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
	)	
Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers	)	CC Docket No. 00-256 ✓

FOURTEENTH REPORT AND ORDER, TWENTY-SECOND ORDER ON RECONSIDERATION, AND FURTHER NOTICE OF PROPOSED RULEMAKING IN CC DOCKET NO. 96-45, AND REPORT AND ORDER IN CC DOCKET NO. 00-256

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By the Commission: Chairman Powell and Commissioner Ness issuing separate statements; Commissioner Furchtgott-Roth concurring in the result.

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I. INTRODUCTION AND OVERVIEW

1. In this Order, consistent with the recommendation of the Federal-State Joint Board on Universal Service (Joint Board), we modify our rules for providing high-cost universal service support to rural telephone companies for the next five years based upon the proposals made by the Rural Task Force.[1] We find that these modified rules strike a fair and reasonable balance among the universal service principles and goals enumerated in section 254 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996.[2] As the Commission continues to develop a long-term coordinated universal service plan, this five-year plan will provide predictable levels of support so that rural carriers can continue to provide affordable service in rural America, while ensuring that consumers in all areas of the nation, including rural areas, have access to affordable and quality telecommunications services.[3]

2. The Telecommunications Act of 1996 codified the Commission's historical commitment to promote universal service to ensure that all Americans have access to affordable, quality telecommunications services. Specifically, in section 254, Congress instructed the Commission, after consultation with the Joint Board, to establish specific, predictable, and sufficient mechanisms to preserve and advance universal service.[4] Moreover, Congress articulated a national goal that consumers in all regions of the nation, including rural, insular and high cost areas, should have access to telecommunications and information services at rates that are reasonably comparable to rates charged for similar services in urban areas.

3. Consistent with the will of Congress, we have taken numerous steps over the last four

[1] *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision, FCC 00J-4 (Jt. Bd. rel. Dec. 22, 2000) (*Recommended Decision*); Letter from William R. Gillis, Chair, Rural Task Force, to Magalie Roman Salas, FCC, dated September 29, 2000 (Rural Task Force Recommendation or Recommendation). We also address proposals related to intrastate high-cost support made by the Multi-Association Group (MAG). The MAG plan is a comprehensive proposal for interstate access charge and universal service reform for non-price cap or rate-of-return carriers submitted to the Commission by four associations that represent rural carriers. *See Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers,* CC Docket No. 00-256, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, CC Docket No. 98-77, *Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket No. 98-166, Notice of Proposed Rulemaking, 16 FCC Rcd 460 (2001) (*MAG NPRM*).

[2] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (1996 Act). The 1996 Act amended the Communications Act of 1934. 47 U.S.C. §§ 151, *et seq.* (Communications Act or Act). References to section 254 in this Order refer to the universal service provisions of the 1996 Act, which are codified at 47 U.S.C. § 254 of the Act.

[3] In this Order, the terms "rural carrier" and "rural incumbent local exchange carrier" refer to incumbent local exchange carriers that meet the definition of a rural telephone company set forth in section 153(37) of the Act. 47 U.S.C. § 153(37). Under this definition, rural telephone companies are local exchange carriers that either serve study areas with fewer than 100,000 access lines or meet one of three additional criteria. We note that, "[a]lthough the Commission uses 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." *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, Tenth Report and Order, 14 FCC Rcd 20156, 20358 para. 458 (1999) (*Tenth Report and Order*).

[4] 47 U.S.C. § 254.

years to carry out these statutory directives and goals. Reforming the patchwork system of largely implicit universal subsidies that existed prior to the 1996 Act has not been an easy task. We have proceeded carefully in stages to provide interested stakeholders with an opportunity to express their competing views on how to resolve these vexing public policy issues. Our action today is an important step in completing the process begun in 1996 to reform our universal service system so that it is sustainable in an increasingly competitive marketplace. In 1997, the Commission established a comprehensive blueprint for universal service reform.[5] In 1999, we took action to ensure that the rates for supported services provided by non-rural carriers remain reasonably comparable and affordable for all Americans.[6] Today, we take action with respect to rural carriers.

4. In implementing the universal service provisions of the 1996 Act, the Joint Board and the Commission have consistently recognized that rural carriers face diverse circumstances and that "one size does not fit all" in considering universal service support mechanisms that are appropriate for rural carriers. When the Commission determined in May 1997 that universal service support should be based on the forward-looking economic cost of constructing and operating the network facilities and functions used to provide the supported services, it also determined that rural carriers would shift gradually to a forward-looking economic cost methodology.[7] The Commission wanted to allow ample time for rural carriers to adjust to any changes in support calculations. In the meantime, rural carriers would receive support based on the existing embedded cost mechanisms, as modified in the *First Report and Order*.[8]

5. The Commission recognized that the forward-looking cost mechanisms available at that time could not predict the costs of serving rural areas with sufficient accuracy.[9] Because rural carriers generally have higher operating and equipment costs, which are attributable to lower subscriber density, small exchanges, and a lack of economies of scale, the Commission recognized that additional effort would be needed to develop a forward-looking mechanism appropriate for rural carriers. To assist in this challenge, the Commission encouraged the Joint Board to establish a task force representing a broad range of interests.[10] To that end, the Joint Board established the Rural Task Force, which was comprised of individuals representing rural telephone companies, competitive local exchange carriers, interexchange carriers, wireless providers, consumer advocates, and state and federal agencies, to assist it in making its recommendation to the Commission.[11]

6. After exhaustive deliberations and considerable effort, including issuing six white papers, the Rural Task Force submitted its Recommendation to the Joint Board on September 29, 2000.[12]

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[5] *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776 (1997) (*First Report and Order*) (subsequent history omitted).

[6] *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, 14 FCC Rcd 20432, 20439 (1999) (*Ninth Report and Order*), *pets. for review pending sub nom., Qwest Corp. v. FCC*, 10th Cir. No. 99-9546 and consolidated cases (1999).

[7] *First Report and Order*, 12 FCC Rcd at 8899 para. 224, 8936 para. 294.

[8] *Id.* at 8937-45 paras. 297-313.

[9] *Id.* at 8935 para. 293.

[10] *See id.* at 8917 para. 253.

[11] *See Federal-State Joint Board on Universal Service Announces the Creation of a Rural Task Force*, CC Docket No. 96-45, Public Notice, 12 FCC Rcd 15752 (Jt. Bd. 1997) (*Rural Task Force 1997 Public Notice*); *Federal-State Joint Board on Universal Service Announces Rural Task Force Members*, CC Docket No. 96-45, Public Notice, FCC 98J-1 (Jt. Bd. 1998) (*Rural Task Force 1998 Public Notice*).

[12] *See* Rural Task Force Recommendation. The Joint Board had requested the Rural Task Force's recommendations no later than nine months after the implementation of the forward-looking high-cost mechanism (continued....)

Rather than attempting to modify the Commission's forward-looking cost mechanism that currently is used to determine non-rural support, the Rural Task Force proposed modifications to the current embedded cost system for a five-year period.[13] The consensus reached by the Rural Task Force members reflects the result of a process in which strongly held opposing views were aired, argued, and eventually accommodated. In recommending a modified embedded cost mechanism, the Rural Task Force attempted to "strike a careful balance between the need to provide a fund that is 'sufficient' under the provisions of the 1996 Act while insuring that the overall size of the fund is reasonable."[14]

7. After reviewing the Rural Task Force's proposal to modify the current embedded cost system for rural carriers, the Joint Board submitted its recommendation to the Commission on December 22, 2000. The Joint Board encouraged the Commission to take advantage of the consensus achieved by the diverse interests represented on the Rural Task Force and use the Rural Task Force Recommendation as a foundation for implementing a universal service plan for rural carriers for the next five years. The Joint Board also recognized that this is an interim plan. To that end, the Joint Board recommended that the Commission undertake a comprehensive review of the high-cost support mechanisms for both rural and non-rural carriers to ensure that both mechanisms function efficiently and in a coordinated fashion. The Joint Board urged the Commission to use this five year period to develop a long-term universal service plan that better targets support to rural carriers serving the highest cost areas.[15]

8. Based on the record before us, we find that adopting a modified embedded cost mechanism for rural carriers for a five-year period strikes a fair and reasonable balance among the goals and principles enumerated in section 254 of the Act. As the Joint Board suggested, we intend to develop over the next few years a long-term universal service plan for rural carriers that is better coordinated with the non-rural mechanism. In particular, we intend to develop a long-term plan that better targets support to carriers serving high-cost areas, while at the same time recognizing the significant differences among rural carriers, and between rural and non-rural carriers.

9. Throughout this proceeding, we have grappled with complex issues and balanced competing interests. We are mindful of the adage "Let not the perfect be the enemy of the good." The 1996 Act charged the Commission with the task of resolving the difficult issues surrounding universal service, consistent with the principles enunciated in section 254. We take action today that is consistent with the statutory requirements, recognizing that views may differ on the best policies to effectuate those requirements. In balancing the competing interests, we draw heavily from the recommendations of the Rural Task Force to the Joint Board, which exhaustively considered the issues before us over a two-year period. We build upon and modify those recommendations only in those areas where we conclude that implementation as proposed may have adverse consequences.

10. We conclude that the plan we adopt today will preserve and advance universal service,

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for non-rural carriers, which became effective on January 1, 2000. *See Rural Task Force 1997 Public Notice*. As explained *infra*, the Joint Board established the Rural Task Force for the purpose of making recommendations to the Joint Board regarding an appropriate forward-looking high-cost support mechanism for rural carriers. After receiving the Rural Task Force's recommendation, the Joint Board recommended that we base modifications to the high-cost support mechanism for rural carriers on the Rural Task Force recommendation. We will, for ease, refer to the Rural Task Force's recommendation interchangeably with the Joint Board's recommendation.

[13] *See* Rural Task Force Recommendation at 17-19; *Recommended Decision* at para. 13.

[14] Rural Task Force Recommendation at 4.

[15] On January 12, 2001, the Commission sought comment on the Joint Board's Recommended Decision. *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Further Notice of Proposed Rulemaking, FCC 01-8 (rel. Jan. 12, 2001) (*Further Notice*).

consistent with the goals and principles set forth in section 254 of the Act, and encourage competition in high-cost areas, consistent with the competitive goals of the 1996 Act. In particular, we find that adoption of the modified embedded cost mechanism is consistent with our obligation to ensure that the support provided to rural carriers over the next five years is specific, predictable, and sufficient. In addition, we find that the mechanism is consistent with the goals of section 254 to ensure that consumers in rural, insular, and high-cost areas have access to telecommunications services at rates that are affordable and reasonably comparable to rates charged for similar services in urban areas. We find further that the flexible plan for disaggregating and targeting support adopted in this Order will facilitate competitive entry into high-cost areas, bringing the benefits of competition to consumers in rural areas.

11. The plan adopted today will provide certainty and stability for rural carriers for the next five years, enabling them to continue to provide supported services at affordable rates to American consumers. While we take an important step today on rural universal service reform, our task is not done. Our universal service rules cannot remain static in a dynamic marketplace. As we move forward, we will continue to refine our policies to preserve and advance universal service, consistent with the mandates in section 254.

II. EXECUTIVE SUMMARY

12. In this Order, we take the following actions in response to the Rural Task Force's recommended reforms to rural high-cost universal service support and the proposals made by the Multi-Association Group (MAG) relating to this mechanism:

- We adopt the Rural Task Force's recommendation to re-base the high-cost loop support fund for rural telephone companies and retain an indexed cap on the fund. We conclude that re-basing the indexed fund will ensure that rural carriers are able to continue providing supported services at affordable and reasonably comparable rates during the transition to a more permanent high-cost support mechanism for rural carriers.

- We adopt a "rural growth factor" that allows the high-cost loop support fund to grow based on annual changes in the Gross Domestic Product-Chained Price Index (GDP-CPI) and the total number of working loops of rural carriers. We find that allowing the fund to grow in this fashion over the next five years will enable rural carriers to make prudent investments in rural America.

- We adopt the Rural Task Force's recommendation to freeze the national average loop cost at \$240.00. We conclude that freezing the national average loop cost will provide rural carriers with greater certainty as to their eligibility for high-cost loop support.

- We adopt a modified version of the Rural Task Force's proposal as it relates to corporate operations expenses. We revise the corporate operations expense limitation calculation so that the dollar values in the formula are re-based and indexed by the GDP-CPI.

- We also raise the minimum cap in the revised corporate operations expense limitation formula. Specifically, we permit small rural carriers to receive support for corporate operations expenses of up to \$600,000 or amounts derived from the revised corporate operations expense formula, whichever is greater. We find that raising the minimum cap from \$300,000 to \$600,000 will enable small rural carriers to receive more support for corporate operations expenses without having to file for waiver of our rules.

- We adopt a modified version of the Rural Task Force's proposed "safety net additive" so that a carrier will receive support for its incremental expense adjustment associated with new investment, rather than 50 percent of the difference between capped and uncapped support in a given year as proposed by the Rural Task Force. By modifying safety net support in this way, we ensure that carriers that meet the threshold requirement for eligibility will receive support for their incremental investment, but do not recover more than the costs incurred as a result of the additional investment.

- Consistent with the Rural Task Force's recommendation, we retain section 54.305 of the Commission's rules, which provides that a carrier acquiring exchanges from an unaffiliated carrier shall receive the same per-line levels of high-cost support for which the acquired exchanges were eligible prior to their transfer. We modify the rule, however, to provide a "safety valve" that provides support for additional investment made in the acquired exchanges.

- We decline at this time to adopt the Rural Task Force's proposal to freeze high-cost loop support upon competitive entry in rural carrier study areas. The proposal may be of limited benefit in serving its intended purpose of preventing excessive fund growth, and in some circumstances might increase high-cost loop support levels. We also conclude that the Rural Task Force's proposal would be administratively burdensome and may have the unintended consequence of discouraging investment in rural America. In the attached Further Notice of Proposed Rulemaking, we invite comment on possible alternative measures.

- We address the Rural Task Force's concerns regarding frequency of reporting and the lag in support in study areas with competitive eligible telecommunications carriers. First, we require all eligible telecommunications carriers serving such areas to report updated line counts on a regular quarterly basis. Second, we clarify that competitive eligible telecommunications carriers may submit data and receive high-cost loop support on a regular quarterly basis.

- We adopt, with certain modifications, the three paths for the disaggregation and targeting of high-cost universal service support proposed by the Rural Task Force. We also adopt the general requirements that the Rural Task Force proposed for all disaggregation plans. We find that providing rural carriers flexibility in the methods of disaggregation and targeting is a reasonable approach to address the significant diversity among such carriers and will facilitate competitive entry in rural areas.

- We find that the Rural Task Force's proposed framework, with certain modifications, shall remain in place for five years and implementation shall begin as of July 1, 2001.

- We adopt the use of a wireless mobile customer's billing address as the basis for determining the customer's location for purposes of delivering high-cost universal service support.

- We conclude that states should file annual certifications with the Commission to ensure that eligible telecommunications carriers providing service in the service area of a rural carrier use universal service support "only for the provision, maintenance and upgrading of facilities and services for which the support is intended" consistent with section 254(e) of the Act.

- Consistent with the Rural Task Force's recommendation, the Joint Board on Universal Service is currently considering the definition of supported services. We agree with the Rural Task Force that our universal service policies should not inadvertently create barriers to the provision of access to advanced services, and believe that our current universal service system does not create such barriers. We commit to further consideration of the Rural Task

Force's proposed "no barriers to advanced services" policy in the future.

- We find the Rural Task Force's recommended principles for access reform to be reasonable and generally consistent with prior Commission actions to reform the access rate structure of price cap carriers. These principles will aid our consideration of access charge reform issues in the pending MAG proceeding. We recognize the importance of completing access reform for rate-of-return carriers and intend to act expeditiously to resolve issues raised in the MAG proceeding.

III. BACKGROUND

A. High-Cost Support for Rural Carriers

13. The purpose of high-cost universal service support is to help provide access to telecommunications service in areas where the cost of such service otherwise might be prohibitively expensive.[16] Historically, this purpose has been achieved both through explicit monetary payments and implicit support flows to enable carriers to serve high-cost areas at below-cost rates.[17] Currently, three federal universal service mechanisms provide high-cost support for rural carriers. High-cost loop support, with which we are principally concerned here, provides support based on embedded costs averaged over entire study areas.[18] Carriers receive high-cost loop support for a variable percentage of their unseparated loop costs, depending on the number of loops they serve and the degree to which their costs exceed the national average cost per loop.[19] High-cost loop support for rural carriers is subject to an indexed cap, which limits total support to the previous year's total, increased by the rate of annual loop growth for all carriers.[20] Rural carriers also receive federal high-cost support through the Long Term Support (LTS) and Local Switching Support (LSS) mechanisms.[21] These three mechanisms

[16] *See Ninth Report and Order*, 14 FCC Rcd at 20439 para. 12.

[17] *See id.* at 20441 para. 15 ("In contrast to explicit support, some state rate designs and, to a lesser extent, the federal interstate access charge system, have provided implicit high-cost support flowing from (1) urban areas to rural areas; (2) business customers to residential customers; (3) vertical services to basic service; and/or (4) long distance service to local service").

[18] The term "embedded costs" refers to a carrier's historic costs, as reflected in its books. A study area is a geographic segment of a carrier's telephone operations, generally corresponding to its entire service territory within a state. The Commission froze all study area boundaries effective November 15, 1984. *See* 47 C.F.R. Part 36, Appendix—Glossary.

[19] *See* 47 C.F.R. §§ 36.601, *et. seq.*; *First Report and Order,* 12 FCC Rcd at 8891-92 paras. 209-11. We define a loop as "the connection between the telephone company's central office and the customer's premises[,]" and loop cost as the fixed cost of this connection. *First Report and Order*, 12 FCC Rcd at 8891 nn.523, 525. The term "unseparated" refers to the jurisdictional separations process which divides between the state and federal jurisdictions the costs of those portions of carriers' telephone plant that are used for intrastate and interstate services. High-cost loop support provides support only for the portion of a carrier's total costs allocated to the intrastate jurisdiction. Specifically, carriers with 200,000 or fewer working loops receive support equal to 65 percent of the portion of their unseparated loop costs greater than 115 percent but less than or equal to 150 percent of the national average, and 75 percent of the portion of their unseparated loop costs greater than 150 percent. For carriers with over 200,000 working loops, the formula is similar, but with reduced levels of support. For example, a carrier with over 200,000 loops reaches the 75 percent support level only for costs that exceed 250 percent of the national average. The national average is calculated based on the loop costs of both rural and non-rural carriers.

[20] *See* 47 C.F.R. Part 36, Subpart F; *First Report and Order*, 12 FCC Rcd at 8929-30 paras. 281-82.

[21] LTS provides support for the interstate loop costs of rate-of-return carriers (typically small, rural carriers) that participate in the National Exchange Carrier Association (NECA) common line pool, and LSS (formerly DEM (continued....)

provide approximately $1.617 billion in annual universal service support to over 1,300 rural carriers.[22]

B. The Act

14. In the 1996 Act, Congress established principles for the preservation and advancement of universal service in a competitive telecommunications environment. In particular, section 254 of the Act provides that consumers in all regions of the nation, including consumers in rural, insular, and high-cost areas, should have access to telecommunications services at rates that are affordable and reasonably comparable.[23] Section 254 also provides that federal universal service support mechanisms should be specific, predictable, and sufficient to preserve and advance universal service.[24] The Commission adopted the additional principle that federal support mechanisms should be competitively neutral, neither unfairly advantaging nor disadvantaging particular service providers or technologies.[25] We have concluded that federal universal service policies should strike a fair and reasonable balance among these principles and goals enumerated in section 254.[26] In so doing, we have held that promotion of any one goal or principle should be tempered by a commitment to ensuring the advancement of each of the principles enumerated above.[27]

C. Prior Joint Board and Commission Actions

15. With passage of the 1996 Act, particularly section 254, the Commission took a fresh look at its universal service support mechanisms. Based on the recommendations of the Joint Board, the Commission began reforming its high-cost support mechanisms in its *First Report and Order* released on May 8, 1997.[28] Among other things, the Commission concluded that federal universal service support for all carriers should be based on the forward-looking economic cost of constructing and operating the network used to provide the supported services, rather than each carrier's embedded costs.[29] The Commission explained that support based on forward-looking economic costs provides sufficient support without giving carriers an incentive to inflate their costs or to refrain from efficient cost cutting.

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Weighting) is available to support a portion of the switching costs of carriers with 50,000 or fewer lines. 47 C.F.R. §§ 36.125(b), 54.301, 54.303. The Commission removed LTS and LSS from the interstate access charge system in 1998. The LTS and LSS support programs now are funded from collections from all providers of interstate telecommunications services made on an equitable and non-discriminatory basis. *See generally Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Fourth Order on Reconsideration, *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge*, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, Report and Order, 13 FCC Rcd 5318, 5343-45 paras. 40-41, 5352-54 paras. 56-58 (1998) (*Fourth Order on Reconsideration*); *see also Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Thirteenth Report and Order and Further Notice of Proposed Rulemaking, FCC 00-428 at paras. 6-9 (rel. Dec. 8, 2000).

[22] *See* Federal Universal Service Support Mechanisms Fund Size Projections and Contribution Base For the Third Quarter 2001, Appendix HC 2 (Universal Service Administrative Company, May 2, 2001).

[23] 47 U.S.C. § 254(b)(3).

[24] *Id.* § 254(b)(5).

[25] *First Report and Order*, 12 FCC Rcd at 8801-03 paras. 46-51; *see* 47 U.S.C. § 254(b)(7).

[26] *First Report and Order*, 12 FCC Rcd at 8803 para. 52. The 1996 Act also requires the Commission to consult with the Joint Board in implementing section 254. *See* 47 U.S.C. § 254(a).

[27] *First Report and Order*, 12 FCC Rcd at 8803 para 54.

[28] *Id.* at 8780-81 paras. 1-3.

[29] *See id.* at 8899-901 paras. 224-229.

16. Although the Commission generally concluded that universal service support should be based on forward-looking economic costs rather than embedded costs, at the request of the Joint Board and rural carriers it proceeded initially with reform of the high-cost support mechanism for non-rural carriers.[30] The new, forward-looking mechanism for non-rural carriers became effective on January 1, 2000.[31] With regard to rural carriers, the Commission agreed with the Joint Board that, compared to the large non-rural carriers, "rural carriers generally serve fewer subscribers, serve more sparsely populated areas, and generally do not benefit as much from economies of scale and scope. For many rural carriers, universal service support provides a large share of the carriers' revenues, and thus, any sudden change in the support mechanisms may disproportionately affect rural carriers' operations."[32] Accordingly, the Commission stated that it would not implement a forward-looking high-cost support mechanism for rural carriers before January 1, 2001, and only after selecting an appropriate mechanism based on recommendations from the Joint Board and a task force appointed by the Joint Board.[33] In this regard, the Commission agreed with the state Joint Board members that a task force "should provide valuable assistance in identifying the issues unique to rural carriers and analyzing the appropriateness of proxy cost models for rural carriers."[34]

D. Rural Task Force Recommendation

17. The Rural Task Force members were appointed by the Joint Board in July 1998, and deliberated for over two years before presenting their Recommendation to the Joint Board on September 29, 2000.[35] These deliberations included 12 meetings and 28 conference calls, as well as numerous sub-group calls.[36] The foundation for the Recommendation is a series of six white papers addressing, among other things, the differences between rural and non-rural carriers, and the appropriateness of using the Commission's forward-looking economic cost model for non-rural carriers to calculate support for rural carriers.[37] The Recommendation represents the consensus of individual Rural Task Force members, who work for a broad range of interested parties, often with competing interests, including rural telephone companies, competitive local exchange carriers, interexchange carriers, wireless providers, consumer advocates, and state and federal government agencies.[38] The Rural Task Force offered its Recommendation as an integrated package, and asked that it be adopted without modification. It urged that the Recommendation be implemented immediately and remain in place over a five-year period. The Rural Task Force's specific proposals are discussed in detail below. Here, we briefly summarize the

[30] *See id.* at 8936 para. 294.

[31] *See Ninth Report and Order*, 14 FCC Rcd at 20439 para. 11.

[32] *First Report and Order*, 12 FCC Rcd at 8936 para. 294.

[33] *Id.* at 8917 para. 252-53; *see also id.* at 8936 para. 294.

[34] *Id.* at 8917 para. 253; *see also id.* at 8918 para. 255; *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Second Recommended Decision, 13 FCC Rcd 24744, 24758 para. 30 (Jt. Bd. 1998).

[35] *See Rural Task Force 1998 Public Notice*; Rural Task Force Recommendation. As stated above, the Joint Board had requested the Rural Task Force's recommendations no later than nine months after the implementation of the forward-looking high-cost mechanism for non-rural carriers, which became effective on January 1, 2000. *See Rural Task Force 1997 Public Notice.*

[36] *See* Rural Task Force Recommendation at Appendix B.

[37] *See id.* at 6. The six Rural Task Force white papers are available on the Rural Task Force's web site at <http://www.wutc.wa.gov/rtf>.

[38] *See* Rural Task Force Recommendation at 6 ("This approach is pragmatic, and it is intended to deliver to the Joint Board a package of recommendations with the potential of being implemented promptly and without legal challenge from affected parties.").

Recommendation.

18. The Rural Task Force recommended against use of the Commission's forward-looking high-cost mechanism for non-rural carriers to calculate high-cost support for rural carriers.[39] Instead, it recommended the use over the next five years of a modified version of the current high-cost loop support mechanism used for rural carriers. The Rural Task Force's proposed modifications to the high-cost loop support mechanism include various upward adjustments to current limits on universal service support for rural carriers. Specifically, the Rural Task Force proposed that: (a) the indexed cap on high-cost loop support and the corporate operations expense limitation be recomputed as if they had not been in effect for the calendar year 2000;[40] (b) a "safety net additive" mechanism be created to provide above-the-cap support for carriers with over 14 percent growth in telecommunications plant in service on a per-line basis;[41] and (c) a "safety valve" mechanism be created to provide additional support for "meaningful new investments" in exchanges acquired by rural carriers.[42] The Rural Task Force also recommended that, once a competitive eligible telecommunications carrier initiates service in a study area served by a rural carrier, per-line support within the study area be fixed and subsequently adjusted for growth in lines and inflation rather than changes in cost.[43]

19. In addition, the Rural Task Force recommended the use of a new annual index or "rural growth factor" to adjust the cap on high-cost loop support, the corporate operations expense limitation, and fixed per-line support in competitive study areas on a going-forward basis.[44] The rural growth factor would be the sum of annual line growth for rural carriers and a general inflation factor (Gross Domestic Product-Chained Price Index). Under the Rural Task Force's proposal, safety net additive support, support for acquired exchanges, and safety valve support, as well as support for competitive eligible telecommunications carriers, would be excluded from the indexed cap on high-cost loop support. The Rural Task Force provided an example of a safety valve mechanism, in which safety valve support would be limited to five percent of the overall indexed cap on high-cost loop support.[45]

20. The Rural Task Force also suggested certain other reforms. It proposed that rural carriers be permitted to elect, within nine months of the effective date of the proposed new rules, whether and how to disaggregate and target universal service support on a per-line basis.[46] It recommended adoption of a "no barriers to advanced services" policy, and identified principles for replacing any implicit support in interstate access charges with explicit universal service support.[47] Furthermore, it

[39] *See id.* at 20. The Rural Task Force emphasized that its Recommendation applies only to rural, insular, and high-cost areas served by *rural carriers*, and not to areas served by non-rural carriers. *See id.* at 18.

[40] *Id.* at 24-25, 27-29. The corporate operations expense limitation limits the amount of such expenses that a rural carrier may recover through high-cost loop support. *See* 47 C.F.R. § Part 36, Subpart F; *First Report and Order*, 12 FCC Rcd at 8930-32 paras. 283-85.

[41] Rural Task Force Recommendation at 27.

[42] *Id.* at 29-30; *see* 47 C.F.R. § 54.305 (limiting universal service support for acquired exchanges to the per-line support received by the seller).

[43] Rural Task Force Recommendation at 25-27.

[44] *Id.* at 25, 26, 28.

[45] *Id.* at Appendix D.

[46] *Id.* at 33-36.

[47] *Id.* at 22-23, 30-32. As indicated above, the Commission is now considering the comprehensive MAG proposal for interstate access charge and universal service reform for rate-of-return carriers. *See supra* n.1; *see also infra* paras. 202-205.

recommended that the Commission delegate to the states responsibility for oversight of rural carriers' compliance with section 254(e) of the 1996 Act, in a manner similar to that adopted for non-rural carriers.[48] Finally, the Rural Task Force recommended that the Commission address a number of issues, such as stranded costs and the interval between the provision of service and receipt of support, regarding which it did not reach agreement or did not formulate specific proposals.[49]

E. Joint Board Recommended Decision

21. As noted above, the Rural Task Force presented its Recommendation to the Joint Board on September 29, 2000. The Joint Board issued a public notice requesting written comments from interested parties, and held an *en banc* hearing regarding the Recommendation in November 2000.[50] The Joint Board submitted its *Recommended Decision* to the Commission on December 22, 2000.

22. In its *Recommended Decision*, the Joint Board concluded that the Rural Task Force Recommendation "presents a good foundation for implementing a rural universal service plan."[51] It stated that the Rural Task Force plan would provide rural carriers with stability for planning their investments over the next several years, while seeking to encourage competition in high-cost areas.[52] It also observed that the Rural Task Force's proposed upward adjustments to limits on universal service support for rural carriers are "generally designed to provide carriers serving rural areas with increased incentives to invest in new infrastructure and technologies."[53] The Joint Board remarked that the range of comments it received—from rural carriers that argued the plan would provide too little support to state commissions and other carriers that argued it would provide too much—were "consistent with a recommendation that is a consensus proposal put forth by representatives of disparate interests."[54] The Joint Board encouraged the Commission "to take advantage of this opportunity to craft a rural universal service plan that enjoys widespread support among diverse interests."[55]

23. In addition, the Joint Board observed that the Rural Task Force's proposals to modify the Commission's rules might raise implementation issues that the Commission would have to address.[56] It

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[48] Rural Task Force Recommendation at 32-33; *see* 47 C.F.R. § 54.313; *Ninth Report and Order*, 14 FCC Rcd at 20481-88 paras. 93-110. Section 254(e) provides that carriers shall use universal service support "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended." 47 U.S.C. § 254(e).

[49] Rural Task Force Recommendation at 38-39.

[50] *Federal-State Joint Board on Universal Service To Hold En Banc Hearing November 13, 2000 on the Rural Task Force Recommendation for Universal Service Reform for Rural Carriers*, CC Docket No. 96-45, Public Notice, 15 FCC Rcd 22149 (Jt. Bd. 2000). The *en banc* hearing took place at the National Association of Regulatory Utility Commissioners conference in San Diego, California, where the Joint Board heard testimony from a diverse group of participants including rural and non-rural local exchange carriers, contributors to the federal universal service support mechanisms, consumer groups, and state and federal regulators.

[51] Rural Task Force Recommendation at para. 13.

[52] *See id.* at para. 11. Specifically, the Joint Board stated that the Rural Task Force plan seeks to encourage competitors to enter high-cost areas by proposing a flexible system for disaggregating support to establish the portable per-line support amount available to all eligible telecommunications carriers. *Id.*

[53] *Id.*

[54] *Id.* at para. 12.

[55] *Id.* at para. 10.

[56] *Id.* at para. 14.

highlighted specific issues in connection with the proposals for a safety valve mechanism, fixed per-line support in competitive study areas, and safety net additive support.[57] With regard to access charge reform, the Joint Board recognized that the access charge issues raised by the Rural Task Force and the MAG plan are interstate in nature and, therefore, are properly before the Commission.[58] It urged the Commission, however, to ensure that the Joint Board remains actively involved in review of those aspects of the MAG plan that relate to universal service. Finally, the Joint Board recommended future steps for consideration of an appropriate universal service mechanism to succeed the Rural Task Force plan, urging the Commission "to use the transitional period during which a modified embedded cost mechanism is in place to develop a long-term universal service plan that better targets support to rural companies serving the highest cost areas, while at the same time recognizing the significant distinctions among rural carriers and between rural and non-rural carriers."[59]

IV. DISCUSSION

A. Consistency with Principles of the Act

24. Based on the record before us, we conclude that the Rural Task Force plan that we adopt today will preserve and advance universal service, consistent with the goals and principles set forth in section 254 of the Act, and encourage efficient competition in high-cost areas, consistent with the competitive goals of the 1996 Act. In particular, we find that adoption of the modified embedded cost mechanism is consistent with our obligation to ensure that the support provided to rural carriers over the next five years is specific, predictable, and sufficient. In addition, we find that this mechanism is consistent with the principles and goals of section 254 to ensure that consumers in rural, insular, and high-cost areas have access to telecommunications services at rates that are affordable and reasonably comparable to rates charged for similar services in urban areas. We find further that the flexible plan for disaggregating and targeting support adopted in this Order will facilitate competitive entry into high-cost areas, bringing the benefits of competition to consumers in rural areas.[60]

25. We find that continuing to base support for rural carriers on embedded cost for the next five years is a reasonable and prudent approach to take in light of the record before us. The present record fails to provide the analysis necessary to permit a transition of rural carriers to a forward-looking high-cost support mechanism.[61] Before we could transition to such a mechanism, it would need to be fully analyzed and considered. Even commenters who urge the Commission to move toward a forward-looking support methodology for rural carriers as soon as possible recognize the need for additional time to develop an appropriate mechanism.[62] In light of the diversity among rural carriers, and based on our experience in developing the forward-looking high-cost support mechanism for non-rural carriers, we find that five years is a reasonable amount of time to maintain the Rural Task Force plan in place, while we consider long-term solutions. In the meantime, providing support based on embedded costs will provide important certainty to rural carriers, which generally receive a greater proportion of their revenues from universal service support mechanisms than non-rural carriers. Accordingly, we conclude that the Rural Task Force plan will provide specific and predictable support to rural carriers over the next five years.

[57] *See id.* at paras. 15-19.

[58] *Id.* at para. 20.

[59] *Id.* at para. 21.

[60] *See infra* discussion at section IV.D.

[61] *See* Ad Hoc Telecommunications User Committee Comments at 9-10; California Commission Comments at 3.

[62] *See, e.g.*, WorldCom Comments at 3; Ad Hoc Telecommunications User Committee Reply Comments at 5-6.

26. In addition, we find that the modified embedded cost mechanism will provide sufficient support for purposes of section 254 of the Act, consistent with the goal of ensuring that consumers in rural, insular, and high-cost areas have access to telecommunications services at rates that are affordable and reasonably comparable to rates charged for similar services in urban areas. The record developed on the sufficiency issue reflects the opposing viewpoints of those receiving support from the fund and those contributing to it. Many commenters representing the interests of rural telephone companies argue that universal service support for rural carriers must be based on embedded costs to be consistent with section 254's sufficiency requirement.[63] Some argue explicitly that the existing and proposed caps on the high-cost loop fund violate this requirement and, by implication, that any mechanism that does not permit full recovery of embedded costs also would violate the Act.[64] Other commenters, namely contributors to the fund and net payor states, oppose any increases in support for rural carriers. They argue that the Rural Task Force has not demonstrated that the current level of rural high-cost support is insufficient, and that sufficiency requires that the universal service support mechanisms provide no more support than is necessary.[65] Notably, although a number of commenters argue generally that the Rural Task Force plan would provide support that is either inadequate or excessive, neither side of the debate has proffered specific evidence supporting their positions.[66]

27. Determining whether support is "sufficient" for purposes of the Act is not a precise exercise: there is a range of funding levels that may be deemed sufficient. As the Fifth Circuit has observed, section 254(e) is ambiguous as to what constitutes "sufficient" support.[67] Thus, the Commission must use its expertise and informed judgement to make a reasonable determination as to what constitutes "sufficient" support. The Fifth Circuit has provided guidance, however. Rejecting challenges by rural telephone companies that, among other things, the continued imposition of the overall cap on high-cost loop support and the corporate operations expenses limitation violated the Act, the court stated that "[s]o long as there is sufficient and competitively-neutral funding to enable all customers to receive basic telecommunications services, the FCC has satisfied the Act and is not further required to ensure sufficient funding of every local telephone company."[68] The court also cautioned that

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[63] *See, e.g.,* Alaska Tel. Assn. Comments at 2-3; NECA Reply Comments at 1-2.

[64] *See, e.g.,* Interstate Telecom Group Comments at 6; NTCA Comments at 3.

[65] *See, e.g.,* NYDPS at 4-5; WorldCom Comments at 2; Ad Hoc Telecommunications User Committee Reply Comments at 12-13. Some commenters also argue that support based on embedded costs may include costs associated with advanced services and other services that are not included in the Commission's definition of universal service. *See, e.g.,* California Commission Comments at 6; Illinois Commission Comments at 5; WorldCom Comments at 3.

[66] We note that the Maine and Vermont Commissions offer anecdotal evidence that specific carriers receive too little and/or too much support. *See* Maine and Vermont Commissions Comments at 6, 9, 13. As discussed below, their arguments are geared primarily towards better harmonization of the high-cost support mechanisms for rural and non-rural carriers, and the Commission will consider their arguments in the context of its comprehensive review of the rural and non-rural high-cost support mechanisms.

[67] *Texas Office of Public Utility Counsel v. FCC,* 183 F.3d 393, 425-26 (5th Cir. 1999); *Alenco Communications, Inc. v. FCC,* 201 F.3d 608, 620 (5th Cir. 2000).

[68] *Alenco Communications, Inc. v. FCC,* 201 F.3d at 619 ("[P]etitioners' sufficiency challenge fundamentally misses the goal of the Act. The Act does *not* guarantee all local telephone service providers a sufficient return on investment; quite to the contrary, it is intended to introduce competition into the market. Competition necessarily brings the risk that some telephone service providers will be unable to compete. The Act only promises universal service, and that is a goal that requires sufficient funding of *customers*, not *providers*.")

"excessive funding may itself violate the sufficiency requirements of the Act."[69] Thus, in crafting universal service policies and programs, the Commission must strike a fair and reasonable balance among the goals and principles of the Act, and consider both the adequacy of support and the burden on contributors.[70]

28. We find that the modified embedded cost mechanism that we adopt in this Order strikes the appropriate balance at this time. In reaching this conclusion, we reject the contention that no increase in current high-cost loop support levels is warranted. In 1997, when the Commission decided to continue using an embedded cost mechanism to determine high-cost loop support for rural carriers pending permanent reform, it declined to adopt a Joint Board recommendation to freeze support for rural carriers at then-current levels.[71] In addition, the Commission did not anticipate that the embedded cost mechanism for rural carriers would be in place for this long. As stated above, there is a range of funding levels that could be deemed sufficient for purposes of the Act, and the Rural Task Force proposal is the product of the consensus of divergent interests. At this time, we find that it is reasonable to modify the high-cost loop support levels for rural carriers established in 1997 to account for changes in costs and technology, and to ensure that rural carriers can maintain existing facilities and make prudent facility upgrades until such time as a long-term rural plan is adopted. Based on the estimates provided by the Rural Task Force and the Joint Board, we estimate that the modified embedded cost mechanism will result in an increase in rural carrier support of approximately $1.26 billion over the five-year period.[72] We anticipate that any increases in the universal service contribution factor as a result of such increases will be modest, ranging from two-tenths to four-tenths of one percent.[73]

29. We also reject the assertions of several commenters, notably state commissions, that any universal service support mechanism should provide each area no more than the amount of support

[69] *Id.* ("Because universal service is funded by a general pool subsidized by all telecommunications providers – and thus indirectly by customers – excess subsidization in some cases may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market.").

[70] *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d at 412; *Alenco Communications, Inc. v. FCC*, 201 F.3d at 620.

[71] *First Report and Order*, 12 FCC Rcd at 8939 para. 300. The Commission agreed with the state members of the Joint Board that "rural carriers may require a greater amount of support than fixed support mechanisms would provide, ... [i]n order to maintain existing facilities and make prudent facility upgrades until such time as . . . forward-looking support mechanisms are in place." *Id.*

[72] *See* Letter from William R. Gillis, Chair, Rural Task Force, to Magalie Roman Salas, FCC, dated November 10, 2000, at Attachment 2; *Recommended Decision* at para. 11 & n.32.

[73] The contribution factor for the second quarter of 2001 was approximately 6.88 percent. *See Proposed Second Quarter 2001 Universal Service Contribution Factor*, CC Docket No. 96-45, Public Notice, DA 01-614 (rel. Mar. 9, 2001). Future changes in the overall amount of federal universal service support and changes in the contribution revenue base may impact these projections. For example, the Commission recently sought comment on proposals to streamline and reform the manner in which the Commission assesses contributions to the federal universal service mechanisms. *See Federal-State Joint Board on Universal Service, 1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms, Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans With Disabilities Act of 1990, Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size, Number Resource Optimization, Telephone Number Portability*, CC Docket Nos. 96-45, 98-171, 90-571, 92-237, 99-200, 95-116, Notice of Proposed Rulemaking, FCC 01-145 (rel. May 7, 2001).

needed to enable the relevant state to ensure reasonably comparable rates among states.[74] These commenters argue, either expressly or implicitly, that because support under the modified embedded cost mechanism will be determined at the study-area level, and not at the state level consistent with the approach of the forward-looking mechanism for non-rural carriers adopted in the *Ninth Report and Order*, the modified embedded cost mechanism will provide excessive support to states that have low costs on average but contain high-cost study areas. The approach adopted in the *Ninth Report and Order*, however, depends on the ability to determine a statewide average forward-looking cost. In the *Ninth Report and Order* we found that, as a policy matter, federal high-cost support should be sufficient to enable reasonably comparable rates among states, while leaving states with sufficient resources to set rates for intrastate services that are reasonably comparable to rates charged for similar services within their borders.[75] To that end, we adopted a mechanism to calculate support for non-rural carriers by comparing the forward-looking costs of providing the supported services, averaged at the statewide level, to a national benchmark.[76] We found that statewide averaging, together with the other components of the forward-looking methodology adopted for non-rural carriers, is consistent with the division of federal-state responsibility for achieving reasonably comparable rates for customers of non-rural carriers.[77] When we adopted the forward-looking methodology for non-rural carriers, we noted that our decision did not necessarily mean that we would adopt a similar approach for rural carriers.[78] As explained above, we will continue to refine our rules as we develop a long-term universal service support mechanism for rural carriers. During the duration of the plan, which we are adopting for the interim, we will continue to consider a forward-looking methodology for rural carriers. Meanwhile, we will rely on the modified embedded cost mechanism to calculate support for rural carriers.

30. In sum, we find that the modified embedded cost mechanism we adopt will provide rural carriers with specific, predictable, and sufficient support over the next five years, consistent with the goals and principles set forth in section 254 of the Act. As a result, rural carriers will be able to continue to provide affordable service in rural America.

B. Modified Embedded Cost Mechanism

1. The Indexed Cap on High-Cost Loop Fund and the Rural Growth Factor

a. Background

31. The high-cost loop support fund currently is subject to an indexed cap, originally adopted in 1993,[79] which limits the maximum growth in the total amount of support available from the

[74] *See, e.g.*, California Commission Comments at 5; Florida Commission Comments at 4; Illinois Commission Comments at 13; NYDPS Comments at 4; Texas Commission Comments at 1, 2.

[75] *Ninth Report and Order* at 20453-54 para. 38.

[76] By averaging costs at the statewide level, the federal mechanism compares the relative costs of providing supported services in different states. The mechanism provides support to carriers in those states with average costs that exceed the national average cost benchmark.

[77] *Ninth Report and Order*, 14 FCC Rcd at 20453-54 para 38.

[78] *Id.* at 20453-54 para 45 n.136.

[79] *See Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Report and Order, 9 FCC Rcd 303 (1993) (*Fund Cap Order*); *see also Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Report and Order, 11 FCC Rcd 2538 (1996); *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 11 FCC Rcd 7920 (1996) (*Fund Cap Extension Order*).

high-cost loop support fund to the previous year's support amount, increased by an index factor that is equal to the rate of growth in the total number of working loops nationwide for the calendar year preceding the annual data filing.[80] For example, in 1998, the total number of working loops grew 3.43 percent. Thus, the amount of high-cost loop support available in 2000 was the 1999 support amount ($864.2 million) increased by 3.43 percent, which equals $893.8 million.

32. The Commission originally adopted the indexed cap on the high-cost loop fund in order to limit fund growth and moderate annual fluctuations in the size of the fund pending the Commission's consideration of permanent changes to the high-cost assistance mechanisms.[81] Prior to the adoption of the indexed cap, the high-cost loop fund had grown by approximately 60 percent in eight years, with annual rates of growth ranging from one percent to more than 19 percent.[82] The Commission reasoned that moderating the growth of the high-cost loop fund would provide carriers with certainty regarding overall support levels and would facilitate the Commission's ability to revise the universal service mechanisms, if necessary, without jeopardizing the continued availability of local telephone service at reasonable rates.[83]

33. After passage of the 1996 Act, the Commission reassessed the operation of the indexed cap and decided to retain the indexed cap until all carriers receive high-cost support based on a forward-looking economic cost mechanism.[84] The Commission reasoned that the indexed cap would prevent excessive growth in the existing high-cost loop fund during the period preceding the implementation of a forward-looking support mechanism.[85] According to the Commission, rapid growth in high-cost loop support would make the transition to a forward-looking mechanism more difficult for rural carriers if the new system provided for significantly different levels of support.[86] In short, the Commission concluded that the indexed cap effectively limits overall growth of the fund, while protecting individual carriers from experiencing extreme reductions in support.[87]

34. In the *Fourth Reconsideration Order*, the Commission concluded that the indexed cap is a reasonable means of limiting the overall growth of the high-cost loop fund, and thus protects contributors from excess universal service contribution requirements, while allowing the high-cost loop fund to grow to support the growth in lines served by carriers in high-cost areas.[88] In the absence of evidence showing that the indexed cap will result in insufficient support, the Commission also concluded that the indexed cap is consistent with the goal of section 254(b)(5) to ensure that universal service support is sufficient.[89]

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[80] *See* 47 C.F.R. § 36.601(c). *See supra* para. 13 describing the operation of the high-cost loop support mechanism.

[81] *See Fund Cap Order*, 9 FCC Rcd at 305 paras. 17-20.

[82] *See id.* at 306 para. 22.

[83] *See id.* at 305 paras. 18-19.

[84] *See First Report and Order*, 12 FCC Rcd at 8940 para. 302, *Fourth Order on Reconsideration*, 13 FCC Rcd at 5340 para. 34.

[85] *First Report and Order*, 12 FCC Rcd at 8940 para. 302.

[86] *Id.*

[87] *Id.*

[88] *See Fourth Order on Reconsideration*, 13 FCC Rcd at 5343 para. 39.

[89] *Id.* at 5341-42 para. 36. *See also* 47 U.S.C. § 254(d) (requiring "[e]very telecommunications carrier that provides interstate services [to] contribute, on an equitable and nondiscriminatory basis, to the specific, (continued....)

35. Against this backdrop, the Rural Task Force recommended that the Commission retain an indexed cap on the high-cost loop support mechanism, but increase the size of the rural carrier portion of the high-cost loop support fund to reflect increased costs for rural carriers and tie the annual rate of growth of the rural carrier portion of the fund to an index that reflects increased costs and lines over time. In particular, the Rural Task Force recommended that the Commission recompute or "re-base" the indexed cap on the rural incumbent local exchange carrier portion of the high-cost loop support fund as if the indexed high-cost loop fund cap and a limitation on support for corporate operations expenses had not been in effect for the calendar year 2000.[90] The Rural Task Force also recommended that the Commission annually increase the re-based rural incumbent local exchange carrier portion of the high-cost loop support fund by an annual "rural growth factor" representing the sum of rural line growth and changes in a general inflation factor -- the United States Department of Commerce's Gross Domestic Product-Chained Price Index (GDP-CPI).[91] The Rural Task Force further recommended that the Commission resize the indexed cap whenever the definition of supported services is changed.[92] Under the Rural Task Force's proposal, "safety net additive" support,[93] support for acquired exchanges and "safety valve" support,[94] and support for competitive eligible telecommunications carriers[95] would be calculated without regard to the re-based cap on high-cost loop support. In other words, these forms of support would be "uncapped."

36. The Joint Board observed that the modifications to the caps and limitations on high-cost loop support proposed by the Rural Task Force, including the modifications to the cap on the high-cost loop fund, are "generally designed to provide carriers with increased incentives to invest in new infrastructure and technologies."[96] The Joint Board concluded that the Rural Task Force Recommendation presents a good foundation for implementing a rural universal service plan.[97]

b. Discussion

37. As discussed in greater detail below, we adopt the Rural Task Force's recommendation to re-base the high-cost loop support fund for rural telephone companies and retain an indexed cap on the fund. Rural carriers shall receive re-based high-cost loop support effective July 1, 2001. We believe that an indexed cap balances the various goals enunciated in section 254 of the Act.[98] These goals include,

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predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service").

[90] *See* Rural Task Force Recommendation at 24. According to the Rural Task Force, re-basing will result in an initial $118.5 million increase in the high-cost loop support fund, representing $83.9 million from removing the overall cap on high-cost loop support and $34.6 million from removing the corporate operations expense limitation, used when calculating high-cost loop support. *See id.* at 20-21. The corporate operations expense limitation is discussed in greater detail in section IV.B.3. *infra.*

[91] *See* Rural Task Force Recommendation at 24-25.

[92] *Id.* at 27.

[93] *Id.*; *see infra* discussion at paras. 77-90.

[94] Rural Task Force Recommendation at 30. The Rural Task Force's example of a "safety valve" mechanism for transferred exchanges includes a proposal to exclude loops transferred to rural telephone companies from the rural growth factor calculation. *Id.* at Appendix D. *See infra* discussion at paras. 91-119.

[95] Rural Task Force Recommendation at 25; *see infra* discussion at paras. 97-119.

[96] *Recommended Decision* at para. 11.

[97] *See id.* at para. 13.

[98] *See* 47 U.S.C. § 254.

among others, keeping the fund specific, predictable, and competitively neutral, as well as the need to achieve service and rate comparability.[99] Moreover, the indexed cap will ensure that the fund is within the range of sufficiency, and will minimize burdens on carriers to contribute to the universal service mechanisms.[100]

38. We agree with the Rural Task Force that "safety net additive" support and support for acquired exchanges and "safety valve" support should be excluded from the re-based cap on high-cost loop support. We believe that the exclusion of such support from the re-based cap on high-cost loop support is consistent with the universal service goals enunciated in section 254 of the Act. By providing carriers above-the-cap support for new investments in their existing networks and acquired exchanges, we introduce an element of predictability that has not been present under the current high-cost universal service mechanism.

39. In addition, we adopt the Rural Task Force's proposal to increase the portion of the high-cost loop support fund that is distributed to rural incumbent local exchange carrier study areas by a rural growth factor equal to annual increases in the GDP-CPI and growth in the total number of working loops of rural incumbent local exchange carriers. As discussed in greater detail below, by reforming the growth factor in this way, we make high-cost support more specific to the needs of rural carriers. We also agree with the proposal included in the Rural Task Force's example of a safety valve mechanism in Appendix D of its Recommendation that all access lines transferred to rural carriers should be excluded from the rural growth factor.[101] We conclude that the Rural Task Force's proposal, as modified herein, represents a reasonable compromise between disparate interests. We also conclude that the Rural Task Force's proposal is consistent with the universal service goals enunciated in section 254 of the Act. Specifically, the Rural Task Force's proposal will ensure that rural telephone companies receive sufficient, specific, and predictable high-cost universal service support during this transition period, while minimizing the burden on carriers to contribute to the universal service mechanisms.

40. *Indexed Cap on the High-Cost Loop Fund*. We agree with the Rural Task Force and commenters that the indexed cap on the rural incumbent local exchange carrier portion of the high-cost loop fund should be recomputed or "re-based" as if the indexed fund cap and the corporate operations expense limitation had not been in effect for the calendar year 2000.[102] Effective July 1, 2001, rural carriers shall receive increased high-cost loop support based on uncapped support amounts for the calendar year 2000, plus a rural growth factor equal to the sum of annual changes in the total number of working loops for rural carriers and the GDP-CPI.[103] In reaching this conclusion, we are mindful that the Rural Task Force's recommendation represents the consensus of the Rural Task Force members, a

[99] *See* 47 U.S.C. § 254(b)(3), (5). In addition to the universal service principles specified in the 1996 Act, Congress directed that the Joint Board and the Commission be guided by such other principles as they determine to be consistent with the Act, and necessary and appropriate for the protection of the public interest, convenience, and necessity. 47 U.S.C. § 254(b)(7). As recommended by the Joint Board, the Commission adopted competitive neutrality as an additional principle for universal service. *See First Report and Order*, 12 FCC Rcd at 8801-02 paras. 46-48, 8932-34 paras. 286-90.

[100] *See* 47 U.S.C. § 254(b)(4), (d).

[101] *See* Rural Task Force Recommendation at Appendix D; *see also infra* discussion at para. 53.

[102] *See* Rural Task Force Recommendation at 24; *see also, e.g.,* Arizona LEC Assn. Comments at 2; AT&T Comments at 12; CUSC Comments App. A at 22; GVNW Consulting Comments at 3; NECA Comments at 7; NTCA Comments at 3-4; Virgin Islands Commission Comments at 6; Sprint Comments at 1-2; Western Alliance Comments at 11; WorldCom Reply Comments at 8.

[103] *See infra* discussion at paras. 48-53.

diverse group representing all points of view affected by a change in the high-cost loop fund.[104] The need for such a consensus is evidenced by the widely differing comments received regarding the Rural Task Force's proposal to re-base the high-cost loop fund. The MAG and some commenters support removal of the indexed cap on the high-cost fund in its entirety,[105] while certain other commenters argue that the high-cost loop fund should not be re-based at this time.[106] Most commenters, however, support the Rural Task Force's proposal to re-base the rural carrier portion of the high-cost loop fund as an acceptable compromise between disparate interests.[107]

41. In the *First Report and Order*, the Commission concluded, in part, that rural carriers may require a greater amount of support than fixed support mechanisms would provide in order to maintain existing facilities and make prudent facilities upgrades until such time as a forward-looking support mechanism is in place.[108] On the other hand, the Commission concluded that the indexed cap on high-cost loop support would moderate growth in the high-cost loop fund until final rules implementing the universal service provisions of the 1996 Act take effect.[109] More than seven years have passed since the Commission originally implemented the indexed cap on the high-cost loop support fund. We observe that the weighted average unseparated per-line loop cost for rural carriers increased by an annual average of approximately one percent per year from 1995 to 1999. The weighted average unseparated per-line loop cost for non-rural carriers decreased by an annual average of approximately 1.2 percent over the same period. Increases in the weighted average unseparated per-line loop cost for rural carriers currently are not reflected in the indexed cap on the high-cost loop fund, which is based on the rate of growth in the total number of rural and non-rural working loops nationwide for the preceding calendar year.[110] Therefore, the indexed cap on the high-cost loop fund increasingly has limited the amount of high-cost loop support for rural carriers. According to the Rural Task Force, without the indexed cap, the portion of the high-cost loop fund that is distributed to rural telephone company study areas would have been

[104] The Rural Task Force was made up of individuals representing rural carriers, competitive local exchange carriers, interexchange carriers, wireless providers, consumers advocates, and state and federal interests.

[105] *See MAG NPRM*, 16 FCC Rcd at 464 para. 11; Arizona LEC Assn. Comments at 2; Interstate Telecom Group Comments at 6; John Staurulaukis, Inc. Comments at 6-8; NECA Comments at 5-7; NRTA, OPASTCO, & USTA Reply Comments at 5; NTCA Comments at 3-4; Western Alliance Comments at 11; *see also* Alabama Rural LECs Comments in CC Docket No. 00-256 at 2; MAG Reply Comments in CC Docket No. 00-256 at 14-15; Rate-of-Return Coalition Comments in CC Docket No. 00-256 at 6-7; Summit Tel. Co. Comments in CC Docket No. 00-256 at 3; Telecom Consulting Associates Comments in CC Docket No. 00-256 at 6; Wisconsin Commission Comments in CC Docket No. 00-256 at 6-7.

[106] *See* California Commission Comments at 8; Florida Commission Comments at 4; Illinois Commission Comments at 4-7; NYDPS Comments at 4; Texas Commission Comments at 3; Qwest Reply Comments at 3; WorldCom Comments at 3; *see also* AT&T Comments in CC Docket No. 00-256 at 9; CUSC Comments in CC Docket No. 00-256 at 18-19; Global Crossing Comments in CC Docket No. 00-256 at 11-12; Illinois Commission Comments in CC Docket No. 00-256 at 11; WorldCom Comments in CC Docket No. 00-256 at 16-17.

[107] *See, e.g.*, Arizona LEC Assn. Comments at 2; AT&T Comments at 12; CUSC Comments App. A at 22; GVNW Consulting Comments at 3; NECA Comments at 7; NTCA Comments at 3-4; Virgin Islands Commission Comments at 6; Sprint Comments at 1-2; Western Alliance Comments at 11; WorldCom Reply Comments at 8.

[108] *See First Report and Order*, 12 FCC Rcd at 8939 para. 300 (rejecting a proposal to base support, on a going-forward basis, on costs reported in 1995).

[109] *See First Report and Order*, 12 FCC Rcd at 8940 para. 302; *Fund Cap Order*, 9 FCC Rcd at 305 para. 17; *Fund Cap Extension Order*, 11 FCC Rcd at 7923-24 paras. 7-9.

[110] *See supra* at para. 31.

$83.9 million higher in calendar year 2000.[111] The Rural Task Force has responded, in part, by recommending that the Commission recompute or "re-base" the indexed cap on the rural carrier portion of the high-cost loop fund as if the indexed cap was not in effect for the calendar year 2000. As discussed above, this proposal represents a compromise of competing interests.[112]

42. Based on the record before us, we find it reasonable to reevaluate and re-base the high-cost loop support fund to ensure that rural telephone companies have incentives to maintain existing facilities and make prudent investments in facility upgrades. At the same time, the record does not reflect a specific point at which support should be set. Indeed, we believe that there is no one specific such point. Rather, establishing sufficient support requires a balancing of goals such as providing incentives for prudent investment and preventing excessive support to the detriment of carriers contributing to the fund.[113] In light of these goals, we believe it is reasonable to re-base the rural incumbent local exchange carrier portion of the high-cost loop fund as if the indexed cap and the corporate operations expense limitation were not in effect for the calendar year 2000. Although this approach may appear more generous to rural carriers than the current mechanism, we believe it is a reasonable approach to accomplishing the sufficiency balance here because we do not want to stifle prudent investment while we continue to transition rural carriers to a support mechanism based on forward-looking economic costs. The adjustments to the indexed cap we adopt today will prevent excessive and erratic growth in the high-cost loop fund, while ensuring that rural telephone companies are able to provide supported services at affordable and reasonably comparable rates.

43. We therefore adopt the Rural Task Force's proposal to re-base the rural carrier portion of the high-cost loop fund as if the indexed cap and the corporate operations expense limitation had not been effect for calendar year 2000. We concur with the Joint Board's observation that the modifications to the caps and limitations on high-cost loop support proposed by the Rural Task Force are "generally designed to provide carriers with increased incentives to invest in new infrastructure and technologies."[114] We conclude that re-basing the indexed fund will ensure that eligible rural telephone companies are able to continue making prudent investments in rural facilities for the next five years, while we develop a more targeted high-cost support mechanism for rural telephone companies.

44. We also agree with the Rural Task Force that safety net additive support, support for acquired exchanges, and safety valve support should be excluded from the re-based cap on high-cost loop support.[115] As discussed in greater detail below, we believe that the exclusion of such support from the re-based cap on high-cost loop support is consistent with the universal service goals enunciated in section 254 of the Act. The availability of uncapped safety net additive support will ensure that rural carriers that make significant investments in telecommunications plant in service receive sufficient, specific, and predictable support for the incremental costs associated with new investment, while minimizing the burden on carriers that contribute to the universal service mechanisms.[116] Support for acquired exchanges in the form of safety valve support will be subject to a cap of five percent of the portion of the annual indexed cap on the high-cost loop fund that is distributed to rural incumbent local

[111] *See* Rural Task Force Recommendation at 20-21. The Rural Task Force also notes that the removal of corporate operations expense limitation would increase the fund for rural carriers by $34.6 million.

[112] *See supra* at para. 35.

[113] *See supra* paras. 26-28.

[114] *See Joint Board Recommended Decision* at para. 12.

[115] *See* Rural Task Force Recommendation at 30.

[116] *See infra* discussion at para. 79.

exchange carrier study areas.[117] We believe that a five percent cap will ensure that sufficient support is available for acquired exchanges and will protect contributors from excessive universal service contributions.

45. We clarify, however, that, because support for acquired exchanges and safety valve support will be provided outside the cap, the overall size of the rural high-cost loop fund should be reduced to reflect the removal of support for access lines transferred from rural carriers to non-rural carriers or to other rural carriers. The reduction shall equal the amount of the expense adjustment available to the transferred access lines at the time of the transfer and shall be effective in the next calendar quarter after the access lines are transferred. Without such an exclusion from the rural incumbent local exchange carrier portion of the high-cost loop fund, the remaining access lines might receive increased per-line support when access lines are transferred from a rural incumbent local exchange carrier study area to a non-rural carrier or to another rural incumbent local exchange carrier.[118] Under such a scenario, the lines included in the rural incumbent local exchange carrier portion of the high-cost loop fund would decrease, without a corresponding decrease in the overall rural incumbent local exchange carrier portion of the high-cost loop fund. Over time, per-line support for the remaining access lines would increase to the extent that more exchanges are transferred from rural incumbent local exchange carrier study areas. Such a result would be inconsistent with the statutory goal of providing no more support than is sufficient and would not prevent excessive growth in the high-cost loop fund.[119] We expect that the exclusion of support for transferred access lines from the rural incumbent local exchange carrier portion of the indexed high-cost loop fund will maintain the relationship between the size of the high-cost loop fund and the number of supported lines.

46. We disagree with commenters and the MAG that the Commission should remove the indexed cap on the high-cost loop fund in its entirety.[120] We find that the MAG proposal to remove the indexed cap on the high-cost fund is incompatible with the modified high-cost loop support mechanism recommended by the Joint Board and adopted in this Order. Based on the record before us, we specifically disagree that an indexed cap on the high-cost loop fund will prevent rural carriers from receiving adequate universal service support.[121] The indexed cap we adopt today will result in an immediate increase in the high-cost loop support available to rural telephone companies and will grow by the rural growth factor, which includes an inflation adjustment – an additional growth element that is not part of our existing cap. In addition, several mechanisms we adopt today, such as safety net additive support[122] and safety valve support[123] will provide carriers with additional support. We also continue to believe that an indexed cap is a reasonable means of limiting the overall growth of the high-cost loop

[117] *See infra* discussion at paras. 107-109.

[118] Assume, for example, that a total of 10 rural carrier lines receive $1 per line or a total of $10 in high-cost loop support. If one line is sold to a non-rural carrier, then the remaining nine lines would be eligible for approximately $1.11 per line in high-cost loop support, representing an 11 percent increase in per-line support. If, however, there is a corresponding $1 reduction in the total amount of available high-cost loop support to reflect the sale of one line to a non-rural carrier, then the remaining lines would not receive increased per-line support.

[119] *See First Report and Order*, 12 FCC Rcd at 8940 para. 302.

[120] *See supra* n.105.

[121] *See, e.g.*, Interstate Telecom Group Comments at 6; John Staurulaukis, Inc. Comments at 6-7; NRTA, OPASTCO, & USTA Comments at 5-7.

[122] *See infra* discussion at paras. 77-90.

[123] *See infra* discussion at paras. 91-119.

fund, and thus protects contributors from excessive universal service obligations.[124] As discussed above, we also believe that an indexed cap balances the universal service goals, such as sufficiency, specificity, and predictability, enunciated in section 254 of the Act.[125]

47. The Rural Task Force also recommended that the indexed cap be resized whenever the definition of supported services is changed.[126] We note that, in accordance with section 254(c)(2) of the Act,[127] the Commission recently requested that the Joint Board review the definition of services eligible for high-cost and low-income universal service support.[128] The Commission specifically asked the Joint Board to address the implications of any proposed modifications to the list of supported services.[129] We therefore will await the Joint Board's recommendations regarding the definition of supported services prior to considering whether the indexed cap should be resized to reflect any modifications to the list of supported services.

48. *Rural Growth Factor*. We adopt the Rural Task Force's proposal to grow the portion of the high-cost loop support mechanism that is distributed to rural incumbent local exchange carrier study areas by a rural growth factor equal to the sum of annual changes in the total number of working loops of rural incumbent local exchange carriers and the GDP-CPI, not the rate of growth for all rural and non-rural working loops.[130] The rural growth factor shall be based on the GDP-CPI for the year in which costs are incurred and the difference between the total number of rural incumbent local exchange carrier working loops for the cost year and the preceding calendar year. For example, for support disbursed in the year 2001, the rural growth factor shall be based on the percentage change in the GDP-CPI for calendar year 1999 and the percentage change in the total number of rural incumbent local exchange carrier working loops between calendar years 1998 and 1999.

49. We note that growth in rural working loops nationwide recently has been higher than growth in non-rural working loops nationwide.[131] We therefore believe that it is appropriate to limit growth in the rural incumbent local exchange carrier portion of the high-cost loop fund based on the growth in the total number of working loops of rural incumbent local exchange carriers. Using a rural growth factor will more accurately reflect changes in the number of rural lines over time. We disagree

[124] *See Fourth Order on Reconsideration,* 13 FCC Rcd at 5343 para. 39. As the Commission concluded in the *First Report and Order*, excessive growth in high-cost loop support may make the transition to other support mechanisms more difficult for rural carriers, especially if those support mechanisms provide significantly different levels of support. *See First Report and Order*, 12 FCC Rcd at 8940 para. 302.

[125] *See supra* discussion at para. 42.

[126] Rural Task Force Recommendation at 27.

[127] Section 254(c)(2) provides that "[t]he Joint Board may, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms." 47 U.S.C. § 254(c)(2).

[128] *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Order, 15 FCC Rcd 25257 (rel. Dec. 21, 2000) (*Referral Order*).

[129] *Id.* at para. 3.

[130] *See* Rural Task Force Recommendation at 25.

[131] For example, the annual rate of growth in the total number of rural and non-rural working loops nationwide, which was 2.86 percent in 1999, is considerably less than the annual rate of growth in the total number of rural working loops nationwide, which was 4.26 percent in 1999. *See* NECA Universal Service Fund 2000 Submission of 1999 Study Results, filed October 1, 2000; NECA Universal Service Fund 1999 Submission of 1998 Study Results, filed October 1, 1999.

with commenters who argue that the Commission should retain the current index factor, which reflects both rural and non-rural line growth, instead of adopting the Rural Task Force's proposal for a rural growth factor.[132] These parties do not suggest that the high-cost loop fund should remain stagnant, rather they disagree with the factor to be used to grow the fund.

50. We also note that the current index factor does not account for varying costs that are unrelated to the increase in working loops. When the Commission extended the indexed cap in the *First Report and Order*, it expected to move rural carriers to a universal service support mechanism based on forward-looking economic costs more quickly than will actually occur.[133] Because the timeframe for moving to a forward-looking economic cost mechanism is now extended for rural carriers, we believe that it is reasonable to acknowledge, in the portion of the high-cost loop support mechanism that is distributed to rural incumbent local exchange carrier study areas, that costs may vary for reasons unrelated to the growth in working loops. For the duration of this plan, we therefore adopt the Rural Task Force's recommendation to use the GDP-CPI as a proxy for cost changes.

51. We reject proposals to include a rural telephone company or telecommunications industry productivity factor in the rural growth factor.[134] Although it appears that rural carrier costs recently have grown at a slightly slower annual rate than growth in the GDP price index (indicating that rural carriers have experienced modest productivity gains over time), at this time, we do not have a reliable methodology for measuring productivity gains for rural telephone companies.[135] Moreover, parties have not submitted a methodology that specifically measures the productivity gains of rural carriers.[136] We note that the high-cost loop fund will be subject to an indexed cap for the life of the plan, thus ensuring that rural carriers do not receive excessive support. We therefore adopt the consensus recommendation of the Rural Task Force to include an inflation factor, the GDP-CPI, in the rural growth factor without also including a productivity factor.

52. We conclude that the rural growth factor proposed by the Rural Task Force will further the universal service goals, such as sufficiency, specificity, and predictability, enunciated in section 254 of the Act.[137] Because the rural growth factor will ensure that the portion of the high-cost loop support mechanism that is distributed to rural incumbent local exchange carrier study areas better reflects growth in rural lines and changed costs over time, we conclude that the rural growth factor will provide rural incumbent local exchange carriers with sufficient support. The rural growth factor also will provide rural incumbent local exchange carriers with specific and predictable growth in the high-cost loop support mechanism over time.

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[132] *See, e.g.*, California Commission Comments at 9; SBC Reply Comments at 6.

[133] *See supra* discussion at para. 41.

[134] *See* Ad Hoc Telecommunications User Committee Comments at 17; Texas Commission Comments at 4; *but see* Innovative Telephone Reply Comments at 5-7.

[135] For example, the weighted average unseparated per-line loop cost for rural carriers increased by an average of approximately one percent per year from 1995 to 1999, while the GDP price index increased by 1.75 percent per year during that same period. *See supra* discussion at para. 41; AT&T Comments in CC Docket No. 00-256 at Table 1. Moreover, AT&T states that average growth in the common line revenue requirement from 1995-1999 was 5.99 percent per year, while average annual growth in the GDP price index plus access lines was 7.19 percent during that same period. *Id.*

[136] *See, e.g.*, Ad Hoc Telecommunications User Committee Comments at 17 (proposing that the Commission use the productivity factor currently applied to price cap LEC rates).

[137] *See* 47 U.S.C. § 254(b)(5).

53. In addition, we adopt the proposal, included in the Rural Task Force's example of a safety valve mechanism, to exclude all access lines transferred to rural carriers from the rural growth factor calculation.[138] This conclusion is consistent with our reasons for excluding support for access lines transferred to rural incumbent local exchange carrier study areas from the rural incumbent local exchange carrier portion of the indexed cap on the high-cost loop fund.[139] Including access lines transferred to rural incumbent local exchange carriers in the rural growth factor, but not in the portion of the indexed high-cost loop fund that is distributed to rural incumbent local exchange carrier study areas, would result in growth in the indexed high-cost loop fund that reflects neither growth in lines eligible to receive support from the indexed high-cost loop fund nor growth in the GDP-CPI for those lines. If transferred loops were included in the rural growth factor, but not in the rural incumbent local exchange carrier portion of the indexed high-cost loop fund, the remaining access lines would receive increased per-line support whenever access lines are transferred to a rural carrier study area. Over time, per-line support for the remaining access lines would increase as more loops are transferred to rural carrier study areas. Such a result would be inconsistent with the goal, enunciated in the *First Report and Order*, of preventing excessive growth in the high-cost loop fund.[140] Consistent with the exclusion of support for competitive eligible telecommunications carriers from the indexed cap, we also will exclude lines operated by competitive eligible telecommunications carriers from the rural growth factor.[141]

2. National Average Loop Cost

a. Background

54. The Rural Task Force's recommendation to re-base the high-cost loop fund includes a proposal to freeze the national average loop cost at $240.00 for the life of the plan, which, according to the Rural Task Force, approximates the actual national average loop cost for year 2000 support (based on 1998 cost data).[142] Under the Commission's existing rules, a rural carrier is eligible for high-cost loop support if its embedded loop costs for a particular study area exceed 115 percent of the national average loop cost.[143] According to section 36.622 of the Commission's rules, the national average loop cost is the greater of: (1) the sum of loop costs nationwide divided by the total number of working loops nationwide; or (2) an amount calculated to maintain the indexed cap on the high-cost loop support fund.[144] If the sum of actual high-cost loop support nationwide exceeds the indexed cap on the high-cost loop support fund (in essence, the indexed cap on the high-cost loop support fund is triggered), the national average loop cost is increased in order to ensure that the total amount of high-cost loop support disbursed does not exceed the indexed cap.

b. Discussion

55. We adopt the Rural Task Force's recommendation to freeze the national average loop

[138] *See* Rural Task Force Recommendation at Appendix D.

[139] *See supra* para. 45.

[140] *See First Report and Order*, 12 FCC Rcd at 8940 para. 302.

[141] *See infra* discussion at para. 125.

[142] *See* Rural Task Force Recommendation at 24.

[143] *See* 47 C.F.R. §§ 36.601-36.631.

[144] *See* 47 C.F.R. § 36.622.

cost at $240.00 for purposes of calculating rural high-cost loop support.[145] We conclude that freezing the national average loop cost for the duration of this plan will provide rural carriers with greater certainty as to their eligibility for high-cost loop support.[146] Because the national average loop cost will be frozen at $240.00, carriers will know in advance whether they may be eligible for high-cost loop support. Such certainty will assist carriers in short- and long-term planning for infrastructure investment, consistent with the goals of specificity and predictability in section 254 of the Act.[147] Because freezing the national average loop cost for rural carriers at $240.00 will provide carriers with greater predictability as to their eligibility for high-cost loop support, carriers also will be better able to achieve rate and service comparability, another goal of section 254 of the Act.[148]

56. At this time and based on the record, we do not believe that freezing the national average loop cost at $240.00 will result in significant numbers of carriers with higher than average loop costs being denied support and carriers with lower than average loop costs being awarded support. If in a given year the actual national average loop cost is significantly above $240.00, support may be directed to certain rural carriers that otherwise would not be eligible for high-cost loop support. If, on the other hand, the actual national average loop cost falls below $240.00, support may be withheld from rural carriers that otherwise would be eligible for high-cost loop support under our current rules.

57. In support of this conclusion, we note that the national average loop cost has experienced only minor fluctuations over the past four years. For example, the national average loop cost (with the corporate operations expense limitation in effect) for high-cost loop support disbursed in 1998 was $247.34, while the national average loop cost (with the corporate operations expense limitation in effect) for high-cost loop support disbursed in 2001 is $239.86.[149] This represents only an approximately three percent reduction in the national average loop cost in four years. We therefore do not anticipate a dramatic increase or decrease in the actual national average loop cost in the near future such that large numbers of carriers with lower than average loop costs will inappropriately receive high-cost loop support or that carriers with higher than average loops costs will inappropriately be denied high-cost loop support. In light of this relatively small percentage change, we believe that the specificity and predictability provided by a frozen national average loop cost outweighs any potential distortions that might occur with a freeze for the limited five-year duration of the plan we adopt today.[150]

58. We also note that, as provided by section 36.622 of the Commission's rules, if the sum of the actual high-cost loop support nationwide exceeds the indexed cap on the high-cost loop support fund, NECA increases the amount of the national average loop cost in order to ensure that the total amount of high-cost loop support disbursed does not exceed the indexed cap.[151] Thus, certain carriers with average loop costs slightly above the proposed frozen national average loop cost would not receive support. To the extent that the frozen national average loop cost is increased to accommodate the

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[145] *See* Rural Task Force Recommendation at 24; *see also* NTCA Comments at 4; Verizon Comments at 3; Sprint Reply Comments at 3; *but see* Texas Commission Comments at 4.

[146] *See* 47 U.S.C. §§ 254(b)(5), (e).

[147] *See* 47 U.S.C. § 254(b)(5).

[148] *See* 47 U.S.C. § 254(b)(3).

[149] *See* NECA Universal Service Fund 1997 Submission of 1996 Study Results, filed October 1, 1997; NECA Universal Service Fund 2000 Submission of 1999 Study Results, filed October 1, 2000.

[150] *See* 47 U.S.C. § 254(b)(5).

[151] 47 C.F.R. § 36.622. The Rural Task Force did not propose to change this aspect of section 36.622 of the Commission's rules.

indexed cap on the high-cost loop fund, carriers with average loop costs below the actual national average loop cost but above the proposed frozen national average loop cost would not receive high-cost loop support. Although we adopt a national average loop cost of $240.00 for the duration of this plan, if the actual national average loop cost experiences significant increases or reductions, we may consider appropriate actions at that time.[152]

59. Under section 36.612 of our rules, every non-rural telephone company is required to submit loop cost data and loop counts on a quarterly basis.[153] Under section 36.611 of our rules, all incumbent local exchange carriers are required to submit loop cost data and loop counts on an annual basis.[154] Because the national average loop cost is based on embedded loop cost data for both rural and non-rural study areas, non-rural carriers currently are required to file such data with the fund administrator even though non-rural carriers now receive high-cost support based on a forward-looking methodology.[155] If we freeze the national average loop cost at $240.00, it will no longer be necessary for NECA to calculate the national average loop cost on a quarterly basis, and, thus, it is unnecessary for non-rural carriers to file loop cost data on a quarterly basis. Nor is there any other reason to require non-rural carriers to file this quarterly loop cost data.[156] Because NECA will no longer make such calculations, it is unnecessary to require submission of that information. We therefore will no longer require non-rural carriers to submit the loop cost data listed in section 36.611 of our rules to NECA on a quarterly basis. In order to enable the Commission to accurately evaluate the operation of the frozen national average loop cost over time, we will continue to require non-rural carriers to submit loop cost data on an annual basis and loop counts on a quarterly basis. Such information is necessary for NECA and USAC to determine the amount of high-cost support available to non-rural carriers.

3. Corporate Operations Expenses

a. Background

60. The high-cost loop support fund provides support for a portion of the corporate operations expenses incurred by rural carriers in providing supported services. Corporate operations expenses consist of total company costs associated with the following activities: formulating corporate policy and providing overall administration and management; long-range planning; providing accounting and financial services; maintaining relations with government, regulators, other companies, and the general public; performing personnel administration activities; operating general purpose computers; providing legal services; procuring material and supplies; developing new products; and performing other general administrative activities.[157] Prior to 1998, the amount of corporate operations expenses that was supported through our universal service mechanisms was determined by multiplying the total corporate operations expense by the ratio of loop investment to total plant in service. As explained below, in the *First Report and Order* the Commission concluded that a carrier's ability to receive

[152] *See infra* paras. 167-177.

[153] *See* 47 C.F.R. § 36.612.

[154] *See* 47 C.F.R. § 36.611.

[155] *See* 47 C.F.R. §§ 36.621, 36.622.

[156] *See* Verizon Comments at 1, 3; Sprint Reply Comments at 2-3.

[157] Corporate operations expenses include all of the expenses listed in sections 32.6710 through 32.6712 and sections 32.6720 through 32.6728 of the Commission's rules. 47 C.F.R. §§ 32.6710-32.6712; 47 C.F.R. §§ 32.6720-32.6728. Those categories of expenses include: executive; planning; general; administrative; accounting; finance; external relations; human resources; information management; legal; procurement; research and development; and other general and administrative expenses. *Id.*

universal service support for corporate operations support should not be unlimited.

61. The corporate operations expense limitation, adopted by the Commission in the *First Report and Order*, limits the amount of corporate operations expenses that a carrier may include in the high-cost loop support mechanism.[158] Under the current mechanism, a carrier compares its actual corporate operations expenses with the expenses calculated by the existing corporate operations expense limitation formula and the lesser amount is used to calculate the carrier's high-cost loop support. The formula was developed to "ensure that carriers use universal service support only to offer better service to their customers through prudent facility investment and maintenance consistent with their obligations under section 254(k)."[159] The Commission agreed with commenters that corporate operations expenses do not appear to be costs inherent in providing telecommunications services, but rather may result from managerial priorities and discretionary spending.[160] The Commission decided to "limit universal service support for corporate operations expense to a reasonable per-line amount," but recognized that "small study areas . . . may experience greater amounts of corporate operations expense per line than larger study areas."[161] The formula allows a greater amount of corporate expense per line for smaller study areas than larger ones because statistical analysis of carrier data show that study areas with fewer loops have more corporate operations expense per loop.

62. In the *First Reconsideration Order* and the *Fourth Reconsideration Order*, the Commission made further refinements to the corporate operations expense cap formula specifically to recognize problems of smaller carriers.[162] On its own motion, the Commission established a floor (or minimum cap) on the corporate operations expense cap to allow carriers with relatively few lines to receive sufficient support to recover initial or fixed corporate operations expenses.[163] Subsequently, the Commission reconsidered, to a limited extent, the dollar amount of the minimum cap on allowable corporate operations expenses for small carriers.[164]

63. In response to requests by small carriers to reconsider its decision to place a limit on the support available for corporate operations expenses, the Commission explained more fully in the *Fourth Reconsideration Order* its reasons for limiting the amount of corporate operations expenses that a carrier could include in the high-cost loop support mechanism.[165] The Commission explained that carrier expenditures for corporate operations expenses may be discretionary in many instances, in contrast to

[158] *First Report and Order*, 12 FCC Rcd at 8930-32 paras. 283-85, 8942 para. 307.

[159] *See id.* at 8930-31 para. 283.

[160] *Id.* at 8931 para. 283.

[161] *Id.*

[162] *See Federal-State Joint Board on Universal Service*, CC Docket 96-45, Order on Reconsideration, 12 FCC Rcd 10102-10105 paras. 17-24 (1997) (*First Reconsideration Order*); *Fourth Order on Reconsideration*, 13 FCC Rcd at 5376-77 paras. 94-95.

[163] *First Reconsideration Order*, 12 FCC Rcd at 10103 para. 19. Under the original formula, carriers with very few lines may have been unable to recover portions of corporate operations expense that do not vary with the number of lines, because allowable corporate operations expenses were determined by a factor that is multiplied by the number of lines. *Id.* The Commission also modified the formula to ensure that the cap on allowable corporate operations expense does not decrease as the number of lines increases. *Id.; see also Fourth Order on Reconsideration*, 13 FCC Rcd at 5377 para. 96.

[164] *See id.* at 5376-77 paras. 94-95.

[165] *See id.* at 5369-70 para. 87 & nn.230-231, 5374-76 paras. 92-93.

expenditures for maintaining plant and equipment.[166] Corporate operations expenses include, for example, travel, lodging, and other expenses associated with attending industry conventions and corporate meetings. While participation in such activities may be prudent, the levels of these expenditures are subject to managerial discretion. The Commission also noted that carriers with 200,000 or fewer working loops had little incentive to minimize these expenses because the previous rules allowed carriers to recover a large percentage of their corporate operations expenses from federal universal service support mechanisms.[167]

64. Although the Commission retained the limitation on support for corporate operations expenses, the Commission raised the minimum cap so that the need for the smallest carriers to seek a waiver would be reduced.[168] Specifically, the Commission adjusted the maximum allowable corporate operations expense formula by permitting carriers with 6,000 or fewer working loops to include in the high-cost loop support mechanism corporate operations expenses of up to $300,000 or amounts derived from the corporate operations expense formulas, whichever is greater, provided that the amount is not greater than a carrier's actual corporate operations expenses.[169] The Commission concluded that "imposing a cap that is relatively generous to small carriers, but still imposes a limitation, is a reasonable method of encouraging carriers to assign corporate operations expenses to the proper accounts and discouraging carriers from incurring excessive expenditures."[170]

65. The Rural Task Force proposed modifying the existing corporate operations expense limitation formula by re-basing and indexing the dollar values in the formula.[171] Since this cap was imposed, the Rural Task Force estimated that the number of rural carriers affected by it -- 205 rural study areas in 2000 -- has increased by 15 percent.[172] To reflect increased work requirements, labor, and other

[166] *See id.* at 5374 para. 92.

[167] *See id.* at 5374 para. 92. Under the Commission's Part 36 rules, carriers with 200,000 or fewer working loops recover 65 percent of loop costs that exceed 115 percent of the national average loop cost and 75 percent of loop costs that exceed 150 percent of the national average. Thus, prior to adoption of the corporate operations expense limitation, carriers with 200,000 or fewer working loops could recover a substantial portion of their operation expenses from the federal universal service support mechanism. *See* 47 C.F.R. § 36.631. By comparison, for example, a carrier with more than 200,000 working loops recovers 10 percent of loop costs that exceed 115 percent of the national average loop cost, 30 percent of loop costs that exceed 160 percent of the national average, 60 percent of loop costs that exceed 200 percent of the national average, and 75 percent of loop costs that exceed 250 percent of the national average. *See* 47 C.F.R. § 36.631.

[168] *Fourth Order on Reconsideration,* 13 FCC Rcd at 5374 para. 92. The Commission recognized, however, that certain carriers, such as those serving Alaska or insular territories, may have unusually high corporate operations expenses, and invited such carriers to file for a waiver "to demonstrate the necessity of these expenses for the provision of the supported services." *Id.*

[169] *See id.* at 5376-77 paras. 94-95. The minimum cap under the previous formula was $114,071. *Id.* In no event may a carrier include in the expense adjustment calculation more than its actual corporate operations expenses. *See* 47 C.F.R. § 36.621(a)(4).

[170] *See Fourth Order on Reconsideration,* 13 FCC Rcd at 5374 para. 92.

[171] As discussed above, the Rural Task Force also recommended that the Commission re-base the indexed cap on the high-cost loop support fund as if both the indexed cap and the corporate operations expense limitation had not been in effect for the calendar year 2000. The Rural Task Force estimated that re-basing the fund would result in a $118.5 million increase in high-cost loop support, representing $83.9 million from removing the overall cap on high-cost loop support and $34.6 million from removing the corporate operations expense limitation. Rural Task Force Recommendation at 24. Note that removing the corporate operations expenses limitation without also removing the overall cap would not increase total support, but would only redistribute support among carriers.

[172] This is based on information provided by NECA. *See* Rural Task Force Recommendation at 27 n.53.

costs since the formula was put in place, the Rural Task Force proposed increasing the dollar values in the formula by the rural growth factor for each year since the cap was adopted. In subsequent years, the dollar values in the formula would be increased each year by the rural growth factor. The Rural Task Force estimated that the number of rural carriers affected by the corporate operations expense cap would have decreased, rather than increasing by 15 percent, if the dollar limitations derived from the formula had been increased annually by five percent.[173] Rather than $34.6 million being excluded by operation of the corporate operations expense limitation in 2000, the Rural Task Force estimated that only $15.1 million would have been excluded.[174]

66. The Rural Task Force also proposed an additional calculation that carriers could use to determine the maximum amount of corporate operations expenses that could be included in the high-cost loop support mechanism. The Rural Task Force noted that some companies consistently have corporate operations expenses above the existing limitation and acknowledged that the waiver process can be economically infeasible for some rural carriers.[175] In order to provide an option other than the waiver process for carriers that would continue to have corporate operations expenses above the section 36.621(a)(4) limitation, even after the dollar amounts in the formula are re-based and indexed, the Rural Task Force proposed an alternative calculation based on uncapped corporate operations expenses for the year 2000. The new alternative formula begins with the uncapped corporate operations expense per line for the year 2000, increases this amount each year by the rural growth factor, and multiplies this amount by the number of lines for the year in question.[176]

67. Under the Rural Task Force proposal, the carrier first compares the amount calculated by the re-based and indexed corporate operations expense limitation formula with the amount calculated under the proposed alternative formula.[177] If the alternative amount based on year 2000 actual expenses is greater than the amount calculated by the re-based and indexed corporate operations expense limitation formula, this is the amount compared with a carrier's actual corporate operations expenses for the year in question and the lesser amount is included in the high-cost loop support mechanism.

68. The Joint Board observed that the modifications to the caps and limitations on high-cost loop support proposed by the Rural Task Force are "generally designed to provide carriers with increased incentives to invest in new infrastructure and technologies."[178] The Joint Board concluded that the Rural Task Force Recommendation presents a good foundation for implementing a rural universal service plan, but did not address the corporate operations expense limitation in specific detail.[179]

b. Discussion

69. We generally agree with the Rural Task Force that modifications to the existing corporate operations expense limitation are appropriate to reflect changes in costs since the limitation was imposed in 1998. Accordingly, as discussed below, we adopt a revised formula to reflect these changes. We also agree with the Rural Task Force's goal of reducing the need for carriers to request

[173] *Id.* at 28 n.55.

[174] *Id.*

[175] *Id.* at 29.

[176] *Id.*

[177] *Id.*

[178] *Recommended Decision* at para. 12.

[179] *See id.* at para. 14.

waivers due to the operation of section 36.621(a)(4) of our rules.[180] We decline, however, to adopt the Rural Task Force's proposed alternative calculation. Instead, as explained below, in order to reduce the need for the smallest carriers to seek a waiver of section 36.621(a)(4), we raise the minimum cap on allowable corporate operations expenses supported by universal service to $600,000.

70. We disagree with the MAG and other commenters who argue that the Commission should remove the limitation on support for corporate operations expenses entirely.[181] Because expenditures for corporate operations expenses are discretionary in many instances, and carriers with 200,000 or fewer loops have little incentive -- absent the limitation -- to minimize these expenses, we continue to believe that some limitation on the universal service support available for these expenses is reasonable and appropriate. We also disagree with those commenters who argue that no adjustment to the corporate operations cap is justified.[182] As discussed below, we find that it is reasonable to make certain adjustments to the corporate operations expense limitation formula.

71. We share the Rural Task Force's concern that the number of rural carriers impacted by the corporate operations expense limitation has increased by 15 percent, affecting 205 rural study areas, in the two years since this limitation was imposed and, therefore, believe that the formula should be revised.[183] The limitation is intended to encourage carriers to assign corporate operations expenses to the proper accounts and to discourage carriers from incurring excessive expenditures. The Rural Task Force suggested that the reason more carriers have been affected by the corporate operations expense limitation is due to "increased work requirements, labor, and other costs."[184] Analysis of carrier data over this period shows that, on average, corporate operations expenses per line have remained essentially constant.[185] For some carriers, however, corporate operations expenses clearly have increased since the limitation was imposed. Without adjustment, the number of rural carriers affected by the cap in 2001 would be 215 – an increase of almost 21 percent since the cap was imposed. We therefore conclude that

[180] 47 C.F.R. §36.621(a)(4).

[181] *See, e.g., MAG NPRM*, 16 FCC Rcd at 464 para. 11; Wisconsin Commission Comments at 7. Most commenters who oppose caps do not specifically discuss the corporate operations expense limitation, but argue generally against any caps or limitations on high-cost loop support. *See, e.g.*, John Staurulaukis, Inc. Comments at 6; NTCA Comments at 3.

[182] *See, e.g.*, California Commission Comments at 10. Most commenters who oppose increases in support for rural carriers do not specifically discuss the corporate operations expense limitation, but argue generally against re-basing the high-cost loop fund. *See, e.g.*, Ad Hoc Telecommunications User Committee Comments at 15-16; NYDPS Comments at 3-5. AT&T points out that any increased support that results from revising the corporate operations expense limitation is subject to the new indexed cap on the high-cost loop fund. *See* AT&T Comments at 12.

[183] *See* Rural Task Force Recommendation at 27 n.53.

[184] *See id.* at 28.

[185] Using publicly available data, Commission staff compared growth in corporate operations expenses from 1997 to 1999. Weighted by 1997 loops, the annual growth rate was 0.10 percent. Weighted by 1999 loops, the annual growth rate declined by 0.39 percent. The source of the data is the NECA Universal Service Fund 2000 Submission of 1999 Study Results, filed October 29, 2000. This data set includes data for the years 1995 to 1999. The sample included 773 rural cost companies. For each of the 773 companies staff listed: USF Loops, Account #6710 – Executive and planning expense; Account #6720 – General and administrative expense; and their sum, which is total corporate operations expense. From these factors staff calculated the monthly cost per loop for 1997 and 1999 for each of the 773 companies. For each of the companies, staff calculated the increase of 1999 expenses over 1997 expenses. This increase for each company was weighted by both the 1997 loops and the 1999 loops and two weighted averages were calculated as follows: using 1997 loops: 1.001009221 – 1 = .001009221 or 0.10 percent; using 1999 loops: .99612603 – 1 = -.00387397 or –0.38 percent.

it is reasonable to revise the formula by increasing the dollar values in the formula.

72. We decline, however, to increase the limitation by the rural growth factor, as suggested by the Rural Task Force. Instead, we adopt a revised corporate operations expense limitation formula in which the dollar values in the formula are re-based and indexed by the Gross Domestic Product-Chained Price Index (GDP-CPI). The Rural Task Force proposed that the dollar values in the corporate operations expense limitation formula be re-based and indexed by the rural growth factor, which is the sum of the GDP-CPI and total annual line growth for rural carriers.[186] We find that it is more appropriate to re-base and index the formula only by the GDP-CPI, without including annual rural line growth. Because the corporate operations expense limitation is calculated as a per-line amount, which is then multiplied by lines to determine the total amount of corporate operations expenses that is used to determine support, the formula already accounts for a carrier's line growth. Multiplying the amount by another line growth factor – the rural line growth – would result in double counting of line growth.

73. In re-basing the dollar values in the formula, we will increase the dollar values for each of four years. We believe that this is more consistent with the Rural Task Force's proposal to increase the dollar values in the formula for each year since the cap was implemented, than the two years referenced in the Recommendation.[187] Although the corporate operations expense cap was implemented in 1998, the formula was based on 1995 cost data.[188] Because support in year 2001 is based on 1999 cost data, we will increase the dollar values in the formula to reflect increases in GDP-CPI from 1995 to 1999. In subsequent years, the per-line allowable expense amount shall be adjusted annually by GDP-CPI. We find that these modifications to the corporate operations expense limitation will adequately account for increases in corporate operations expenses since the cap originally was adopted.

74. We recognize that smaller carriers in particular may be affected by the current corporate operations expense limit and agree with the Rural Task Force that the waiver process can be a very expensive option for small carriers.[189] To reduce the need for small carriers to seek a waiver, the Commission previously raised the minimum cap in the corporate operations expense limitation formula to $300,000.[190] We adopt further protections for small carriers by raising the minimum cap in the revised formula. Specifically, we permit carriers with 6,000 or fewer loops to receive support for corporate operations expenses of up to $600,000 or amounts derived from the revised corporate operations expense formulas, whichever is greater.[191] We find that by raising the minimum cap from $300,000 to $600,000 an increased number of small carriers will have expenses that fall within the revised limitation. Consistent with current rules, we propose that if a carrier's actual corporate operations expenses are less than $600,000 then the carrier would recover high-cost loop support based on its actual corporate operations expenses.

75. We find that raising the minimum cap in the corporate operations expense limitation formula to address the needs of smaller carriers is preferable to the alternative proposed by the Rural Task Force. The Rural Task Force's proposed alternative calculation would essentially eliminate the corporate operations expense limitation currently in effect. We note that the corporate operations

[186] *See* Rural Task Force Recommendation at 26.

[187] *See id.* at 28 & n.55.

[188] *See supra* n.158.

[189] *See* Rural Task Force Recommendation at 28-29. The Rural Task Force noted that one Alaska carrier received a waiver, but only for one year.

[190] *See supra* para. 62.

[191] *See* 47 C.F.R. § 36.621.

expense limitation was adopted, in part, to prevent carriers from recovering from the high-cost loop support mechanism excessive expenditures unrelated to the provision of supported services.[192] The limitation is designed to allow carriers to receive support for corporate operations expenses based on typical expenses for companies of comparable size. As demonstrated by the graph in Appendix D, some carriers are extreme outliers and have corporate operations expenses that far exceed the average range of expenses for companies of comparable size. The Rural Task Force's proposal would permit these outliers to receive support for these uncapped expenses as if the corporate operations expense limitation had never been adopted.[193] For example, under the Rural Task Force proposal, these outliers could include in the high-cost loop support mechanism either their actual corporate operations expenses in 2001 or their actual per-line expenses in the year 2000, increased by the rural growth factor and the number of lines served in 2001. The latter would be more than 2001 actual expenses if a carrier's per line actual expenses increase by more than the rural growth factor. A carrier would only receive less than the adjusted, uncapped 2000 amount in future years if its actual corporate operations expenses were lower in those years. The Rural Task Force's proposal therefore would provide no incentive for carriers to limit their corporate operations expenses.

76. By imposing a reasonable limit on the universal service support available for carriers' corporate operations expenses, we are not precluding carriers that incur unusually high corporate operations expenses from receiving support for such expenses. To the extent that individual companies continue to incur corporate operations expenses that exceed the limitation, they may ask the Commission to waive these rules on a case-by-case basis.[194]

C. Support Above the Cap

1. Safety Net Additive

a. Background

77. In addition to the existing support provided by the high-cost loop fund, the Rural Task Force proposed a "safety net additive," which would provide additional support to carriers "who make significant investment in rural infrastructure."[195] Safety net additive support would only be available in years in which support levels would otherwise exceed the new indexed cap on the high-cost loop support fund.[196] To receive such support in a particular study area, a carrier would need to show that growth in telecommunications plant in service (TPIS)[197] per line is at least 14 percent greater than the study area's

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[192] *See Fourth Order on Reconsideration*, 13 FCC Rcd at 5374 para. 92.

[193] *See* Texas Commission Comments at 4 (suggesting that the Commission consider raising the corporate operations cap for very small rural carriers "rather than eliminating the limitation in its entirety").

[194] We clarify that the Commission's rules do not preclude a multi-year waiver. *See* California Commission Comments at 11 ("California supports a change to the waiver process that would allow a multi-year waiver if a petitioner supports the need for a waiver for more than one year."). The Rural Task Force stated that the waiver process "has yielded petitioners only a one-year waiver" and cited an example in which this was the case. Rural Task Force Recommendation at 28 & n.55. The Commission's rules do not require a carrier to seek a waiver every year if a waiver is granted for a longer period of time.

[195] *See Joint Board Recommended Decision* at para. 19; *see also* Rural Task Force Recommendation at 27.

[196] Rural Task Force Recommendation at 27. In years when the cap is not triggered, rural carriers would receive support in an amount that would cover the added expense associated with the new investment, and thus it is unnecessary to provide safety net additive support in those years.

TPIS per line in the prior year, or the "base year."[198] As proposed, safety net additive support would allow a carrier to recover 50 percent of the difference between the capped and uncapped expense adjustment for the qualifying year.[199] Any study area that initially qualifies for safety net additive support would also qualify for such support in each of the four succeeding years if the cap is again triggered, regardless of whether the study area meets the 14 percent criterion in the succeeding years.[200]

78. In the *Further Notice*, the Commission sought comment on issues relating to implementation of the safety net additive mechanism. Specifically, the Commission asked whether the safety net additive mechanism would allow carriers to recover more than 100 percent reimbursement of their incremental loop investment and on any other implementation issues raised by the Rural Task Force's plan.[201]

b. Discussion

79. We agree with the Joint Board, the Rural Task Force, and several commenters that we should adopt some form of safety net additive that will provide additional support to those rural carriers that have made significant investment in years in which the fund is capped.[202] We believe that providing this additional support will provide rural carriers with appropriate incentives to invest in the network infrastructure serving their communities. As the Rural Task Force stated in *White Paper 3*, which reviewed alternatives to the current embedded cost mechanism, no mechanism for universal service support is without weaknesses.[203] The Rural Task Force, however, also recognized that a mechanism could be designed so that it mitigates specific weaknesses.[204] One of the identified weaknesses of an embedded cost mechanism that incorporate an overall cap is that it may hinder the ability of rural carriers to invest in infrastructure.[205]

80. While we make modifications to the operation of the safety net additive mechanism proposed by the Rural Task Force, we find that the implementation of a safety net mechanism is a reasonable consensus approach arrived at by competing interests to mitigate the potential negative effects of a cap, and provide rural carriers with the predictability to make investments in their communities.[206]

(Continued from previous page)

[197] TPIS is an accounting category used by the Commission and carriers to classify certain elements of their operation. TPIS includes, for example, the carrier's cable and wire facilities, poles, central office switching facilities, public telephone terminal equipment, and customer premises wiring. It also includes general support facilities such as buildings, office equipment, and general purpose computers. 47 C.F.R. §32.2001.

[198] Rural Task Force Recommendation at 27. The Rural Task Force stated in its recommendation that the 14 percent figure represents an estimate of two times the average rural growth factor in recent years.

[199] *Id.* The "qualifying year" is the first year in which the study area meets the criterion for receiving support.

[200] *Id.* Safety net additive support would only be available in years in which the cap is triggered because, in years when the cap is not triggered, carriers would already receive 100 percent of their expense adjustment.

[201] *See Further Notice* at para. 7.

[202] *See Joint Board Recommended Decision* at para. 19; *see also* Rural Task Force Recommendation at 27; AT&T Comments at 15; NRTA, OPASTCO, & USTA Comments at 6; Texas Commission Comments at 5; Telecom Consulting Associates Comments at 11.

[203] *Alternative Mechanisms for Sizing a Universal Service Fund for Rural Telephone Companies: Rural Task Force White Paper 3* (Aug. 2000) (visited May 2, 2001) <http:www.wutc.wa.gov/rtf> at 29 (*White Paper 3*).

[204] *Id.* at 29.

[205] *Id.* at n.10.

[206] *White Paper 3* at 29.