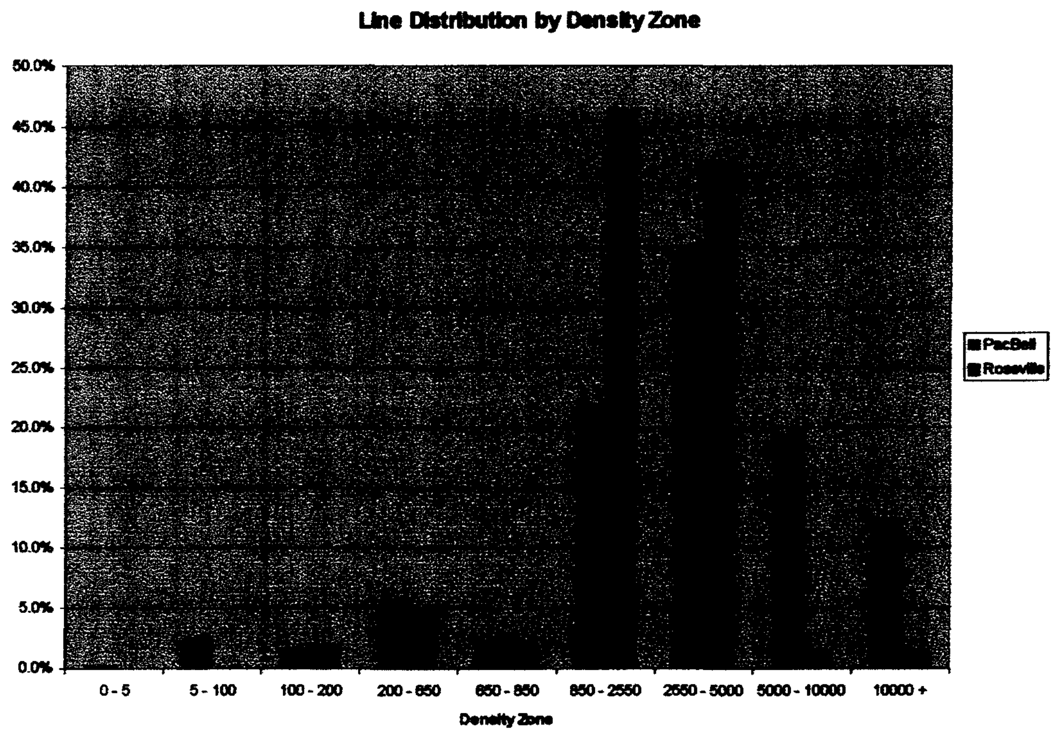
> "According to Roseville's own data, its average line density is approximately 1,500 lines per square mile. This places it well above the average for rural carriers, at 13 persons per square mile, as well as the average density of non-rural carriers, at 150 persons per square mile."

However, averages are often misleading, particularly when examining the costs of providing telephone service in a complex competitive environment. Costs tend to be relatively low in areas in close proximity to the central office, and quite high in areas many miles distant. Density also plays a role, since economies in distribution plant occur when customers are clustered together. It is this combination of distance and density that ultimately determines cost.

Most people live clustered in towns or cities. There are also some customers who live in the remote areas between towns, and (except in the most dense population corridors) there is lots of land where no one lives. As a result, a very large serving area with most customers clustered in one town in its center could still have relatively

[10] Of course, if Roseville's PFR is not granted, it may subsequently seek relief based on a showing that the non-rural Synthesis Model does not accurately model Roseville's costs.

<u>low</u> average cost per line, even though the lines per square mile would be very low. Conversely, a serving area where the average density is relatively <u>high</u> could also experience <u>higher</u> costs if the customers are uniformly disbursed throughout the serving area. Thus to examine relative cost, you must also examine the relative density groupings. The following chart was developed from the density-zone output run used by the FCC in their June, 1999 Order:



This chart contrasts Roseville's density distribution to its non-rural neighbor, Pacific Bell. While over one-third of Pacific Bell's customers are located in the top two density zones (over 5,000 lines per square mile), less than three percent of Roseville's customers are in these zones. This is very significant, since these are the density zones where costs are the lowest. It also should be noted that almost half of

Roseville's customers are in the 850-2550 lines per square mile density zone, a density pattern that might well be observed in a rural town.

In sum, the line density statistics provided by MCI says little about how the customers are clustered within a service area. Yet, it is the clustering pattern that is determinative of costs. And, as shown in the chart above, there is a significant difference between the clustering patterns for Roseville, and the clearly non-rural company Pacific Bell.

IV. Conclusion

The distinction between "rural" and "non-rural" companies set forth in the *Tenth R & O* improperly places smaller mid-sized carriers in the same category as LECs hundreds of times their size, thus basing high-cost support for such companies on models and transition mechanisms designed for carriers with significantly different cost structures and current support resources. Since companies like Roseville receives 65% of its high costs from the USF, a three year phase-out of Hold Harmless support could impact its customers with rate increases of almost $2 per line per month, in each of the next three years. In light of the harm likely to be caused as a result, and because the distinction used by the Commission is not mandated by the Act for use in connection with federal universal service, Roseville urges the Commission to revise that distinction in a manner that treats the smaller mid-sized carriers in a manner more similar to the rural LECs. Such a revision should distinguish LECs subject to the new high-cost support mechanism as those with more than 200,000 access lines in a study area, as provided in the current rules for USF.

Respectfully submitted,

ROSEVILLE TELEPHONE COMPANY

Paul J. Feldman, Esq.
FLETCHER, HEALD & HILDRETH, PLC
1300 North Seventeenth Street
11th Floor
Arlington, Virginia 22209
(703) 812-0400

Glenn H. Brown
MCLEAN & BROWN
9011 East Cedar Waxwing Dr.
Chandler, Arizona 85248
(480) 895-0063

February 22, 2000

CERTIFICATE OF SERVICE

I, Stacy R. Eveslage, a secretary in the law firm of Fletcher, Heald & Hildreth, P.L.C., hereby certify that true copies of the foregoing Reply to Opposition to and Comments on Petition for Reconsideration of Roseville Telephone Company was served this 22nd day of February, 2000, upon:

Chris Frentrup
MCI Worldcom
Senior Economist
1801 Pennsylvania Avenue, N.W.
Washington, D.C. 20006

Ellen S. Levine, Esq.
Attorneys for the People of the
State of California and the
California Public Utilities Commission
505 Van Ness Avenue
San Francisco, CA 94102

Stacy R. Eveslage

Stacy R. Eveslage