

The TELRIC methodology embodies the importance of cost-based pricing. The Commission instructed that in using the TELRIC method, “states may not set prices lower than the forward-looking incremental costs directly attributable to provision of a given element.”<sup>84</sup> Costs that are too low could distort economic investment decisions. As explained by one economic expert, “if UNE prices understate the total costs of unbundled entry, they will systematically bias entrants towards unbundling and away from facilities-based competition.”<sup>85</sup> The short-term harm of such market distortion is that CLECs are encouraged to enter the market primarily via UNEs because the CLEC is guaranteed a steady revenue stream without building its own facilities even when facilities-based competition would otherwise be feasible. Competitors will enter the market solely to benefit from the disparity between the regulated UNE price and the true economic cost of the UNEs. The arbitrage opportunity created by this scenario results in a windfall to the CLEC, and cannot encourage CLECs to build their own facilities or contribute to improvements in services to end-user customers.<sup>86</sup>

The long-term effect of such distortions is the demise of the incumbent *and* the competitor. Over time, “prices that are too low will deter the incumbents from making investments in their own networks because they will have to share the benefits, although not the

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<sup>84</sup> *Id.*

<sup>85</sup> Declaration of Howard A. Shelanski filed with the Comments of SBC in CC Docket 01-338, at ¶ 23 (“*Shelanski Declaration*”).

<sup>86</sup> “[G]reater public benefits flow from facilities-based competition than from the efforts of competitors reselling the ILEC facilities, taking advantage of regulatorily-created opportunities.” Declaration of Alfred E. Kahn and Timothy J. Tardiff filed with Comments of Verizon in CC Docket 01-338, at ¶ 19 (“*Kahn & Tardiff Declaration*”).

full costs, with competitors using UNEs.”<sup>87</sup> Additionally, such prices will undermine those CLECs that have invested in their own facilities.<sup>88</sup>

**2. TELRIC assumes deployment of forward-looking technology at the location of the ILECs wire centers, not a reconfiguration of the network.**

In developing the TELRIC methodology, the Commission expressly rejected a cost model based on a purely hypothetically designed network. Therefore, the Commission intended states to take into consideration some inefficient characteristics of the ILEC’s existing network. In its *Local Competition First Report and Order*, the Commission considered an approach in which the forward-looking economic cost for interconnection and unbundled elements are based on the “most efficient network architecture, sizing, technology, and operating decisions that are operationally feasible and currently available to the industry.”<sup>89</sup> However, the Commission concluded that this approach to network design “may discourage facilities-based competition by new entrants because new entrants can use the incumbent LEC’s existing network based on the cost of a hypothetical least-cost, most efficient network.”<sup>90</sup>

Instead, the Commission opted for a rule in which the “forward-looking pricing methodology for interconnection and unbundled network elements should be based on costs that assume that wire centers will be placed *at the incumbent LEC’s current wire center locations*, but that the design for the remainder of the reconstructed local network will employ the most efficient technology for reasonably foreseeable capacity requirements.”<sup>91</sup> The Commission

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<sup>87</sup> Shelanski Declaration at ¶24.

<sup>88</sup> *Id.*

<sup>89</sup> *Local Competition First Report and Order* at ¶ 683.

<sup>90</sup> *Id.*

<sup>91</sup> *Local Competition First Report and Order* at ¶ 685 (emphasis added); *see also*, 47 C.F.R. § 51.505(b)(1).

reasoned that this “hypothetical network architecture” would most closely represent the incremental costs that ILECs “actually could expect to incur” in making UNEs available to new entrants.<sup>92</sup> Thus, while UNE prices may be based on a forward-looking network technology, which might require the states to hypothesize that the ILEC would in the future employ a technology it has not yet deployed, the states must also take into account the existing infrastructure – the current location of the ILEC’s existing wire centers.<sup>93</sup>

**3. UNE prices must be based on *the ILEC’s* costs, not a national average or a hypothetical carrier’s costs**

Both the statute and the Commission’s rules reference “*the ILEC’s* costs,” and neither makes any mention of “a carrier” or “average” or “hypothetical” costs. The *Local Competition First Report and Order* contains numerous references to the costs and attributes of a specific ILEC. “As a result of the availability to competitors of the incumbent LEC’s unbundled elements *at their economic cost*, consumers will be able to reap the benefits of the incumbent LECs’ economies of scale and scope, as well as the benefits of competition.”<sup>94</sup> Additionally, the Commission explains that the TELRIC methodology aims to “establish[] prices for interconnection and unbundled elements *based on costs similar to those incurred by the incumbent.*”<sup>95</sup> Further, as noted above, the Commission’s requirement that states take into account the actual location of the ILEC’s switches is an indication that UNE costs must reflect “existing network design [and] on efficient, new technology that is compatible with the *existing infrastructure*”<sup>96</sup> of the particular ILEC in question.

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<sup>92</sup> *Local Competition First Report and Order* at ¶ 685 (emphasis added).

<sup>93</sup> *Id.*

<sup>94</sup> *Local Competition First Report and Order* at ¶ 679 (emphasis added).

<sup>95</sup> *Local Competition First Report and Order* at ¶ 679 (emphasis added).

<sup>96</sup> *Local Competition First Report and Order* at ¶ 685.

Furthermore, the Commission's rules require that each state conduct a forward-looking cost study in order to properly establish UNE rates for each ILEC in accordance with TELRIC.<sup>97</sup> The Commission intended that each state examine the costs of each ILEC as part of its obligation to adopt permanent, cost-based UNE rates to replace the FCC's interim proxy prices set forth in section 51.513 of the rules.<sup>98</sup> The state may determine rates either in a rulemaking or in the context of a particular arbitration proceeding,<sup>99</sup> but the FCC left no ambiguity about the state's obligations to review the ILEC's costs.

By requiring states to replace the FCC's interim proxy prices with UNE rates based on a cost study, the Commission acknowledged that nationwide values are not an appropriate measure for UNE pricing. Especially when dealing with costs in Alaska, nationwide values do not adequately approximate ILEC costs. As evidence of this, the Commission, in setting default proxy prices and ranges for pricing UNEs in its *Local Competition First Report and Order*, did not establish such proxies for Alaska:<sup>100</sup>

We are not establishing default loop cost proxies for these areas because we are unsure that comparisons of the population densities of the continental states and of Alaska and other non-contiguous areas subject to the 1996 Act fully capture differences in loop costs. Regulatory authorities in those areas may seek assistance from this Commission should default loop cost proxies be needed before they have completed their investigations of the forward-looking costs of providing unbundled loop elements.<sup>101</sup>

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<sup>97</sup> 47 C.F.R. § 51.505(e).

<sup>98</sup> *Local Competition First Report and Order* at ¶ 619 (“In setting a rate pursuant to the cost-based pricing methodology, . . . the state must give full and fair effect to the economic costing methodology we set forth in this Order and must create a factual record, including the cost study, sufficient for purposes of review after notice and opportunity for the affected parties to participate.”).

<sup>99</sup> *Local Competition First Report and Order* at ¶ 693.

<sup>100</sup> *Local Competition First Report and Order* at ¶ 794.

<sup>101</sup> *Id.*

Thus, the Commission recognized that there are unique factors in the Alaska market that makes the use of national averages wholly inappropriate.

**4. The TELRIC rules assume a hypothetical network design, but require actual costs incurred to construct such a network.**

The Commission's TELRIC methodology assumes a hypothetical network design, however, nowhere in the rule does the Commission refer to hypothetical costs of constructing such a network, or that costs be based on a hypothetical carrier. The rule indicates that "the total element long-run incremental cost of an element should be measured based on the use of the most efficient telecommunications technology *currently available* and the lowest cost network configuration, given the *existing location of the incumbent LEC's wire centers*."<sup>102</sup> The language of the rule does not infer that the other components of TELRIC, the forward-looking cost of capital and depreciation rates, are based on anything other than those of the carrier in question.<sup>103</sup>

In support of this interpretation, the Commission stated in its *Local Competition First Report and Order* that TELRIC "is designed to permit incumbent LECs to recover their economic costs of providing interconnection and unbundled elements, which may minimize the economic impact of [the Commission's] decisions on incumbent LECs, including small incumbent LECs."<sup>104</sup> Further, TELRIC includes "a depreciation rate that reflects the true changes in economic value of an asset and a cost of capital that appropriately reflects the risks incurred by an investor."<sup>105</sup> It is clear that the Commission intended TELRIC prices to reflect carrier-specific cost inputs, not nationally averaged costs or other hypothetical costs. For instance, the costs of constructing a hypothetical network in Alaska would be higher than the

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<sup>102</sup> 47 C.F.R. § 51.505(b)(1) (emphasis added).

<sup>103</sup> See 47 C.F.R. § 51.505(b)(2), (3).

<sup>104</sup> *Local Competition First Report and Order* at ¶ 697.

<sup>105</sup> *Id.* at ¶ 703.

costs of constructing a hypothetical network in the continental U.S. because of Alaska's higher labor costs and the higher prices for components in this region.<sup>106</sup>

**5. The U.S. Supreme Court has affirmed the FCC's TELRIC methodology.**

The U.S. Supreme Court has affirmed the FCC's forward-looking cost model for determining UNE prices.<sup>107</sup> The Court approved the Commission's adoption of a cost model that takes into consideration the existing location of the ILEC's wire centers. The Court recognized that this requirement built some "inefficiency" into the TELRIC standard. As a result, UNE rates should not be set as if the ILEC could always deploy the most efficient technology immediately upon its introduction.<sup>108</sup> Therefore, a state may not price elements, such as UNE loops, as if the ILEC's wire centers could be "relocated for a snugger fit."<sup>109</sup> The implication of the Court's example is especially apt in Alaska: UNE loop prices must be based on the ILEC's actual loop lengths and costs, based on where its wire centers are located, not some shorter loop length that may exist elsewhere in the country.

Additionally, the Court confirmed the conclusion that the universal service model is not appropriate for determining UNE prices. In *Iowa Utilities III*, the Court rejected an argument by the ILECs in which they compared an estimate of a TELRIC valuation of building a new and efficient national system of local exchanges providing universal service and the actual "total plant" value on the industry balance sheet for the same time period. The ILECs argued that the size of the disparity demonstrated that TELRIC would necessarily result in confiscatory rates. The ILECs used the same universal service model relied on by the RCA. The Supreme

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<sup>106</sup> Affidavit of Timothy J. Tardiff at ¶ 12 ("Tardiff Affidavit"), Attachment C.

<sup>107</sup> *Iowa Utilities III*.

<sup>108</sup> *Iowa Utilities III*, slip op. at 34.

<sup>109</sup> *Iowa Utilities III*, slip op. at 33.

Court disagreed with the ILECs, noting that the ILECs' TELRIC value in that example was unreasonably low because, it was "based on constructing a barebones universal-service telephone network, and so it fails to cover elements associated with more advanced telecommunications services that incumbents are required to provide by lease under 47 U.S.C. § 251(c)(3)."<sup>110</sup> The Court declined to guess the appropriate TELRIC value, however, it stated that it "can reasonably assume that [the ILECs' TELRIC value] is too low."<sup>111</sup> Likewise, the RCA's use of the universal service model (the Synthesis Model) results in an unreasonably low TELRIC estimate.

**B. The RCA disregarded the TELRIC rules.**

**1. Anchorage**

The current UNE rates to which ACS-Anchorage is currently subject violate the cost-based pricing principle of the TELRIC methodology. The current UNE rate of \$14.92 in Anchorage is based on a statement by GCI's attorney during oral argument regarding the result of the FCC Synthesis Model substituting inputs used in the Fairbanks arbitration.<sup>112</sup> GCI did not submit documentary support for this proposed rate. Therefore, as these are national average default-based inputs (inadequately adjusted to account for Alaska conditions), the current rate is in no way based on ACS's costs in Anchorage. The RCA set this rate as an interim rate in order to relieve ACS of even lower interim UNE prices established by the RCA's predecessor agency, the APUC, in 1997.

At the time the parties arbitrated the original interconnection agreement, the Commission's *Local Competition First Report and Order* had been recently released, and the

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<sup>110</sup> *Iowa Utilities III*, slip op. at 54-55 (citing the Commission's explanation in the *Inputs Order* that the universal-service model may not be appropriate for determining prices for unbundled network elements).

<sup>111</sup> *Id.* at 55.

<sup>112</sup> Oral Argument in Docket No. U-96-89, transcript at 150 (Reg. Comm. of Alaska August 17, 2001).

1997 rates were not determined in accordance with TELRIC. The RCA's predecessor agency agreed to approve the rates in the interconnection agreement on a temporary basis, to give it time to conduct a forward-looking cost study, as the Commission's rules instruct state commissions to do. However, neither the APUC nor the RCA have developed forward-looking cost-based UNE rates for Anchorage that are compliant with the Commission's TELRIC methodology. In Anchorage, where ACS has lost approximately *half* of the residential market primarily to one UNE-based competitor, Alaska never even purported to conduct a study of ACS's costs, but promised it would do so – a promise still unfulfilled six years after passage of the Telecommunications Act. Moreover, despite repeated requests for a schedule to resolve the matter, the RCA has failed to calendar a hearing in this proceeding. While the RCA complies with the nine-month timeframe mandated by the Act when CLECs seek arbitration, ACS's request with respect to rates in Anchorage has been pending at the RCA for two and a half years.

## **2. Fairbanks**

### **a. The UNE rates for Fairbanks are not cost-based.**

During arbitration, the RCA hearing officer stated that “before the FCC default inputs should be replaced by company specific values, it must be shown that the proposed specific company inputs is [sic] reflective of an efficient, least cost company in a competitive marketplace.”<sup>113</sup> The hearing officer concluded that ACS had not met this burden of showing that their proposed company specific cost inputs were those of an “efficient, least cost company in a competitive marketplace.” However, the Commission explicitly rejected this approach in

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<sup>113</sup> See *Arbitration Decision on Model Inputs*, U-99-141, U-99-142, U-99-143 (Reg. Comm. of Alaska July 17, 2000).

adopting the TELRIC model.<sup>114</sup> Therefore, the arbitrator selected the input values based entirely on the wrong standard.

Because the UNE rates were based on purely hypothetical costs, the RCA approved below-cost UNE prices that result in a windfall to GCI and encourage behavior, which would be justified neither under market conditions, nor TELRIC-based pricing. Since the price GCI pays per UNE loop (\$19.19) is well below both the embedded cost (\$33.51) and ACS's forward-looking cost (about \$36.00), GCI is presented with an arbitrage opportunity (further exacerbated by the portability of the high-cost support) it would be foolish not to seize.<sup>115</sup>

**b. The UNE rates in Fairbanks do not take into consideration ACS-specific costs.**

During the Fairbanks arbitration, the RCA went through the motions of conducting a cost study but instead of considering the cost *to ACS* of providing the UNEs in question, a set of nationally averaged costs was the starting point, using the universal service

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<sup>114</sup> *Local Competition First Report and Order* at ¶ 683.

<sup>115</sup> Further exacerbating the confiscatory rates is the fact that under existing FCC rules, GCI is entitled to significant USF subsidies. Although its costs of providing service are unknown, its costs appear to be significantly below the FCC benchmark for high cost loop support. High cost loop support for competitive carriers is currently based on the underlying carrier's costs, and not the cost of the competitive carrier. See 47 C.F.R. § 54.307. The RCA certified GCI as an Eligible Telecommunications Carrier ("ETC") even though it did not comply with requirements to disclose the uses of support money. See *Commission Compliance with Federal Requirements to Certify Proper Use of Federal Universal Service Funds by Telecommunications Carriers*, U-01-90 (6) (Reg. Comm. of Alaska Apr. 18, 2002); *Request by GCI Communications Corp d/b/a General Communication, Inc., and d/b/a GCI for Designation as a Carrier Eligible to Receive Federal Universal Service Support Under the Telecommunications Act of 1996 for the Fairbanks, Fort Wainwright, and Juneau Areas*, U-01-11 (1) (Reg. Comm. of Alaska Feb. 19, 2002); *Request by GCI Communications Corp d/b/a General Communication, Inc., and d/b/a GCI for Designation as a Carrier Eligible to Receive Federal Universal Service Support Under the Telecommunications Act of 1996 for the Fairbanks, Fort Wainwright, and Juneau Areas*, U-01-11 (2) (Reg. Comm. of Alaska Aug. 28, 2001). The RCA reasoned that because GCI's rates equaled ACS's rates, there must be no improper use of funds, even though the RCA never reviewed GCI's costs. The RCA's flawed logic allows GCI to continue to take advantage of the below-market UNE rates.

Synthesis Model for non-rural carriers. However, the FCC and the U.S. Supreme Court have noted that this Model is inappropriate for determining UNE rates.<sup>116</sup>

ACS submitted a forward-looking cost study that complied with section 51.505(e) of the FCC's rules. The RCA disregarded this study and instead adopted the Synthesis Model with the FCC's default inputs or GCI's proposed inputs. GCI's proposed inputs selected by the arbitrator were essentially the same as the FCC default value but with a minor adjustment factor.<sup>117</sup> Such adjustments were not nearly enough to approximate realistic costs for a facilities-based LEC in Alaska. By acknowledging that costs in Alaska are higher, GCI merely attempted to give the appearance of fairness in offering a slightly increased cost input.<sup>118</sup> In reality, however, ACS's increased costs in Alaska are represented by the ACS cost study. Furthermore, GCI's adjustment factors were not based on any actual costs. As discussed in the Wilks Affidavit, GCI in some cases used its own actual costs, even though it does not maintain an area-wide network.<sup>119</sup>

Under the Commission rules, UNE rates should be determined based on the location of the ILEC's wire centers and the ILEC's costs to construct the otherwise hypothetical network. Therefore, ACS's UNE rates should be based on the most efficient network available *in Alaska* and on new technology that is compatible with existing infrastructure *in Alaska* and on

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<sup>116</sup> See *Platform Order* at ¶ 12; *Iowa Utilities III*. Furthermore, the Synthesis Model represents the costs of a local carrier providing only narrowband service in a non-rural market, whereas ACS's actual forward-looking costs reflect the provision of services over a network with advanced capabilities. Affidavit of Timothy J. Tardiff, filed with the RCA in U-99-141, U-99-142, U-99-143 ¶ 5 (Feb. 11, 2000); Affidavit of Walter J. Haug, filed with the RCA in U-99-141, U-99-142, U-99-143 ¶ 8 (Feb. 10, 2000).

<sup>117</sup> See *In the Matter of Interconnection Agreement Between General Communication, Inc. and PTI Communications of Alaska, Inc. Telephone Utilities of the Northland, Inc. and Telephone Utilities of Alaska, Inc.*, Arbitration Decision on Model Inputs, Interconnection Arbitration U-99-141, U-99-142, U-99-143 (July 17, 2000). See also, Wilks Affidavit at ¶ 21; see generally, Tardiff Affidavit.

<sup>118</sup> See Wilks Affidavit; Tardiff Affidavit.

<sup>119</sup> Wilks Affidavit at ¶ 21.

ACS's cost to construct that network *in Alaska*. If a state commission fails to take the location of the ILEC's wire centers and the ILEC's costs into account, the UNE price will be based on a purely hypothetical network, which the FCC explicitly rejected.<sup>120</sup>

By adopting the Synthesis Model and related inputs, the RCA implemented a hypothetical carrier model that did not reflect any costs specific to ACS's territory and therefore, did not take into account the location of ACS's wire centers. Because the FCC's rules require costs to reflect the actual location of the ILEC's wire centers and the cost to the ILEC, construction and related costs, will be actual forward looking costs of an Alaska carrier and are unaffected by the use of a most efficient, least cost hypothetical network model. Therefore, the RCA's use of hypothetical costs of constructing the hypothetical network is inconsistent with the TELRIC methodology.

Additionally, the RCA approved the arbitrator's decision to use these actual, or slightly adjusted, FCC Synthesis Model default inputs for almost all variables.<sup>121</sup> Like the Synthesis Model, the default inputs measure the wrong costs entirely because they were designed to measure costs for non-rural companies with lower costs than those of rural companies in Alaska.<sup>122</sup> The default inputs are largely based on the costs in the lower 48 states, which reflect lower labor rates and volume discounts available to the regional Bell operating companies.<sup>123</sup> Further, as indicated in the Tardiff Affidavit, because the FCC's inputs generally combine labor and material costs into a single value, there appears to be no way to properly adjust the inputs to

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<sup>120</sup> *Local Competition First Report and Order* at ¶ 683.

<sup>121</sup> See *Order Approving, In Part, and Modifying, In Part, Arbitrator's Recommendation*, U-99-141(9), U-99-142(9), U-99-143(9) (Reg. Comm. of Alaska August 24, 2000).

<sup>122</sup> *Universal Service Report and Order* at ¶ 255.

<sup>123</sup> Wilks Affidavit; Tardiff Affidavit.

reflect labor cost differences in Alaska.<sup>124</sup> Therefore, the RCA's failure to consider ACS's rural attributes violates TELRIC.<sup>125</sup>

In sum, UNE prices in Anchorage and Fairbanks were developed without reference to the ILEC's costs and therefore fail to comply with the FCC's TELRIC rules as affirmed by the U.S. Supreme Court.

#### IV. ACS IS BEING SUBJECTED TO CONFISCATORY RATES.

##### A. **The Commission should look to tariff law to determine whether UNE rates are confiscatory.**

There is not yet a body of case law on what constitutes a confiscatory UNE rate because UNEs are a relatively new creation of law. UNE rates differ from tariffed rates because UNE prices are meant to be governed by market forces. Where the market for UNEs fails, regulators substitute arbitration for the market determination of rates. UNE rates, however they are established, are embodied in an agreement between the parties approved by the state. On the other hand, tariffed rates are established solely by regulators.<sup>126</sup> The legal effect and structure of a tariff is different from that of an interconnection agreement. Nonetheless, it is helpful to look to case law governing tariffed rates to determine when UNE rates are confiscatory.<sup>127</sup>

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<sup>124</sup> Tardiff Affidavit at ¶ 12.

<sup>125</sup> Furthermore, in calculating proxy costs for unbundled loop elements in the *Local Competition First Report and Order*, the Commission determined that "some upward adjustment is warranted as a safety margin to ensure that the [proxy] ceiling captures the variation in forward-looking economic costing prices on a state-by-state basis. [The Commission] therefore chose[] to adjust the hybrid cost estimates upward by five percent for each state." *Local Competition First Report and Order* at ¶ 794. The Commission cited the fact that the proxies were developed based on studies that were conducted by a small number of states. The RCA, however, did not build any type of cushion into the costs produced by the Synthesis Model and the default inputs, or otherwise attempt to reflect the higher than average costs in Fairbanks.

<sup>126</sup> In fact, in Alaska, the UNE rates were established solely by regulators, and in that sense, they are more like tariffed rates than contractual rates.

<sup>127</sup> The U.S. Supreme Court in *Iowa Utilities III* confirmed that the principle established in *FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944) ("it is not theory, but the impact of the rate order which counts")

In addition to violating section 252 of the Act, the UNE prices set by the RCA are confiscatory. The Fifth Amendment to the Constitution of the United States provides that “private property shall [not] be taken for public use without just compensation.”<sup>128</sup> The United States Supreme Court has long held that this injunction applies not only to physical invasions or trespass, but also to governmental restrictions on the use of private property that amount to a taking.<sup>129</sup> Applying the Fifth Amendment to a regulated utility, if a rate set by a state public utility commission “does not afford sufficient compensation, the State has taken the use of utility property without paying just compensation and so violated the Fifth and Fourteenth Amendments.”<sup>130</sup> Similarly, in the context of regulatory ratemaking for public utilities, it is well-settled that “the Constitution protects utilities from being limited to a charge for their property serving the public which is so ‘unjust’ as to be confiscatory.”<sup>131</sup>

There is not one constitutionally mandated method for determining rates, for “circumstances may favor the use of one ratemaking procedure over another.”<sup>132</sup> Nevertheless, “[i]t is not theory, but the impact of the rate order which counts,”<sup>133</sup> for “[t]he Constitution protects the utility from the net effect of the rate order on its property” and not against particular

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applies to UNEs even though the Court declined to find TELRIC per se confiscatory. *Iowa Utilities III*, slip op. at 53, 54.

<sup>128</sup> U.S. Const. amend. V. Under the Fourteenth Amendment, “[no state] shall . . . deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.” U.S. Const. amend XIV.

<sup>129</sup> See, e.g., *Reagan v. Farmers’ Loan & Trust Co.*, 154 U.S. 362, 410 (1894).

<sup>130</sup> *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 308 (1989).

<sup>131</sup> *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 307 (1989); *FPC v. Texaco, Inc.*, 417 U.S. 380, 391-92 (1974); *FPC v. Natural Gas Pipeline Co.*, 315 U.S. 575, 585 (1942).

<sup>132</sup> *Duquesne Light*, 488 U.S. at 315–16; see also *Wisconsin v. FPC*, 373 U.S. 294, 309 (1963); *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944).

<sup>133</sup> *Hope*, 320 U.S. at 602.

infirmities in the method actually employed.<sup>134</sup> Thus, so long as the rate fixed is within the “zone of reasonableness,” the Constitution’s protections against unjustly compensated takings are not implicated.<sup>135</sup>

A rate is confiscatory if it is “so unjust as to destroy the value of [the] property for all the purposes for which it was acquired,” and thereby “practically deprive[s] the owner of property without due process of law.”<sup>136</sup> In this regard, the Constitution requires the “return to the equity owner [to] be commensurate with returns on investments in other enterprises having corresponding risks,”<sup>137</sup> and “[a] public utility is entitled to such rates as will permit it to earn a return . . . equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding risks and uncertainties.”<sup>138</sup>

Although a rate is not *per se* confiscatory because a utility would fail to make a profit or be forced to operate at a loss if subjected to such a rate,<sup>139</sup> “the due process clause has been applied to prevent governmental destruction of *existing* economic values.”<sup>140</sup> Instead, “there must be a reasonable judgment having its basis in a proper consideration of all relevant

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<sup>134</sup> *Duquesne Light*, 488 U.S. at 314.

<sup>135</sup> *Natural Gas Pipeline*, 315 U.S. at 585–86.

<sup>136</sup> *Covington & Lexington Turnpike Road Co. v. Sandford*, 164 U.S. 578, 597 (1896).

<sup>137</sup> *Hope*, 320 U.S. at 603.

<sup>138</sup> *Bluefield Water Works & Improvement Co. v. Public Serv. Comm’n of W. Va.*, 262 U.S. 679, 692–93 (1923); see also *Duquesne Light*, 488 U.S. at 310 (“[W]hether a particular rate is ‘unjust’ or ‘unreasonable’ will depend to some extent on what is a fair rate of return given the risks under a particular rate-setting system, and on the amount of capital upon which the investor are entitled to earn that return.”).

<sup>139</sup> The Supreme Court has held that regulation does not insure that the business shall produce net revenues or that the regulated business make a profit. See *Natural Gas Pipeline*, 315 U.S. at 590; *Market St. Ry. Co. v. Railroad Comm’n of Cal.*, 324 U.S. 548, 566–67 (1945).

<sup>140</sup> *Market St. Ry. Co. v. Railroad Comm’n of Cal.*, 324 U.S. 548, 566–67 (1945) (emphasis added). The due process clause “has not and cannot be applied to insure values or to restore values that have been lost by the operation of economic forces.” See *id.*

facts,”<sup>141</sup> including “the economic impact of the regulation, the extent to which it interferes with investment-backed expectations, and the character of the governmental action.”<sup>142</sup> Although in the end this inquiry is “essentially . . . ad hoc [and] factual in nature,”<sup>143</sup> it is a necessary component of the constitutionally mandated “balancing of the investor and the consumer interests.”<sup>144</sup>

**B. The Commission Can and Should Act to Prevent Irreparable Harm to ACS and the Public.**

**1. The Commission has jurisdiction to preempt the RCA**

The Commission has the authority to grant ACS relief from the RCA’s confiscatory rates. Section 252(e)(5) of the Act provides that:

if a State commission fails to act to carry out its responsibility under this section in any proceeding or other matter under this section, then the Commission shall issue an order preempting the State commission’s jurisdiction of that proceeding or matter within 90 days after being notified (or taking notice) of such failure, and shall assume the responsibility of the State commission under this section with respect to the proceeding or matter and act for the State commission.<sup>145</sup>

This preemption authority is not limited to enforcing the states’ obligations under section 252 to mediate or arbitrate interconnection agreements.

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<sup>141</sup> *Minnesota Rate Cases*, 230 U.S. 352, 434 (1913).

<sup>142</sup> *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 432 (1982).

<sup>143</sup> *Kaiser Aetna v. United States*, 444 U.S. 164, 175 (1979).

<sup>144</sup> *Hope*, 320 U.S. at 603; *see also Jersey Cent. Power & Light Co. v. FERC*, 810 F.2d 1168, 1177–78 (D.C. Cir. 1987) (“In reviewing a rate order courts must determine whether or not the end result of that order constitutes a reasonable balancing, based on factual findings, of the investor interest in maintaining financial integrity and access to capital markets and the consumer interest in being charged non-exploitative rates. Moreover, an order cannot be justified simply by a showing that each of the choices underlying it was reasonable; those choices must still add up to a reasonable result.”). Although *Hope* primarily addressed a statutory requirement that rates set be just and reasonable, “the *Hope* test defines the point at which a rate become unconstitutionally confiscatory as well.” *Jersey Central*, 810 F.2d at 1175. The Supreme Court did nothing to alter this jurisprudence when it upheld TELRIC. *See Iowa Utilities III*, slip op. at 53, 54.

<sup>145</sup> 47 U.S.C. § 252(e)(5).

**a. Under the Starpower Preemption Order, the Commission may assert jurisdiction if a state fails to act under Section 252.**

In the *Starpower Preemption Order*, the Commission held that it may, under section 252(e)(5), preempt a state that fails to interpret and enforce an existing interconnection agreement.<sup>146</sup> There is nothing in the language or legislative history of section 252(e)(5) to prevent the FCC from preempting state actions that clearly violate the pricing standards set forth in section 252(d)(1). As in the *Starpower* case, ACS seeks resolution of confiscatory rates arising from interconnection agreements approved by the RCA. Although there is an interconnection agreement between ACS and GCI in Anchorage, the RCA approved the UNE rates as temporary and interim rates because they were not based on the TELRIC methodology. The agreement is silent as to the rates applicable after 1999, however, the RCA has still not arbitrated new UNE rates. ACS has repeatedly requested that the RCA perform a TELRIC-based cost study in Alaska, but the RCA has failed to carry out its responsibility under section 252(d)(1) of the Act and section 51.505(e)(2) of the FCC's rules.<sup>147</sup>

As described in section II.D.2 above, the RCA has subjected ACS-Anchorage to interim rates for the past five years. Despite ACS-Anchorage's repeated requests for a new proceeding, the RCA has not even set a schedule for arbitration of a new interconnection agreement. If the Commission refuses to preempt the RCA for its failure to set new UNE rates in the last five years, ACS-Anchorage will have no recourse against the RCA for the UNE rates that it believes are confiscatory. ACS must simply wait at the mercy of the RCA while it continues to lose primary lines and market share to GCI, who is taking advantage of the

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<sup>146</sup> *Starpower Communications, LLC Petition for Preemption of Jurisdiction of the Virginia State Corporation Commission Pursuant to Section 252(e)(5) of the Telecommunications Act of 1996*, Memorandum Opinion and Order, 15 FCC Rcd 11277 (2000) ("*Starpower Preemption Order*").

<sup>147</sup> 47 U.S.C. § 252(d)(1); 47 C.F.R. § 51.505(e)(2).

confiscatory rates. Therefore, because the RCA has failed to act to carry out its responsibility under section 252, the Commission should preempt the RCA and implement the appropriate methodology to determine reasonable UNE rates. ACS asks the Commission to preempt the RCA immediately because five years of inaction demonstrates that the RCA will not act if given 90 days to comply with the rules. Based on the extreme and unprecedented hardship facing ACS, the Commission should preempt the RCA immediately.

**b. The state's assertion of sovereign immunity waives its right to object to FCC jurisdiction.**

The Commission has held that a state commission's refusal to apply federal rules to arbitration of an interconnection agreement is a failure to act to carry out its responsibility under section 252(e)(5).<sup>148</sup> In the *WorldCom Preemption Order*, the Commission preempted the Virginia Public Utilities Commission ("VA PUC"). The VA PUC indicated that it would arbitrate the interconnection agreement under state law instead of federal law because it would be waiving its sovereign immunity by arbitrating under federal law and subjecting itself to federal court review under section 252(e)(6).<sup>149</sup> The Commission held that this was a failure to act to carry out its responsibilities under section 252 of the Act and preempted the VA PUC. The RCA in this instance has failed to arbitrate the interconnection agreements between the Rural Companies and GCI in accordance with the Commission's rules and federal law regarding the determination of UNE pricing. The RCA did not apply TELRIC, but rather, it applied its own method of determining UNE rates. Therefore, ACS asks that the Commission preempt the RCA in this instance because it has failed to arbitrate the interconnection agreements between the

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<sup>148</sup> *Petition of WorldCom, Inc. for Preemption of Jurisdiction of the Virginia State Corporation Commission Pursuant to Section 252(e)(5) of the Telecommunications Act of 1996 and for Arbitration of Interconnection Disputes with Verizon-Virginia, Inc.*, Memorandum Opinion and Order, 2001 FCC LEXIS 411 (Jan 19, 2001) ("*WorldCom Preemption Order*").

<sup>149</sup> *Id.* at ¶ 4.

Rural Companies and GCI in accordance with the Commission's rules and federal law regarding UNE pricing.

Additionally, when ACS sought review of the UNE rates of ACS-Fairbanks in the District Court of Alaska pursuant to section 252(e)(6) of the Act, the RCA attempted to avoid judicial review, claiming sovereign immunity.<sup>150</sup> By applying its own rules in setting UNE rates instead of the Commission's rules, and then refusing to subject itself to federal court review under section 252(e)(6), the RCA effectively is submitting the matter to the Commission, as the VA PUC did in the *WorldCom* case.<sup>151</sup> Likewise, the RCA has failed to act to carry out its responsibilities under section 252 of the Act and therefore, the Commission should preempt the RCA.

**c. In upholding the FCC's TELRIC methodology, the U.S. Supreme Court has upheld FCC preeminence in establishing standards for UNE pricing.**

The U.S. Supreme Court has affirmed the authority of this Commission to interpret sections 251 and 252 and establish guidelines for the states in setting UNE pricing. Under section 201(b) of the Act, "[t]he FCC has rulemaking authority to carry out the 'provisions of this Act' which include §§ 251 and 252, added by the Telecommunications Act of 1996."<sup>152</sup> Because of this explicit authority, the Supreme Court in *Iowa Utilities I* rejected the argument that Commission jurisdiction was only conferred by the Telecommunications Act of

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<sup>150</sup> *Memorandum of Support of Motion to Dismiss, ACS of Fairbanks, Inc. v. GCI Communication Corp.*, A-00-288-CIV (JKS) (October 17, 2001).

<sup>151</sup> The U.S. Supreme Court has recently decided that U.S. district courts have jurisdiction to hear suits for declaratory or injunctive relief against state commissioners in their official capacity for claims arising out of a State's review or enforcement of an interconnection agreement or arbitration under Section 252. See *Verizon Maryland, Inc. v. Public Service Comm'n of Maryland*, 122 S.Ct. 1753 (2002). However, the FCC remains the only forum that can provide effective relief to ACS. During the time it takes to obtain an adjudicated decision from a district court, ACS will suffer sever harm from the current UNE rates, which it believes are confiscatory.

<sup>152</sup> *Iowa Utilities I* at 378.

1996 as to a few matters. Further, the Supreme Court's opinion in *Iowa Utilities III* affirms the Commission's authority to adopt a cost methodology to be applied by the state commissions.<sup>153</sup> The limitation of the Commission's authority in section 2(b)<sup>154</sup> of the Act does not override the explicit authority Congress grants to the Commission in sections 201(b), 251 and 252.<sup>155</sup> Similarly, section 252(e)(5) does not narrow the Commission's authority to grant the relief that ACS requests in this petition, but is an express mandate (as the title indicates) for the "Commission to act if state will not act."<sup>156</sup>

**2. The FCC has demonstrated its willingness and authority to review UNE rates that may be confiscatory.**

The Commission has expressed its willingness to review cases in which the UNE pricing mechanism has failed, recognizing the possibility that the TELRIC pricing mechanism could have a confiscatory effect. In the *Local Competition First Report and Order*, the Commission acknowledged that, even in promoting competitive entry, it would not establish a pricing methodology that denies ILECs a reasonable opportunity to earn a lawful return on their investment.<sup>157</sup> The FCC recognized that, in some cases, TELRIC might produce inadequate rates. Therefore, the Commission indicated that "[i]ncumbent LECs may seek relief from the Commission's pricing methodology if they provide specific information to show that the pricing methodology, as applied to them, will result in confiscatory rates" and promised to revisit the issue of confiscatory pricing, although it has not yet done so.<sup>158</sup>

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<sup>153</sup> See *Iowa Utilities III*.

<sup>154</sup> 47 U.S.C. 152(b).

<sup>155</sup> *Iowa Utilities I* at 379.

<sup>156</sup> 47 U.S.C. §§ 252(e)(5), 251, 252.

<sup>157</sup> *Local Competition First Report and Order* at ¶¶ 682, 685.

<sup>158</sup> *Local Competition First Report and Order* at ¶ 739; see also, *id.* at ¶ 707 ("To the extent that any such residual consists of costs of meeting universal service obligations, the recovery of such costs can and

In its brief filed with the Supreme Court on June 8, 2001, the Commission reiterated the availability of a federal remedy for state-mandated rates that produced a confiscatory effect.<sup>159</sup> The Commission there indicated that ILECs may seek relief from the TELRIC pricing methodology if they provide specific information to show that the pricing methodology as applied to them will result in confiscatory rates. The Supreme Court in *Iowa Utilities III* cited the Commission's offer to consider a challenge to rates in advance of a rate order, resulting from the TELRIC methodology.<sup>160</sup> As demonstrated in this petition, ACS has suffered and will continue to suffer under the confiscatory rate scheme implemented by the RCA unless the Commission intervenes and establishes a proper methodology for setting appropriate UNE rates.

ACS requests that the Commission apply forward-looking UNE prices based on the forward-looking costs of ACS's current network. The RCA has refused to apply the FCC's rules on UNE pricing; these rules have now been upheld by the U.S. Supreme Court. The RCA's own faulty methodology has resulted in confiscatory rates. Therefore, ACS urges the Commission to apply the controlling law established by the Supreme Court and in the Commission's own rules in order to relieve ACS from being further subjected to these confiscatory rates.

With respect to ACS-Anchorage, section 252(e)(6) review in federal district court is not available because the RCA has not made a determination, as required under that

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should be considered in our ongoing universal service proceeding. To the extent a significant residual exists within the interstate jurisdiction that does not fall within the ambit of section 254, we intend that to address that issue in our upcoming proceeding on access reform.”).

<sup>159</sup> Brief for Respondent FCC at 28, *Verizon Communications, Inc. v. Federal Communications Commission*, 531 U.S. 1124 (2001) (Nos. 00-511, 00-555, 00-586, 00-590, 00-602).

<sup>160</sup> *Iowa Utilities III*, slip op. at n.39 (“The FCC, in other words, is willing to consider a challenge to TELRIC in advance of a rate order, but any challenger needs to go beyond general criticism of a method's tendency, and to show with ‘specific information’ that a confiscatory rate is bound to result.”).

provision.<sup>161</sup> ACS is still, after over five years, waiting for a cost study to be conducted and permanent TELRIC-based rates to be established. Although ACS-Fairbanks has brought an action in U.S. district court under section 252(e)(6) on the initial interconnection agreement, ACS does not have an avenue for redress for the confiscatory rates to which ACS currently is being subjected. The RCA refuses to follow the Commission's rules and then asserts sovereign immunity from federal court review. Because the RCA is unwilling to resolve these issues and state courts are explicitly excluded by the statute, ACS is left without a forum to review the confiscatory effect of the UNE rates currently in effect in Fairbanks and in Anchorage, unless the Commission asserts its authority under section 252(e)(5). Therefore, Commission preemption of the state is the only effective remedy for ACS. Due to the uniqueness of the situation in Alaska and the extreme hardship facing ACS, the Commission should step in where the RCA has failed to act to establish TELRIC-based UNE pricing.

### 3. ACS's claim is ripe.

ACS's claim that these rates are confiscatory, unlike the takings claims addressed in *Iowa Utilities II* and *Iowa Utilities III*, are ripe for review by the Commission. The Eighth Circuit declined to entertain claims that TELRIC effects a taking without just compensation in violation of the Fifth Amendment, reasoning simply that such claims as to the TELRIC *method* are not ripe because "it is not theory, but the impact of the rate order which counts" in a takings claim.<sup>162</sup> The Supreme Court reiterated this general rule in *Iowa Utilities III*.<sup>163</sup> In the case of ACS, however, the rates are already defined and have been implemented, and the uncompensated

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<sup>161</sup> 47 U.S.C. §252(e)(6) states that "[i]n any case in which a State commission makes a determination under this section, any party aggrieved by such determination may bring an action in an appropriate Federal district court to determine whether the agreement or statement meets the requirements of Section 251 and this section."

<sup>162</sup> *Hope*, 320 U.S. at 602.

<sup>163</sup> *Iowa Utilities III*, slip op. at 54.

taking is occurring. As explained above, the RCA established the UNE rates in the interconnection agreements based on a theoretical model that had no bearing on ACS's actual network configuration or operation costs. The RCA simply did not follow either the statute or the FCC's rules, and the result is confiscatory rate-making. Thus, ACS does not challenge TELRIC itself under the Fifth Amendment, but rather the confiscatory *effect* of the rates actually adopted by the RCA in Alaska.

**C. The UNE rates set by the RCA are confiscatory and, therefore, effect an unconstitutional taking without just compensation.**

Essentially, the UNE rates in question do not aim to compensate ACS for any measure of its actual costs. In setting these rates, the RCA has not exercised "reasonable judgment having its basis in a proper consideration of all relevant facts," as required by the U.S. Constitution.<sup>164</sup> Therefore, the effect of the UNE rates established by the RCA gives rise to a regulatory taking without just compensation and, as explained above, the amounts lost may not be recoverable under Alaska law. The Tardiff Affidavit describes the large disparity between the Synthesis Model inputs selected by the RCA and those proposed by ACS.<sup>165</sup>

Under the rates set by the RCA, there is no way that ACS's returns can be "commensurate with returns on investment in other enterprises having corresponding risks."<sup>166</sup> In Anchorage, ACS's return on investment is only 2.2%. According to the Meade Affidavit, this return is not high enough to cover ACS's cost of debt.<sup>167</sup> Without a higher return, ACS will be

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<sup>164</sup> *Minnesota Rate Cases*, 230 U.S. 352, 434 (1913).

<sup>165</sup> Tardiff Affidavit.

<sup>166</sup> *Hope Natural Gas Co.*, 320 U.S. at 603.

<sup>167</sup> Meade Affidavit at ¶ 10.

unable to attract capital for investment, and will not be able to fund capital investment from earnings.<sup>168</sup>

The unreasonably low UNE rates set by the RCA disrupt investor expectations by creating a distorted market for UNEs. As discussed in section III.A.1 above, the Commission's rules reflect economic incentives that promote facilities-based entry into the market. Because the RCA's UNE rates are too low, market entrants will be biased towards UNE-based entry because of the windfall gains to these entrants. Therefore, ILECs and other facilities-based carriers will be harmed by this unfair competition. As a result, incentives for facilities-based carriers to upgrade their networks or offer advanced services to customers will be severely attenuated.

Finally, the RCA itself has declared that UNE rates that are as low as the UNE rates set in Fairbanks are unreasonable. As discussed above in Section II.B.2, the RCA indicated in its order terminating ACS's rural exemption in Fairbanks and Juneau, that GCI's proposed hypothetical UNE price of \$27.30 for Fairbanks was unrealistically low.<sup>169</sup> Consequently, the RCA's order setting the UNE rate in Fairbanks at \$19.19 is wholly inconsistent with its reasoning in terminating ACS's rural exemption in the first instance.

**V. THE PUBLIC INTEREST WILL BE HARMED IF THE RCA'S UNE RATES CONTINUE TO APPLY.**

The unreasonably low UNE rates paid by GCI will deny consumers the long-term benefits of having a competitor in the market. These low UNE loop rates have restricted ACS's capital spending and have retarded investment in LEC facilities for both basic and broadband

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<sup>168</sup> *Id.*

<sup>169</sup> *Order Granting Reconsideration and Terminating Rural Exemption*, U-97-82 (11), U-97-143 (11), U-97-144 (11) (Reg. Comm. of Alaska, Oct. 11, 1999); Prefiled Direct Testimony of Robert A. Smith in Docket No. U-97-82 at 26 (April 27, 1999, as modified May 7, 1999).

services.<sup>170</sup> ACS will be unable to upgrade services or even maintain the quality of the existing network. In the long run, consumers will suffer from lower quality services. Additionally, because the improper rates do not encourage CLECs to build new facilities, there will be no facilities alternatives to those of ACS. For both these reasons, in addition to the confiscatory effect of these UNE rates on ACS, the FCC should preempt RCA's UNE rate-making decisions.

**A. The RCA's UNE prices cause immediate harm to all users of ACS's network.**

ACS's capacity to invest in these networks and maintain service is undermined when they are not compensated for their costs. ACS will not satisfy the purpose of the Act itself, to "accelerate rapidly . . . deployment of advanced telecommunications and information technologies and services" if it cannot recover costs necessary to sustain, much less increase, investment in the network.

**B. The RCA's UNE prices thwart the long-term federal policy of encouraging facilities-based competition.**

**1. The Commission strongly supports facilities-based competition.**

In its *Local Competition First Report and Order*, the Commission emphasizes the importance of facilities-based competition, indicating that TELRIC is designed to promote facilities-based competition.<sup>171</sup> Moreover, the Commission has repeatedly emphasized its commitment to promoting facilities-based competition in recent orders.<sup>172</sup> The Commission has

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<sup>170</sup> Meade Affidavit at ¶ 14.

<sup>171</sup> *Local Competition First Report and Order* at ¶ 685.

<sup>172</sup> See, e.g., *Review of Commission Consideration of Applications Under the Cable Landing License Act*, Report and Order, 16 FCC Rcd 22165 (2001) (adopting streamlined procedures for processing applications for submarine cable landing licenses designed to facilitate the expansion of capacity and facilities-based competition; ¶ 1); *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, Second Report and Order and Further Notice of Proposed Rulemaking, FCC 01-304 (rel. Nov. 8, 2001) ("By rationalizing the rate structure for recovery of interstate-allocated loop costs, we are fostering competition for residential subscribers in rural areas by facilities-based carriers." ¶ 11);

stated that it is committed to “ensuring that facilities-based competitors have the incentive and ability to invest in alternative infrastructure and innovative technologies, while at the same time, ensuring that incumbents retain similar incentives and capabilities.”<sup>173</sup>

Additionally, ensuring that facilities based competitors have the incentive and the ability to invest in the goal of promoting facilities-based entry has been discussed frequently in recent statements by the commissioners.<sup>174</sup> Despite its efforts to promote facilities-based competition, the Commission has recognized that some competitors may have the ability but not the incentive to build their own facilities because of the availability of UNEs.<sup>175</sup> ACS urges the Commission to address the ill effects of such competition in order to protect the public interest.

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*Application of Verizon Pennsylvania Inc., Verizon Long Distance, Verizon Enterprise Solutions, Verizon Global Networks Inc., and Verizon Select Services Inc. for Authorization To Provide In-Region, InterLATA Services in Pennsylvania*, CC Docket No. 01-138, Memorandum Opinion and Order, FCC 01-269 (rel. Sept. 19, 2001) (evaluating facilities-based competition in the market in Pennsylvania is part of the determination; ¶ 124)

<sup>173</sup> *Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Fourth Report and Order, 16 FCC Rcd 15435 ¶ 14 (2001).

<sup>174</sup> See, e.g., Separate Statement of Commissioner Michael K. Powell, *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers* (Dec. 12, 2001) (“[The review of unbundling obligations] underscores the Commission’s ongoing commitment to the promotion of facilities-based competition...”); Separate Statement of Commissioner Kevin J. Martin, *Performance Measurements and Standards for Unbundled Network Elements and Interconnection*, Notice of Proposed Rulemaking, FCC 01-331 (rel. Nov. 19, 2001) (“... the promotion of facilities-based competition should be a fundamental priority of the Commission. The goal of the Telecommunications Act of 1996 was to establish an environment that promotes meaningful competition and allows for deregulation. To get to true deregulation, we need facilities-based competition ...”); Competition Policy Institute Forum: *Keeping Telecom Competition on Track*, Address by Commissioner Kathleen Q. Abernathy (Dec. 7, 2001) (“The Commission is now engaged in an effort to restore the incentives for facilities-based investment that Congress intended. The same facilities-based competitive model that has driven the success of the wireless and long-distance marketplaces. This means a shift away from policies that actively encourage resale as a long-term business strategy and force the unbundling of virtually every network element at TELRIC rates.”).

<sup>175</sup> See *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers, Implementation of the Local Competition Provisions of the Telecommunications Act of 1996, Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Notice of Proposed Rulemaking, FCC 01-361, ¶ 23 (rel. Dec. 20, 2001).

**2. Economic studies support facilities-based competition.**

Economic experts have noted that facilities-based competition provides greater public interest benefits than does allowing competitors to take advantage of regulatory-created opportunities.<sup>176</sup> “Facilities-based competition promises far greater benefits than does competition through unbundled access and should never be displaced by unbundling rules.”<sup>177</sup> A carrier who faces competition from rivals with their own networks will have an incentive to cut its own costs and offer new services as a means of gaining market share. A policy allowing substitution of UNEs for facilities-based entry when facilities-based entry is a reasonable possibility creates “the risk of supplanting the substantial benefits of facilities-based entry with the comparatively anemic returns, and potentially high costs, of unbundled access.”<sup>178</sup>

**3. The RCA’s application of the Synthesis Model is detrimental to facilities-based competition.**

Due to the manner by which the RCA has applied the TELRIC methodology, new facilities-based entrants are not likely to exist in the relevant markets in Alaska because it will be more profitable to use ACS’s network and exploit the arbitrage opportunity that exists here. GCI’s participation in the local exchange markets in question demonstrates the adverse affect that the below-market UNE rates have on facilities-based competition. GCI is affiliated with the only local cable television franchisee, and offers a broadband cable modem platform providing high-speed Internet as well as video programming over facilities wholly independent from those

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<sup>176</sup> Kahn & Tardiff Declaration at ¶19; Shelanski Declaration at 2.

<sup>177</sup> Shelanski Declaration at 2.

<sup>178</sup> Shelanski Declaration at ¶16.

of ACS.<sup>179</sup> For some time, it has claimed it has the capability to offer “cable telephony” over its broadband cable TV platform.<sup>180</sup> It apparently has not deployed this capability for the mass market, however. Rather, it provides telephony using its own switching and transport capability but with UNE loops purchased from ACS. ACS believes this is due to the below-cost UNE pricing ACS has been required to offer its competitors in these markets. As a result, ACS-Anchorage is losing hundreds of customers daily. Since unbundling their networks, the Rural Companies have been experiencing a similar trend. ACS urges the Commission to step in to resolve the UNE pricing issues and prevent continued harm to ACS and detriment to consumers in Alaska.

## VI. REQUESTED RULING AND RELIEF

ACS requests immediate action by the Commission to prevent further irreparable harm under the RCA’s UNE rates. First, ACS asks that the Commission declare that the RCA violated the Commission’s rules and sections 251 and 252 of the Act and has failed to carry out its responsibility to arbitrate an interconnection agreement with valid UNE prices that conform to section 252(d)(1) and the *Local Competition First Report and Order*. Second, ACS asks that the Commission declare that the UNE rates established by the RCA are confiscatory in violation of the Fifth and Fourteenth Amendments of the U.S. Constitution.

The Commission has authority under section 252(e)(5) of the Act to order the RCA to arbitrate the terms of interconnection under the proper standards by conducting a

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<sup>179</sup> See General Communication, Inc. SEC Form 10-K for the fiscal year ended December 31, 2001 (SEC File No. 0-15279) at 31-32, available on-line at:

[http://www.nasdaq.com/asp/quotes\\_news.asp?symbol=GNCMA%60&selected=GNCMA%60](http://www.nasdaq.com/asp/quotes_news.asp?symbol=GNCMA%60&selected=GNCMA%60)

<sup>180</sup> *Id.* at 25, 27. See also RCA Order U-01-11(2) (granting GCI request to use its cable facilities to provide CLEC services as an eligible telecommunications carrier within the meaning of Section 214(e) of the Act), available on-line at:

[http://www.state.ak.us/rca/orders/2002/u01011\\_2.pdf](http://www.state.ak.us/rca/orders/2002/u01011_2.pdf)

forward-looking cost study and adopting cost-based UNE rates within 90 days. However, ACS urges the Commission instead to preempt the RCA immediately, and establish UNE rates based on ACS's forward-looking cost studies.

ACS-Anchorage has already endured an unreasonably long delay in the establishment of UNE rates complying with TELRIC. The RCA should not be able to simply ignore the Commission's mandates and escape review by then asserting sovereign immunity. The RCA is not likely to complete the arbitration of new UNE rates in Anchorage or the review of ACS's forward-looking costs, given the fact that it has not been able to accomplish this in two and a half years and given that, under current law, it will have to wind down its affairs beginning on July 1, 2003. Therefore, it will be unable to comply with any such mandates from the Commission. While futilely awaiting the RCA's compliance, ACS will continue to lose market share to GCI. ACS urges the Commission to grant it immediate relief due to the extraordinary circumstances in this case.

Specifically, the Commission should:

(i) preempt the RCA for failing to carry out its responsibilities under section 252 of the Act;

(ii) immediately establish compensatory UNE rates on an interim basis, based on the forward-looking UNE cost data proffered by ACS; and

(iii) conduct a thorough review of ACS's forward-looking costs to confirm the interim rates or establish new rates.

ACS is willing to have new rates adopted on an interim basis, subject to a "true up" between ACS and UNE-based CLECs of any difference in price between such rates and the final rates established by this Commission. The Commission previously approved the use of

interim UNE rates, subject to a truing up between the interconnecting carriers, when it first adopted TELRIC.<sup>181</sup> The Commission recognized that UNE rates should allow ILECs to recoup a reasonable return on investments.<sup>182</sup> ACS has demonstrated that its current UNE rates are confiscatory. Therefore, the Commission should promptly replace those rates with prices supported by ACS's cost study, subject to Commission ultimate review of ACS's costs and determination of TELRIC-based rates for Anchorage and Fairbanks.

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<sup>181</sup> *Local Competition First Report and Order* at ¶ 1066 (“States must adopt “true-up” mechanisms to ensure that no carrier is disadvantaged by an interim rate that differs from the final rate established pursuant to arbitration.”).

<sup>182</sup> *Local Competition First Report and Order* at ¶ 673 (“the price of a network element should include the forward-looking costs that can be attributed directly to the provision of services using that element, which includes reasonable return on investment (i.e., “profit”), plus a reasonable share of the forward-looking joint and common costs.”).

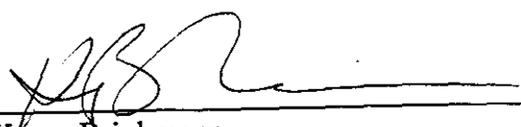
## VII. CONCLUSION

For the foregoing reasons, ACS urgently requests that the Commission issue an Order granting the above-requested relief. In granting this petition, the Commission will ensure that UNE prices in Alaska are set in compliance with the Commission's TELRIC rules.

Respectfully submitted,

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*Their Attorneys*

July 24, 2002

## CERTIFICATE OF SERVICE

I, Richard W. Smith, hereby certify that a copy of the foregoing Emergency Petition for Declaratory Ruling and Other Relief of ACS of Anchorage, Inc. and ACS of Fairbanks, Inc., was delivered to each of the following parties by first-class mail, unless otherwise indicated, on July 24, 2002:

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