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

In the Matter of	)	
	)	
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

To: The Commission

REPLY TO OPPOSITION TO PETITIONS FOR RECONSIDERATION

The South Dakota Telecommunications Association (SDTA), Townes Telecommunications, Inc., and Public Service Telephone Company (the Rural Service Coalition) hereby reply to the oppositions filed against SDTA's Petition for Reconsideration in the above-referenced proceeding by the Competitive Universal Service Coalition (CUSC), the Rural Consumer Choice Coalition (RCCC) and the Association of Communications Enterprises (ASCENT). Each of the Rural Service Coalition parties serve sparsely populated rural areas characterized by low subscriber density and high loop costs. These parties are very substantially affected by the Commission's unexpected policy shift treating all common line costs as a "subsidy" and its related action reclassifying Transport Interconnection Charge (TIC) amounts and requiring common line costs, formerly recovered under traffic sensitive rate structure, to be

portable. Among these parties filing this joint Reply, SDTA filed a Petition or Reconsideration which is supported by both the Townes companies and Public Serve Telephone Company. Specifically, this Reply responds to the RCCC's arguments concerning the nature of the common line rate element and the arguments concerning portability of the CUSC, RCCC and ASCENT. The Rural Service Coalition also supports the Plains Rural Independent Companies' (Plains Companies') Petition for Reconsideration concerning the transport interconnection charge (TIC).

INTRODUCTION

In its Petition for Reconsideration, SDTA described the unlawful elements of the Commission's decision to eliminate common line (CCL) charges to interexchange carriers in favor of a portable universal service mechanism. The petition specifically described the lack of record support to conclude that 100% of rural loop costs, currently recovered by CCL charges, represent a "subsidy," and that such amounts have long been considered as a legitimate cost of doing business by the courts and the Commission.[1] Under these circumstances, the Commission's decision as currently written cannot pass muster as rational decision making under the arbitrary and capricious standard of appellate review.[2]

RCCC'S VIEW OF IMPLICIT SUBSIDY MISSES THE MARK

The RCCC, consisting of AT&T, General Communication Inc., and Western Wireless, opposed SDTA's Petition for Reconsideration on this point.[3] RCCC argues that, contrary to SDTA's Petition, the entire category of NTS costs are in fact an implicit subsidy, citing the *1997 Access Reform Order*;[4] it argues that certain Court of Appeals decisions[5] make "clear" that the

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1 SDTA Petition for Reconsideration, pp. 5-6.

2 *Id.*, pp. 3-4.

3 RCCC Opposition to Petitions for Reconsideration, pp. 10-12.

4 *Access Charge Reform, First Report and Order* 12 FCC Rcd. 15982 (1997) ("1997 Access Charge Reform Order").

Commission can "...legally recover 100% of loop and other...costs from the end user..." and it argues that certain appellate cases relied upon by SDTA are inapplicable, either because the cases dealt with cost allocation and not cost recovery, and were pre-1996.[6]

While none of these arguments can successfully justify the Commission's decision to transform legitimately incurred costs into subsidies, the absence of any discussion of the record by RCCC is certainly noteworthy. SDTA's Petition for Reconsideration pointed out that no effort was made by the Commission to identify in the record those loop costs which contain "subsidy" amounts, and those that do not.[7] The absence of a record on this point is not a trifling oversight, since the agency is charged under the arbitrary and capricious standard with articulating a satisfactory explanation for its action against the facts found.[8] This lack of a record no doubt prompted RCCC's doctrinaire defense of the Commission's decision based on the theory that, since the Commission may "legally recover 100% of loop...costs from the end user," all other loop costs must be a subsidy.[9]

But the Commission's decision is not grounded upon RCCC's proffered rationale. Instead, the "implicit subsidy" finding turns on the Commission's analysis of how the long distance carriers recover costs from their own customers, whose rates and rate structure, of course, remain untouched by the Commission's regulatory hand.[10]

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5 Southwestern Bell v. FCC, 153 F.3d 523 (8th Cir. 1998); Texas Office of Public Utility Counsel v. FCC, 265 F3d 313 (5th Cir. 2001).

6 *Id.*, pp10-12.

7 SDTA Petition for Reconsideration, p. 5.

8 Motor Vehicle Mfrs. Ass'n. v. State Farm Auto Ins. Co., 463 U.S. 29 (1983).

9 *See*, RCCC Opposition, p.9.

10 *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and interexchange Carriers*, Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket Nos. 98-77 and 98-166, ¶¶ 61-2, n. 192 (FCC 01-304)(rel. November 8, 2001) ("*MAG*" or "*MAG Order*").

What emerges from close examination of the Commission's *MAG* decision is that the Commission impermissibly confused the CCL rate structure[11] with the underlying costs. More than once, the Commission has recognized the intermingled nature of universal service-related costs within interstate access and that such intermingling requires a careful examination of such costs.[12] The Commission noted that such intermingling (and hence the need for examination) exists with "any implicit support mechanism."[13]

Indeed, the Commission performed such an examination in the CALLS proceeding[14] when it identified approximately $650 million in universal service costs which were intermingled with interstate access[15] and even provided an opportunity for an examination of company specific costs to determine these amounts.[16] And, while the Commission's inquiry in the CALLS proceeding far outstrips its efforts here in terms of actually examining intermingled "subsidies," it bears mentioning that even the Commission's CALLS effort could not pass appellate muster.[17]

RCCC's allergy to the record in this proceeding is matched by its other efforts to explain away the flaws of the Commission's decision. In this regard, and as noted earlier, RCCC argues that Smith v. Illinois Bell, 282 U.S. 133 (1930) and Rural Telephone Coalition v. FCC, 838 F.2d

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11 SDTA assumes for argument's sake only that the Commission is justified in determining that traffic sensitive recovery of common line costs constitutes "implicit subsidy" because of how interexchange carriers recover those costs from their customers in an unregulated environment. SDTA does question this logic.

12 *1997 Access Charge Reform Order*, 12 FCC Rcd 15989-15990, n.16.

13 *Id.*

14 *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262 and 94-1, Sixth Report and Order, Low-Volume Long-Distance Users, CC Docket No. 99-249, Report and Order, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Eleventh Report and Order, 15 FCC Rcd 12962 ("CALLS Order"), aff'd in part, rev'd in part, and remanded in part, Texas Office of Public Util. Counsel et al. v. FCC, No. 00-60434 (5th Cir. September 10, 2001).

15 See *CALLS Order*, ¶¶ 198-205.

16 *Id.* at ¶ 197.

17 Texas Office of Public Util. Counsel et al. v. FCC, No. 00-60434 (5th Cir. September 10, 2001)

1307 (D.C. Cir. 1988), (and both relied upon in SDTA's reconsideration petition) are distinguishable because they dealt with cost allocation, and not cost recovery, and because they pre-dated the 1996 Act.[18] Both of these criticisms are off the mark. In Rural Telephone Coalition, for instance, the Court rejected MCI's argument that NTS costs are a subsidy in significant part because "there is no purely economic method of allocation...[of such costs]"[19] The court's specific reliance on the 1982 MCI case, issued one year before the Commission adopted end-user surcharges for partial common line recovery, exposes RCCC's claim as untrue that the end-user charge policy was "the main reason" that MCI's subsidy argument was rejected. Indeed, the suggestion is naïve, to say the least, that either the Rural Telephone Coalition case, or the 1982 MCI case, carry less weight because they dealt with cost allocation. MCI's arguments were based upon the real expectation that it would have to pay for the costs which it unsuccessfully had branded as "subsidy," not because it enjoyed an abstract economic debate. NARUC v. FCC,[20] cited several times by RCCC, itself recognizes that Smith's separations process does not deal simply with labels ("local telephone costs are real")[21] while holding that the FCC could properly order cost recovery charges through end user charges.

That the Commission has required RCCC's members to pay CCL access charges for their use of loop plant in providing interstate services certainly does not render such charges a "subsidy." The Rural Telephone Coalition Court's observation that no purely economic allocation exists for these costs is as valid today as in 1988. And if there is a subsidy produced within the rate structure of the unregulated long distance industry, it has yet to be identified, or

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18 RCCC Opposition, pp. 11-12.

19 Rural Telephone Coalition at 1314 *citing* MCI Telecommunications Corp. v. FCC, 218 U.S. App. D.C. 389, 675 F.2d 408, 416 (D.C. Cir. 1982). Also see, SDTA Petition for Reconsideration, pp. 4,5.

20 NARUC v. FCC 737 F.2d 1095 (D.C. Cir. 1984)

21 NARUC, 737 R.2d 1095, 1114.

even examined in this proceeding. In short, nothing in RCCC's Opposition detracts from the conclusion that the entire NTS category (less end user charges) is not a subsidy.

Finally, RCCC's suggestion that the 1996 Act evidently erases pre-1996 precedent on this score, merits brief discussion. The suggestion is made because the 1996 Act prohibits "implicit subsidies."[22] This begs the question, of course, since the primary question is whether costs currently recovered by CCL charges are really a "subsidy." The Rural Service Coalition submits, obviously, that such costs are clearly not a subsidy. The 1996 Act does not add or detract to the debate, except to the extent that Congress did not intend that the 1996 Act disturb the existing interstate access charge regime.[23] RCCC's argument on this score is meritless.

In sum, the Commission should reconsider its decision to lump all costs recovered through CCL charges into the "implicit subsidy" category. No inquiry has been made by the Commission as to what intermingling of costs within the common line access charge category could properly be deemed as "implicit subsidy," a particularly exacting task given the long distance industry's rate structure as a contributing factor to this "subsidy." Moreover, court precedent suggests that such costs are not a prohibited subsidy at all, but merely are real costs having no purely economic method of allocation. The fact that the *MAG Order* seizes on the rate structure itself, as opposed to the underlying costs, underscores the fact that the Commission's earlier analysis was misdirected, and should be reconsidered.

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22 RCC Opposition, p. 12.

23 47 U.S.C. § 254(b)(3) requires that "[c]onsumers in all areas of the Nation ,...should have access to telecommunications...that are reasonably comparable to those services...[and] rates charged for similar services in urban areas." 47 U.S.C. § 254(g) requires "the rates charged by providers of interexchange telecommunications services to subscribers in rural and high cost areas shall be no higher than...[rates] in urban areas." A provider of interstate interexchange telecommunications services is required to "provide such services...in each State at rates no higher than the rates charged...in any other State." *Id.*

OPPOSERS' MISS THE MARK ON PORTABILITY

In its Petition, SDTA demonstrated that the Commission's decision that ICLS should be portable to competitors will create a new subsidy by rewarding competitors with the cost-based CCL revenue streams of the ILECs, regardless of the competitors' own costs. As demonstrated by SDTA, the substitution of one subsidy to cure another alleged subsidy is irrational and clearly wrong.

CUSC, ASCENT and RCCC attempt to refute SDTA's position on the portability of the ICLS by stating, essentially, that the Commission previously has found that universal service subsidies must be available to all eligible telecommunications carriers; that competitive neutrality compels that the same amount of support per line be given to carriers competing in the same market; and that the Commission's portability requirement has been upheld by the courts. CUSC, ASCENT and RCCC, however, fail to address SDTA's argument and ignore that the facts, circumstances and Commission's findings require a different result in connection with the portability of ICLS.

As an initial matter, and as demonstrated herein, the CCL, which will be converted to ICLS, is not a subsidy and the Commission has failed to conduct any inquiry as to the amount of the common line costs recovered by CCL that might properly be classified as an "implicit subsidy." In the *MAG Order*, the Commission found that rural rate-of-return LECs should be able to set rates to recover their interstate access costs based on their historic booked costs. In addition, the Commission found that rural LECs should be allowed to set rates based on an 11.25 percent rate-of-return. The Commission specifically established the ICLS to recover that portion of the ILECs' allowed interstate revenues, as determined by historic booked costs and an 11.25

percent return, that exceeds the revenues recoverable through subscriber line charges. According to the Commission, ICLS "will recover any shortfall between the allowed common line revenues of rate-of-return carriers and their SLC revenues..."[24] and, as a result, it "will ensure that changes in the rate structure do not affect the overall recovery of interstate access costs by rate-of-return carriers serving high cost areas."[25] Thus, the CCL, and now the ICLS, represent the rural carriers' allowed interstate revenue requirement-- not a universal service subsidy.

This is different from the other universal service fund mechanisms implemented by the Commission, in which the Commission identified specific subsidy amounts.[26] Since the ICLS is not a subsidy, at a minimum, the Commission should reexamine whether the existing portability rule should apply. The Commission also should suspend application of the portability rules to ICLS in the interim, as requested by the National Telecommunications Cooperative Association[27] in its Petition for Reconsideration.[28]

However, even assuming for the sake of argument that some or all of the CCL is a subsidy, the Commission still should reexamine whether the existing portability rule should apply. As demonstrated by SDTA, the existing portability rule will create a new subsidy to competitors because the ICLS is intended to be a replacement mechanism for the ILEC's interstate revenue requirement as determined by the ILEC's interstate costs. Accordingly, the principle of competitive neutrality will be better served by a different mechanism that does not reward competitors with a subsidy of their own. As noted earlier, administrative agency

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24 *MAG Order*, ¶ 15.

25 *Id.*

26 It is noteworthy that in the *CALLS Order*, the Commission did not adequately explain how it determined that the implicit subsidy in CCL rate element for price cap carriers was $650 million and the Fifth Circuit remanded the issue to the Commission for further determination.

27 NTCA was formerly known as the National Telephone Cooperative Association and its Petition for Reconsideration was filed under that name.

28 *See*, NTCA Petition at 6.

decisions must demonstrate a connection between the facts found and choice made.[29] In short, they must make sense. The decision to require a cost-based revenue requirement to be portable to competitive carriers, regardless of their own costs, fails that test here.

PLAINS' CORRECT OBSERVATION OF TIC

SDTA also files in support of the Petition filed by the Plains Companies concerning the TIC. In its Petition, the Plains Companies demonstrate that the *MAG Order*, which shifts a significant portion of the TIC cost recovery to the common line element, is improper, arbitrary and requires reconsideration. As demonstrated by the Plains Companies, the TIC was designed to recover traffic sensitive transport cost assigned to the local transport element that would not be recovered by the actual transport rate elements. Moreover, there are no specific common line costs recovered by the TIC. The *MAG Order*, however, now reallocates the TIC element to both traffic sensitive and non-traffic sensitive elements. The allocation of traffic sensitive costs across non-traffic sensitive elements is inconsistent with the traffic sensitive nature of the transport costs that are recovered by the TIC and the Commission's policies and principles regarding the alignment of cost recovery with cost causation. Therefore, as requested by the Plains Companies, the TIC should be restored until such time as the costs currently recovered via the TIC can be reallocated to the proper access elements.

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[29] See Motor Vehicle Mfrs. Ass'n. v. State Farm Auto Ins. Co., 463 U.S. 29 (1983). See also SDTA Petition for Reconsideration at pp. 6-8.

CONCLUSION

Based on the foregoing, SDTA respectfully request that the Commission should find the Oppositions filed by CUSC, RCCC, and ASCENT without merit.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I, Douglas W. Everette, hereby certify that I am an attorney with the law firm of Blooston, Mordkofsky, Dickens, Duffy & Prendergast, and that copies of the foregoing "Reply To Opposition To Petitions for Reconsideration" were served by first class U.S. mail or hand delivery on this 25th day of February, 2002 to the persons listed below:

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