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Washington, D.C. 20554

FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)
)
Federal-State Joint Board on) CC Docket No. 96-45
Universal Service)

COMMENTS OF THE RURAL INDEPENDENT COMPETITIVE ALLIANCE
ON THE RECOMMENDATIONS OF THE RURAL TASK FORCE

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November 3, 2000

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**COMMENTS OF THE RURAL INDEPENDENT COMPETITIVE ALLIANCE
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The Rural Independent Competitive Alliance (“RICA”), by counsel, files these comments on the recommendation of the Rural Task Force (“RTF”) in this proceeding,¹ pursuant to FCC Public Notice 00J-3, released October 4, 2000.

RICA is an alliance of Competitive Local Exchange Carriers (“CLECs”) providing competitive service in rural areas of the United States. RICA members are generally affiliated with a rural incumbent local exchange carrier (“ILEC”) and compete in adjacent markets in which the ILEC is a Bell Operating Company or affiliate of a large holding company. These comments will focus on the RTF’s recommendations for changes in the Merger and Acquisition Cap.

**I. UNIVERSAL SERVICE SUPPORT SHOULD BE AVAILABLE TO SUPPORT
NEW INVESTMENT IN RURAL AREAS WHETHER CONNECTED WITH
PURCHASE OR OVERBUILDING**

**A. Universal Service Support Should Not Distort the Economics of Rural
Carriers “Make or Buy” Decisions.**

Since the passage of the Telecommunications Act of 1996 (the “1996 Act”), rural

¹*In the Matter of Federal-State Joint Board on Universal Service: Rural Task Force Recommendation to the Federal-State Joint Board on Universal Service*, CC Docket 96-45 (rel. Sept. 29, 2000) (“RTF Recommendation”).

telephone companies have had two options to respond to requests from neighboring communities to provide them with improved telecommunications service: overbuild or purchase existing facilities from the ILEC. The RTF Recommendation correctly recognizes the public interest benefits that may occur on sale of the large company exchanges to smaller companies, and proposes to correct, to some extent, the long standing hostility of the Commission to such transfers. This is all to the good, but it does not go far enough, and by itself will produce uneconomic decisions in some cases.

When a rural carrier is conducting the difficult “make or buy” decision as to how best to bring its improved service into neighboring communities, it must necessarily consider whether the differing regulatory requirements of the alternatives will have a material effect on the economics of the operation. To the extent that universal service support is available for the purchase alternative, but not for the overbuild alternative, the scales may be unnaturally tilted towards purchase when that would not be the preferable alternative for society.

B. Universal service support should be available to rural CLECs at a level comparable to that for rural ILEC acquisitions.

The solution to this potential distortion is to recognize that comparable levels of support should be provided regardless of the form that a rural carrier chooses to use to enter into areas heretofore denied modern, reliable service. As demonstrated below, the rural areas served by the large companies are the areas most in need of competitive entry. It would make no sense to adopt rules encouraging competition in the rural ILEC areas, where superior service is generally available, but discouraging it in the rural areas of the large companies where such service is not available. The federal government has made clear the goal of as wide as possible deployment of

advanced services. Without the basic infrastructure in place, advanced services will remain unavailable in rural areas.

RICA therefore proposes that CLECs which meet the definition of a rural telephone company, and receive ETC designation, be eligible for the same level of universal service support as a rural ILEC would receive upon purchase and upgrading of exchanges of non-rural carriers.

II. THE RTF CORRECTLY RECOGNIZED THE NEED FOR UNIVERSAL SERVICE SUPPORT TO NEW INVESTMENTS IN RURAL AMERICA

A. Rural America Continues to Be Underserved by Large Companies

Over the past 120 years, the ILEC industry in the United States has evolved into a structure in which virtually all urban as well as smaller market centers areas are served by large holding companies while the smallest towns and vast rural stretches are served by very small telephone companies. These small companies serve a substantial portion of the geographic area of the country but only a few percent of the population, have much lower business to residence subscriber ratios and are generally locally owned and controlled, either as cooperative or closely held corporations.

These companies have an excellent record of providing modern, efficient and reliable telecommunications services because they serve only rural areas, have had adequate access to capital (after 1949) through programs of the Rural Electrification Administration (“REA”—now Rural Utilities Service “RUS”), and have operated under regulatory cost allocation rules which allowed adequate cost recovery from both local and long distance services. By contrast, the large companies have, at least over the last 25 years or more, kept to an absolute minimum their new

investment in the rural areas they serve in reaction to increasing competitive pressure in their urban areas, and increasing earnings pressure on their publicly traded stock.

The result of this disinterest in rural America has been twofold. Some of the large companies have sold many of their rural exchanges to the existing smaller companies in the area, or to new companies focused on rural areas. The new owners of these exchanges have made substantial investments to modernize these facilities, which typically required complete rebuilding. In other areas which have not been sold, modern reliable service remains unavailable. CLASS services are typically not offered, advanced services are not even considered, and the nearest human customer service representative/service personnel of the carrier may be hundreds, or even thousands of miles away.

In most cases, the carriers serving these areas have received little or no universal support under the mechanism adopted in 1984 as a result of two factors. First, support eligibility was based upon study area average cost compared to the national average. A study area with large urban areas and even extensive rural areas generally did not have high enough cost, on average, to qualify for support. Second, to the extent it did qualify, a large company study area received a lower proportionate amount of support.

The RTF Recommendation correctly recognizes this problem and the need for revision to the universal service rules to encourage investment in these areas.² The RTF Recommendation to revise Section 54.305 of the Commission's Rules, however, focuses on only one means of achieving the necessary new investment, while in some situations there are preferable alternatives, such as the overbuild alternative described below.

²See RTF Recommendation at 29-30 & Appendix D.

B. Overbuilding, Rather than Purchase Is Often the Preferable Solution to Obtain Improvements in Telecommunications Services

As a result of the neglect of rural areas by large companies, many small rural companies have been solicited by the large companies' customers to expand their superior service into the adjacent areas. In some instances, the small companies have successfully negotiated purchase agreements with the large companies and then provided vastly improved service. It is often the case, however, that the purchase option is either not available or is not economically rational. Large companies are usually not willing to undergo the transactions costs involved in the sale of only a few exchanges, and so will consider sales only in large lots. When a small company does have an option to purchase through a consortium, the asking price is usually not only substantially above the book price of the assets, but usually well above the replacement cost, i.e., the forward looking cost. Sales at these levels may provide significant capital gains to the seller, but hinder the buyer's ability to invest in new facilities.

For this reason, many small ILECs created CLEC subsidiaries, such as the members of RICA, as the most economically effective and efficient way to respond to the requests from their neighboring communities, to extend the levels and quality of service into the areas historically served by the large companies. Because the incumbent's outside plant and switching facilities were usually old, poorly maintained and technologically obsolete, resale or unbundled network elements would not allow the rural CLEC to offer the improved grades and quality of service demanded by the communities. For this reason, most of the customers of RICA members are served by newly constructed facilities. Although less than the cost of purchasing the exchange from the incumbent and then rebuilding, this overbuilding nevertheless has required substantial

capital investment. The result of this investment has been that for the first time many residential and business customers in rural markets have access to such services as caller ID, voice mail, DSL and cable modems as well as lower rates, local customer service offices and job opportunities.³

Under the portability rules of the Commission's universal service support mechanism, the rural CLEC with ETC status is nevertheless limited to the support received by the ILEC. Upon expiration of the hold-harmless rules, this support will only be available in seven states, and then only in certain wire centers.⁴

³According to a recent survey of 23 RICA members serving 27,923 residential and 11,957 business access lines, 40 percent had brought Caller ID to rural markets for the first time; 65 percent had brought voice mail; 83 percent had brought DSL; and 35 percent had brought cable modems. On average, the 23 respondents have made capital investments of \$6.6 million in their CLEC areas and have spent over \$140 million to improve service in rural America. The survey also revealed that an average of 9.5 new jobs are created with an average of 13.73 positions projected in a year and that 73 percent of the members responding have opened a local customer service office in the markets they are serving. The average penetration rate for the respondents is 53.81 percent with the seven respondents who have been in business for more than 3 years reporting an average penetration rate of 72.14 percent.

⁴See RICA's Reply Comments filed in response to the Common Carrier Bureau's request for comment as to the Federal-State Joint Board on Universal Service's Recommended Decision for phasing down the interim hold-harmless provision of the new, forward-looking high-cost universal service support mechanism for non-rural carriers (*Federal-State Joint Board on Universal Service*, CC Docket 96-45, Recommended Decision, FCC 00J-1 (rel. June 30, 2000)) (RICA argued that hold-harmless support received by rural CLECs should be excluded from phase down for the same reasons that the Joint Board proposes not to phase down the hold-harmless support of rural ILECs that acquire exchanges from non-rural ILECs).

III. CONCLUSION

The Task Force should be commended for its diligent efforts to address the daunting task of balancing the mandate to preserve universal service while simultaneously facilitating competition in areas served by rural carriers. The Recommendation reflects serious and substantial effort to reach viable solutions by all participants. RICA requests, however, that in developing its Recommendation, the Joint Board adopt a provision that will permit CLECs which meet the definition of a rural telephone company, and receive ETC designation, to be eligible for the same level of universal service support as a rural ILEC would receive upon purchase and upgrading of exchanges of non-rural carriers. Additionally, RICA urges that provisions be inserted that would provide adequate funding to assist such rural CLECs in their efforts to overbuild in rural areas. These adjustments aimed specifically to provide needed assistance to rural CLECs would be in line with the goals of the Task Force in striking a balance in providing a fund that is "sufficient" under the provisions of the 1996 Act while insuring that the overall size of the fund is reasonable.

Respectfully submitted,

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November 3, 2000

CERTIFICATE OF SERVICE

I, Nancy Wilbourn, of Kraskin, Lesse & Cosson, LLP, 2120 L Street, NW, Suite 520, Washington, DC 20037, do hereby certify that a copy of the foregoing "Comments of the Rural Independent Competitive Alliance on the Recommendations of the Rural Task Force" was served on this 3rd day of November 2000, by first class, U.S. Mail, postage prepaid to the following parties:


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