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

REPLY COMMENTS OF GENERAL COMMUNICATION, INC.

John T. Nakahata
*Maureen K. Flood
HARRIS, WILTSHIRE & GRANNIS LLP
1200 Eighteenth Street, N.W.
Washington, D.C. 20036
Phone (202) 730-1300
Fax (202) 730-1301
Counsel for General Communication, Inc.

*Telecom Policy Analyst

June 3, 2003

SUMMARY

The comments filed in this proceeding present two views of competition and universal service that stand in stark contrast. One view is that competition is utterly irreconcilable with historical universal service policies in rural, insular and high cost areas. This view, which is advanced largely by rural incumbent local exchange carriers ("ILECs") and their representatives, would maintain the ILECs as monopolies in the name of preserving universal service. This view relies on government regulation of monopolies rather than marketplace forces to ensure that consumer welfare benefits are maximized. Importantly, this first view was rejected by Congress in enacting the Telecommunications Act of 1996 (the "1996 Act").

The second view – embodied in Section 254 of the Communications Act (the "Act") – is that the pre-1996 historical system of implicit universal service support can be replaced with explicit support mechanisms that harness the benefits of competition to improve consumer welfare without sacrificing universal service. The Senate Commerce Committee itself recognized that universal service and competition were mutually reinforcing objectives, with competition and innovation critical to ensuring that universal service goals would be met, over time, at the lowest overall cost to society: "The Committee expects that competition and new technologies will greatly reduce the actual cost of universal service over time, thus reducing or eliminating the need for universal service support mechanisms as actual costs drop to a level that is at or below the affordable rate for such service in an area."[1] GCI agrees that competition and universal

[1] S. Rep. No. 104-23, at 26.

service are complementary policy goals. In fact, one cannot be fully achieved without the other.

The Joint Board should therefore reject any attempt by rural ILECs to rewrite the 1996 Act to shield themselves from the forces of competition under the guise of protecting the integrity of universal service. Rather than retreat into monopoly and forego the consumer welfare benefits of competition, along with the potential for competition and innovation to lower the overall social cost of delivering universal service, the Joint Board should focus on completing the transition from the pre-1996 Act universal service support mechanisms to universal service policies that are compatible with a more dynamic, more competitive telecommunications industry. In doing so, the Joint Board can fully empower consumers to select their preferred provider and thereby harness the proven power of competition to deliver enduring benefits to consumers without artificially subsidizing competitive entry.

The record confirms that, seven years after the passage of the Act, the Commission's universal service policies for rural, insular and high cost areas are still a hodgepodge of mechanisms lacking a coherent, unifying framework. Instead of simply providing sufficient, but not excessive, support to ensure that consumers can purchase telecommunication services at affordable and reasonably comparable rates, high cost support today guarantees a portion of the rural ILEC's revenues in the face of competition, irrespective of whether the ILEC is actually the customer's service provider or whether another carrier now provides universal service to that customer.

The Commission has taken steps to make implicit support explicit, which was necessary with the introduction of competition. But as GCI and several other

commenting parties explained, further steps must be taken. The record confirms that the current hodgepodge of universal service policies is unsustainable in competitive markets. Foreclosing competition to maintain the status quo is not an option under the Act, and it also disserves consumers. Instead, the Joint Board and the Commission need to engage in a principled overhaul of high cost support mechanisms, beginning first by better articulating with greater specificity their objectives of reasonably comparable and affordable rates. The Joint Board and the Commission next should clarify critical dimensions of universal service, including whether it encompasses a single line to a home or business or all lines to a home or business, and whether there are specific service quality specifications. Finally, the Joint Board and the Commission should reform the mechanisms for distributing high cost support to eliminate the vestiges of today's rural ILEC entitlement system, and focus high cost support once and for all on benefiting the consumer, not the ILEC. GCI has proposed the following five basic principles to guide efforts to reform USF so it is consumer, rather than ILEC, focused:

> **Principle No. 1: Provide adequate, but not excessive, support.** High cost support must be adequate to ensure that rates are affordable and reasonably comparable, but support should be the lowest amount necessary to achieve these objectives.
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> **Principle No. 2: Deliver support to the service provider.** High cost support should be paid to the service provider that pays the cost of facilities employed to deliver the service to the end user customer. High cost support should not be paid to all potential providers of service, regardless of whether they are actually providing the supported service to the end user customer.
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> **Principle No. 3: Ensure equal opportunity for support.** The support paid to the appropriate provider should be the same for all competitors, regardless of the facilities they employ, the manner in which they procure facilities, or the metric used to determine the per line support level.

Principle No. 4: No double payments. If one carrier gets high cost support for providing a line to a household, another provider should not also get support for providing (or being able to provide) a line to the same household.

Principle No. 5: Let the market work as it would in the absence of subsidies. Other than permitting more consumers to purchase service, high cost support should not alter the competitive signals that the market would send to ILECs and CETCs in the absence of support payments.

To effectuate these five principles and create a more coherent framework that harnesses competition to preserve and enhance universal service at the lowest overall cost to society, GCI has made six specific recommendations to reform the current high cost support mechanisms:

Recommendation No. 1: Eliminate duplicate high cost support payments to ILECs when a CETC serves the end user through a method other than resale.

Recommendation No. 2: Cap per line high cost support within a study area upon CETC entry.

Recommendation No. 3: Reduce per line high cost support when a market can be served at a lower cost.

Recommendation No. 4: Limit high cost support to a single line to a home or business.

Recommendation No. 5: Consolidate study areas within a state for high cost support purposes.

Recommendation No. 6: Define the upper limit of "affordable" and "reasonably comparable" rates.

Adoption of these recommendations would keep faith with Congress' vision of universal service and competition as mutually reinforcing goals, and would not simply retreat into perpetual regulated monopoly, as the ILEC proposals in the comments attempt to do. Instead, GCI's recommendations would ensure that high cost support is targeted to those

areas of the country that truly need such support to ensure affordable and reasonably comparable rates for consumers.

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REPLY COMMENTS OF GENERAL COMMUNICATION, INC.

General Communication, Inc. ("GCI") hereby files reply comments in response to the *Public Notice* ("Notice") issued by the Federal-State Joint Board on Universal Service ("Joint Board") seeking comment on certain of the Federal Communications Commission's ("Commission") rules relating to high-cost universal service support and the Eligible Telecommunications Carrier ("ETC") designation process.[2]

I. INTRODUCTION

The comments filed in this proceeding present two views of competition and universal service that stand in stark contrast. One view is that competition is utterly irreconcilable with historical universal service policies in rural, insular and high cost areas. This view, which is advanced largely by rural incumbent local exchange carriers ("ILECs") and their representatives, would maintain the ILECs as monopolies in the name of preserving universal service. This view relies on government regulation of

[2] *See* Federal-State Joint Board on Universal Service Seeks Comment on Certain of the Commission's Rules Relating to High-Cost Universal Service Support and the ETC Designation Process, Public Notice, CC Docket No. 96-45 (rel. Feb. 7, 2003) ("*Public Notice*").

monopolies rather than marketplace forces to ensure that consumer welfare benefits are maximized. Importantly, this first view was rejected by Congress in enacting the Telecommunications Act of 1996 (the "1996 Act").

The second view – embodied in Section 254 of the Communications Act (the "Act") – is that the pre-1996 historical system of implicit universal service support can be replaced with explicit support mechanisms that harness the benefits of competition to improve consumer welfare without sacrificing universal service. The Senate Commerce Committee itself recognized that universal service and competition were mutually reinforcing objectives, with competition and innovation critical to ensuring that universal service goals would be met, over time, at the lowest overall cost to society: "The Committee expects that competition and new technologies will greatly reduce the actual cost of universal service over time, thus reducing or eliminating the need for universal service support mechanisms as actual costs drop to a level that is at or below the affordable rate for such service in an area."[3] GCI agrees that competition and universal service are complementary policy goals. In fact, one cannot be fully achieved without the other.

The Joint Board should therefore reject any attempt by rural ILECs to rewrite the 1996 Act to shield themselves from the forces of competition under the guise of protecting the integrity of universal service. Rather than retreat into monopoly and forego the consumer welfare benefits of competition, along with the potential for competition and innovation to lower the overall social cost of delivering universal service, the Joint Board should focus on completing the transition from the pre-1996 Act

[3] S. Rep. No. 104-23, at 26 (1995).

universal service support mechanisms to universal service policies that are compatible with a more dynamic, more competitive telecommunications industry. In doing so, the Joint Board can fully empower consumers to select their preferred provider and thereby harness the proven power of competition to deliver enduring benefits to consumers without artificially subsidizing competitive entry.

The record confirms that, seven years after the passage of the Act, the Commission's universal service policies for rural, insular and high cost areas are still a hodgepodge of mechanisms lacking a coherent, unifying framework.[4] Instead of simply providing sufficient, but not excessive, support to ensure that consumers can purchase telecommunication services at affordable and reasonably comparable rates, high cost support today guarantees a portion of the rural ILEC's revenues in the face of competition, irrespective of whether the ILEC is actually the customer's service provider or whether another carrier now provides universal service to that customer.

The Commission has taken steps to make implicit support explicit, which was necessary with the introduction of competition. But as GCI and several other commenting parties explained, further steps must be taken. The record confirms that the current hodgepodge of universal service policies is unsustainable in competitive markets. Foreclosing competition to maintain the status quo is not an option under the Act, and it also disserves consumers. Instead, the Joint Board and the Commission need to engage in a principled overhaul of high cost support mechanisms, beginning first by better

[4] The federal Universal Service Fund has several components. GCI's comments and these reply comments concern High Cost Fund support ("high cost support") mechanisms for rural, rate-of-return ILECs. "Rate-of-return ILEC" refers to ILECs that are subject to rate-of-return regulation for interstate revenues. Most, but not all, rate-of-return ILECs also meet the definition of "rural telephone company" in 47 U.S.C. § 153(37).

articulating with greater specificity their objectives of reasonably comparable and affordable rates. The Joint Board and the Commission next should clarify critical dimensions of universal service, including whether it encompasses a single line to a home or business or all lines to a home or business, and whether there are specific service quality specifications. Finally, the Joint Board and the Commission should reform the mechanisms for distributing high cost support to eliminate the vestiges of today's rural ILEC entitlement system, and focus high cost support once and for all on benefiting the consumer, not the ILEC. GCI has proposed the following five basic principles to guide efforts to reform USF so it is consumer, rather than ILEC, focused:

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Adoption of these recommendations would keep faith with Congress' vision of universal service and competition as mutually reinforcing goals, and would not simply retreat into perpetual regulated monopoly, as the ILEC proposals in the comments attempt to do. Instead, GCI's recommendations would ensure that high cost support is targeted to those areas of the country that truly need such support to ensure affordable and reasonably comparable rates for consumers.

II. THE JOINT BOARD MUST DEVELOP A COHERENT, CLEAR AND TRANSPARENT SET OF OBJECTIVES AND SERVICE CHARACTERISTICS FOR HIGH COST SUPPORT

The comments make clear that the Joint Board and Commission must further clarify the objectives and characteristics of universal service. Commenting parties make a wide range of assumptions about the nature of the services that are to be delivered using

high cost support, with some commenters, particularly rural ILECs, arguing that ETC designations should be based on a laundry list of service characteristics not currently included in the definition of universal service.[5] Other commenters buttress their assertions that universal service has evolved to "anytime, anywhere" connectivity to the Public Switched Telephone Network ("PSTN")[6] with the Commission's 1997 decision to merely postpone implementation of the Joint Board's recommendation to limit high cost support to a single residential or business connection.[7] Moreover, there has never been a clear articulation of what constitutes an "affordable" and "reasonably comparable" rate for rural ILECs, which means the actual objective of the Commission's universal service policies remains shrouded in a haze of ambiguity. The Joint Board and the Commission cannot seriously evaluate issues regarding the portability of high cost support and ETC designations without addressing the fundamental questions of what service it is trying to support and what constitutes an affordable and reasonably comparable rate.

A. Diverse Commenters Make Clear that the Joint Board Must Precisely Define the Upper Limits of Rate Affordability and Reasonable Comparability.

Sprint[8] and SBC[9] agree with GCI that a singular flaw of the Commission's high cost support mechanisms has been the failure to define with any specificity the regulatory outcome that these mechanisms seek to achieve. Section 254(b)(1) of the Act states that

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5 *See, e.g.,* CenturyTel Comments at 22-24; OPASTCO Comments at 46-47; NASUCA comments at 8-10.

6 *See, e.g.,* Western Wireless Comments at 2-3, 10; Dobson Comments at 8.

7 *Federal-State Joint Board on Universal Service*, Report and Order, 12 FCC Rcd 8776, 8829 (1997) ("*Universal Service First Report & Order"*).

8 *See* Sprint Comments at 15-20.

9 *See* SBC Comments at 6.

universal service should be available at "affordable" rates[10] and Section 254(b)(3) states that residents of rural, insular and high cost areas should pay rates that are "reasonably comparable to rates charged for similar services in urban areas."[11] However, while rates are supposed to be "affordable" and "reasonably comparable," the Commission has never seriously examined the *rates* (as opposed to costs) that would violate either affordability or reasonable comparability.

Congress, however, recognized the essential importance of a clear and transparent affordability threshold. The Senate Commerce Committee, in its report accompanying S.652, the bill that ultimately became the 1996 Act, set forth the critical role of the affordability threshold in establishing the level below which no high cost support would be necessary: "For areas where carriers may provide universal service for costs (including a reasonable profit) that are at or below the affordable rate, no [ETC] designation would be needed."[12] Using such a benchmark, the Committee recognized that the Commission could then "reduce or eliminate support payments to areas where they are no longer needed…."[13]

GCI therefore supports Sprint's recommendation that the Joint Board consider a minimum price benchmark for local service that will be a condition for the receipt of high cost support, and revise high cost support mechanisms to factor in the additional revenues received by moving to a more cost-based approach to pricing.[14] Under this approach, an ETC would not receive high cost support if its retail rates for the supported universal

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10 47 U.S.C. § 254(b)(1).

11 47 U.S.C. § 254(b)(3).

12 S. Rep. No. 104-23, at 31-32.

13 *Id.* at 29.

14 *See* Sprint Comments at 15-16.

services (at least in the absence of any explicit, intrastate USF support) fell below the minimum affordable price benchmark. Similarly, GCI believes SBC's proposal to establish an "affordability benchmark" based on a generalized assessment of the ability of non-Lifeline-eligible end users to bear the cost of their own service, and to "provide high cost support only where market-based rates would exceed this threshold," is a step in the right direction.[15] Both proposals would provide a principled basis on which to determine whether a rate is affordable and reasonably comparable. Currently, without such a limiting principle, the Commission has no means to determine the amount of high cost support necessary, or even *whether* high cost support is necessary in a given area, to comply with the requirements of Section 254.

There are several shortcomings to the Commission's current approach. First, the Commission's current two-pronged definition of "affordability," which includes "an absolute component ('to have enough or the means for')" and "a relative component ('to bear the cost of without serious detriment')"[16] is vague and indefinite, bearing a striking resemblance to the formulation of "reasonably comparable" rejected by the Tenth Circuit Court of Appeals as legally inadequate.[17] Without defining its objectives more precisely, the Commission will continue to have difficulty both in defending its application of this definition against criticism that it has acted in an arbitrary and capricious manner, and in sending proper signals to the market and the states about the extent of federal high cost support. The Sprint and SBC proposals, in contrast, do not suffer from vagueness

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15 *See* SBC Comments at 6.

16 *Universal Service First Report & Order*, 12 FCC Rcd. 8776, 8837 (¶ 110) (1997).

17 *Qwest v. FCC,* 258 F.3d 1191, 1202 (10th Cir. 2001) ("*Qwest"*).

because they allow the Commission to actually quantify whether a rate is "affordable" and "reasonably comparable" based on objective criteria.

Second, the Commission's failure to adequately define the terms "affordable" and "reasonably comparable" means that the Commission lacks the ability to determine whether USF in fact provides high cost support that is "sufficient," as required by Section 254(e).[18] By its plain meaning, the term "sufficient" can only be defined with respect to its goal – answering the question "sufficient to do what?" Too little support, resulting in rates that are not affordable or reasonably comparable, violates the sufficiency requirement. However, too much support raises its own set of concerns. As the Fifth Circuit held, "excessive funding may itself violate the sufficiency requirements of the Act," because "excess subsidization in some cases may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market."[19] Without any benchmark for determining whether retail rates are affordable or reasonably comparable, there is no way to assure that support is adequate, but not excessive: USF likely provides high cost support where it is not needed, and may also provide inadequate support where it is needed. GCI agrees with Sprint that an initial focus on rates rather than costs "could go far in controlling the size and growth of the high cost program" and better comply with the requirements of Section 254(e).[20]

Third, the failure to apply a specific, rate-based affordability and comparability threshold to High Cost Loop Support ("HCLS") for rural ILECs violates Section 254(f) by permitting a state to unnecessarily "rely on or burden Federal universal service

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18 47 U.S.C. § 254(e).

19 *Alenco Communications, Inc. v. FCC*, 201 F.3d 608, 620 (5th Cir. 2000) *("Alenco")*.

20 *See* Sprint Comments at 16.

support mechanisms."[21] Using USF to subsidize intrastate retail rates that are below the upper limits of affordable and reasonably comparable rate levels violates Section 254(f) by needlessly increasing the high cost support drawn from USF. Sprint correctly states that "[t]here is nothing inequitable in asking financially able customers to pay a price that recovers more of the costs of service," arguing that an "ETC should first ask its own customers to pay a reasonable amount of the costs of service" before seeking high cost support, which is generated by contributions from the customers of other telecommunications carriers.[22] GCI agrees.

Sprint vividly illustrates the current irrationality of retail rates among states that has resulted from the Commission's failure to address affordability and reasonable comparability with specificity: Sprint customers in Wyoming pay $28 per month for local service whereas Sprint customers in North Carolina pay only $6.74.[23] SBC confirms that some "states have done little, if anything, to eliminate the widespread reliance on implicit subsidies in intrastate prices to support universal service, in direct conflict with the Act's requirement that universal service support be specific, predictable, and sufficient."[24] Yet

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21 47 U.S.C. § 254(f).

22 Sprint Comments at 17-18; *see also* SBC Comments at 9 ("To the extent a carrier charges less than an 'affordable' rate for service, there is no justification or basis in the Act for requiring other carriers and customers to subsidize that service.").

23 *See* Sprint Comments at 16-17; *see also* Gregory L. Rosston and Bradley S. Wimmer, "Local Telephone Rate Structures: Before and After the Act," Stanford Institute for Economic Policy Research Discussion Paper No. 01-30 at 17-18, available at http://siepr.stanford.edu/papers/papers_num.html (finding that "there is virtually no relationship between [retail telephone] rates and the cost of providing service to particular customer" and that "the introduction of competition has resulted in a small amount of rebalancing of business rates, but has had very little, if any, effect on urban/rural inequities.").

24 SBC Comments at 4. However, some states have addressed the issue of affordability. The Illinois Commerce Commission, for example, utilizes an affordability benchmark when it calculates support from its own intrastate universal service fund. In essence, rural ILECs are not eligible for support unless their retail rates for universal service exceed a specified, affordable rate. The Illinois commission's use of an affordability threshold was recently upheld in *Harrisonville Telephone Co. v. Illinois Commerce Comm'n*, NO. 5-02-0199, 2003 Ill. App. LEXIS 639 (Ill. App. Ct. May 23, 2003).

the federal high cost support mechanisms ignore entirely whether the resulting retail rates are at or are far below affordable and reasonably comparable levels.

As Sprint points out, clarifying with specificity what constitutes an affordable and reasonably comparable rate for USF purposes does not interfere with a state commission's ability to pursue lower pricing targets using its own intrastate resources. As Sprint notes, a state commission can establish its own universal service program to fund the difference between local rates and the level of the minimum affordable rate established by the Commission.[25] The basic point is that a state must take some responsibility for recovering its own intrastate costs *before* it relies on federal USF. It is inequitable to both customers and carriers to permit one state to establish very low retail rates for local service and then expect interstate customers, particularly those in other states, to pay increased retail rates to offset that state's policy choice.

Importantly, setting a minimum affordable rate as a pre-condition for the receipt of high cost support is not likely to have any discernable impact on telephone penetration rates. The national average rate paid by customers in urban areas for local service is approximately $22.[26] In contrast, the Commission's own data show that the average household now spends more than $80 per month on all telecommunications services.[27] Of this amount, only $12 is spent on long distance services, whereas $36 is spent on service from local exchange carriers ("LECs") and $35 is spent on services from wireless

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[25] *See* Sprint Comments at 18.

[26] *See Federal-State Joint Board on Universal Service,* CC Docket 96-45, Recommended Decision, 17 FCC Rcd. 20716, ¶ 49 (rel. Oct. 16, 2002) ("*Ninth Report & Order Joint Board Recommended Decision"*) *citing Reference Book of Rates, Price Indices, and Household Expenditures for Telephone Service* (FCC Industry Analysis and Technology Div. July 2002).

[27] *See Statistics of the Long Distance Telecommunications Industry, Industry Analysis and Technology Division*, Wireline Competition Bureau, Table 13 (May 2003).

carriers – expenditures that are well above the average retail rate for local service in urban areas.[28] In other words, actual consumer spending on telecommunications shows that raising retail rates to a minimum affordable rate level – even the $28 (plus Subscriber Line Charge) that Sprint charges today in Wyoming – will likely have little impact on telephone penetration.[29] Many non-Lifeline eligible retail customers can pay a rate for local service that more closely reflects the underlying cost of their service. Moreover, because Lifeline mechanisms provide a safety net for customers who are in jeopardy of falling off the network based on economic hardship, any disproportionate impact on the affordability of universal service for lower income consumers can be ameliorated by adjusting Lifeline mechanisms to provide modest additional assistance to these at-risk consumers.

The Joint Board should also consider the availability of wireless services in its evaluation of whether rates meet the affordability and reasonable comparability requirements of Sections 254(b)(1) and (b)(3). The Commission has concluded that wireless carriers provide services within its definition of universal service, and the Commission has generally found that the rates for wireless plans in the rural areas are comparable to wireless rates in urban areas even though wireless service is, for the most part, provided without high cost support.[30] Wireless service rates (as well as the rates of any other carriers in the market) generally place an upper bound on the rates that

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28 *See id.*

29 *See* Sprint Comments at 19.

30 *See Implementation of Section 6002(b) of the Omnibus Reconciliation Act of 1993, Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, 17 FCC Rcd. 12985, 13023 (2002) (citing, for example, an Econ One study finding "that there was virtually no difference in the average monthly charge for wireless service between the [urban and rural wireless service]").

wireline-based service providers, including ILECs, can charge consumers for the supported services alone.[31] Thus, where wireless carriers already offer affordable and reasonably comparable rates without support, there is no reason to expand high cost support to all existing wireless customers in areas where wireless carriers seek ETC designations. To the contrary, the fact that wireless carriers can provide universal service without high cost support in those areas validates Congress' vision that competition and new technologies can eliminate the need for high cost support in some areas.[32]

Better targeting of high cost support by clearly defining "affordable" and "reasonably comparable" rates will reduce unnecessary support and alleviate many of the concerns about fund growth expressed by a wide range of commenters. As GCI explained in its comments, without a meaningful measure of what constitutes an affordable and reasonably comparable retail rate for universal service, it is impossible to allocate high cost support to those areas that really need it, such as the Alaska Bush, and away from those areas that might not, such as Anchorage, Fairbanks and Juneau.[33] Moreover, limiting support to areas that truly need it – and excluding areas where wireless carriers are already providing services within the definition of universal service

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[31] Wireless does not, of course, provide other carriers with an alternative to ILEC-provided access services or UNEs.

[32] Rural ILECs would undoubtedly argue that limiting support in this manner would harm the deployment of advanced services in rural areas. Such an assertion should not be accepted without further empirical verification. GCI has successfully offered high-speed Internet access services in rural Alaska without such support. Similarly, direct-to-home satellite providers offer high-speed Internet access to most of the United States. Furthermore, the Joint Board and the Commission have consistently – and properly – declined to include advanced services in the definition of universal service. *See Federal-State Joint Board on Universal Service*, Recommended Decision, 18 FCC Rcd. 2943, ¶ 11 (rel. July 10, 2002) (declining to "recommend that the Commission expand the definition of supported services to include advanced or high-speed services at this time.").

[33] *See* GCI Comments at 73 (explaining that ACS only receives high cost support for these three communities – which are the largest cities in Alaska – based on the fact that ACS has not consolidated the seven separate study areas served by the company for the purpose of determining high cost support).

at affordable and reasonably comparable rates – will substantially limit the extent to which wireless carriers can receive high cost support for their "installed base," which some parties predict will swell USF to $2 billion annually.[34] High cost support would revert to what Congress truly intended (and which is reflected in GCI Principle No. 1): sufficient, but not excessive support to ensure that all Americans have access to universal service, as defined by the Joint Board and Commission, at an affordable and reasonably comparable rate.

B. The Joint Board Must Also Clarify Whether Supported Services Include Specific Service Quality Standards.

Several rural ILECs, under the guise of competitive neutrality, urge the Joint Board to require CETCs serving rural service areas to comply with service quality standards that are based on the service quality levels offered by the ILEC.[35] Although GCI believes that competitive market pressures render such requirements unnecessary, if the Joint Board and the Commission wish to enforce minimum service quality requirements, they should do so by incorporating objective (rather than ILEC-determined) service quality standards into the definition of universal service pursuant to Section 254(c) of the Act.[36]

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[34] *See* OPASTCO Comments at 10, NTCA Comments at 10; CenturyTel Comments at 12; Alaska Telephone Association Comments at 12. Several commenting parties fear that wireless carriers will race to the FCC and the state commissions for ETC designations, inspired by recent petitions filed by Nextel and Alltel for New York and Pennsylvania, and Alabama Michigan and Virginia, respectively. This "domino effect" results when one wireless carrier receives ETC designation in a market served by several wireless carriers. To avoid being placed at a cost disadvantage relative to the new ETC's high cost support, other wireless carriers will also seek ETC designation. This, of course, will cause USF to swell.

[35] *See, e.g.,* CenturyTel Comments at 4; Alaska Telephone Association Comments at 9.

[36] 47 U.S.C. § 254(c).

As a wireline carrier, GCI provides competitive local, long distance, and advanced telecommunications services through a combination of its own facilities and unbundled network elements ("UNEs") purchased from the incumbent, ACS.[37] GCI already meets or exceeds service quality standards applied to all LECs by the Regulatory Commission of Alaska ("RCA"). As noted by the Rural Cellular Association and the Alliance of Rural CMRS Carriers ("Rural Cellular Association"), despite these regulatory requirements, CETCs like GCI have every incentive to provide high quality service, even without regulatory requirements, because competitive carriers "cannot afford to act like a monopoly because its customers have a choice of service provider."[38] And, a CETC like GCI has "every incentive to maintain high customer satisfaction levels," because the CETC "receives high-cost support only when it gets a subscriber and loses support when a subscriber terminates service."[39] In short, if a customer is not satisfied with GCI's service, the customer can switch to ACS, and GCI will lose high cost support. By contrast, customer satisfaction provides no incentive for ACS, which continues to receive high cost support regardless of which carrier serves the customer. The competitive market truly ensures that high quality telecommunications services are available in Anchorage, Fairbanks and Juneau.

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[37] In GCI's service areas, the ILECs are Alaska Communications Systems Group, Inc. and its operating subsidiaries, ACS of Alaska, Inc., ACS of Anchorage, Inc., ACS of Fairbanks, Inc., and ACS of the Northland, Inc. (collectively "ACS"). ACS is a rate-of-return ILEC. It also is designated as a rural telephone company pursuant to 47 U.S.C. § 153(37) with respect to its Fairbanks and Juneau operations, but not its Anchorage operations. Only ACS of Fairbanks, Inc. ("ACS-F") filed comments in this docket. When GCI's comments discuss its interactions with all of ACS' ILEC subsidiaries, GCI's comments refer to them collectively as "ACS." When GCI discusses ACS of Fairbanks' comments, or GCI's interactions with ACS of Fairbanks, it refers to this ILEC subsidiary as "ACS-F."

[38] Rural Cellular Association Comments at 23.

[39] Smith Bagley Comments at 10.

If the Joint Board and the Commission desire to create minimum service quality requirements for universal service, GCI believes that those requirements should be incorporated into the definition of universal service. By including a minimum service quality requirement in the definition itself, the Joint Board and Commission will ensure that a minimum service quality level is met for all consumers served by ETCs. Further, this approach will be competitively neutral because both ILECs and CETCs must provide universal service at the minimum service quality level to receive high cost support. By contrast, if service quality is merely incorporated into a list of factors that states and the FCC can consider in making ETC designations, service quality will not itself be a clear requirement for all ETCs. Moreover, given that carriers – ILECs and non-ILECs alike – have already been designated as ETCs, evaluating service quality only in the ETC designation process effectively applies service quality review only to new CETCs. This outcome would erect a non-transparent barrier to entry so it would not be competitively neutral.

Service quality standards should also be objective and established by regulators, not ILECs. The rural ILECs' invitation to hold all ETCs to ILEC service quality levels would effectively give the ILEC the authority to set the applicable standard in ways that might exclude efficient competition. For example, it is quite clear that the ILEC proposals are meant to set the minimum service quality level so that many CETCs will not be able to comply, foreclosing access to high cost support and keeping CETCs out of rural telephone company service areas. Also, by linking service quality standards to the method of the ILEC's service offerings, the standards will foreclose innovation. Consumers may be willing to accept a lower level of reliability in order to gain additional

functionality, such as mobility and broader calling scopes (as in the case of wireless) or speed (in the case of broadband access). Importantly, regulation should not prevent consumers from making this choice, particularly in competitive markets served by several providers.

Further, it is not clear that the ILECs in fact provide the "best" quality service. GCI plans to roll out cable telephony throughout its Alaska service areas starting in Anchorage in 2004.[40] Once cable telephony is deployed, GCI believes it will be able to provide consumers with a more robust package of services than ACS. Establishing service quality standards based on the ILEC's historical service levels could short-change consumers by setting the minimum service quality level too low.

In short, the Joint Board should not duck the service quality issue by encouraging state commissions to evaluate a potential ETC's service quality levels – with no criteria – as part of the public interest test under Section 214(e)(2).[41] If universal service does not require a minimum level of service quality, then the Joint Board and Commission should so hold. If the definition of universal service must meet some minimum service quality standard, the Joint Board and the Commission should incorporate such requirement into the definition of universal service pursuant to Section 254(c). Regardless of their decision, the Joint Board and the Commission should clearly express their policy choices so all carriers can make fully informed decisions about whether and where to seek ETC designation.

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40 *See* GCI Comments at 8.

41 47 U.S.C. § 214(e)(2).

C. The Joint Board Must Decide Whether the Scope of Support Will Be a Single Line or All Lines.

The comments also squarely pose the question of whether high cost support should be provided to permit access to the PSTN through a single connection to each home or business, or whether the concept of universal service has evolved to a "new paradigm" of personal communication that provides anytime, anywhere access to the PSTN. GCI agrees with several commenting parties that argue for the former, consistent with the Joint Board's 1996 Recommendation to limit high cost support to a single connection for each residential and business customer.[42]

Limiting support to a single connection has a number of benefits. First, it "would protect the sustainability of the universal service fund and, at the same time, re-focus and enhance high-cost support in a manner that is more consistent with the essential purpose of universal service policies," which is to "provide affordable access to telecommunications services in every household in the United States."[43] In contrast, the current system is "grossly inflating the universal service fund and harming all consumers by increasing the cost of telecommunications services across the nation" by providing support for "two, four or more connections for a single residence," a purpose that "cannot be squared with the language and the goals of Section 254."[44] As AT&T observes: "if universal access to the PSTN is the goal, that goal is fully served by supporting one connection at each residence and business," *not* multiple connections.[45] And, limiting support to a single line ensures that high cost support will be sufficient while minimizing

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42 *See* SBC Comments at 12-16; NASUCA Comments at 4-7; AT&T Comments at 4.

43 NASUCA Comments at 5-6

44 SBC Comments at 14.

45 AT&T Comments at 10.

the burden on contributors, consistent with Section 254(e) and the Fifth Circuit's prohibition on excessive USF support.[46] Second, providing support to multiple connections gives all carriers, including wireless carriers, a strong incentive to obtain the customer's designation as the primary or first line carrier. As NASUCA correctly notes, today "[m]ost consumers are not choosing wireless service as a substitute for existing landline service, but as a complementary additional service."[47] AT&T concurs, citing statistics showing that only three to five percent of customers have "cut the cord" and obtain service solely from a wireless carrier.[48] Supporting only the first or primary line – as designated by the customer – would encourage wireless carriers and all other ETCs to improve service quality and pricing packages such that the customer will consider the carrier to offer a true substitute for the ILEC's primary line service, and not just a complement. In contrast, supporting all lines allows wireless carriers to design and sell their product as a less robust second line substitute.

Moreover, as the comments establish, funding for these additional connections, standing alone, places unnecessary stress on USF.[49] The strain will only grow over time. As discussed herein, Nextel recently filed petitions for ETC designation in New York and Pennsylvania with the FCC,[50] and Alltel filed petitions for ETC designation with state

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46 *See* AT&T Comments at 9.

47 NASUCA Comments at 5.

48 *See* AT&T Comments at 6.

49 *See* CenturyTel Comments at 14-15; OPASTCO Comments at 10-11; NTCA Comments at 10.

50 *See Federal-State Joint Board on Universal Service,* Petition for Designation As An Eligible Telecommunications Carrier in the State of New York, CC Docket 96-45 (filed April 3, 2003); *Federal-State Joint Board on Universal Service,* Petition for Designation As An Eligible Telecommunications Carrier in the State of Pennsylvania, CC Docket 96-45 (filed April 3, 2003).

commissions in Alabama, Michigan and Virginia.[51] As more and more wireless carriers seek ETC designations, their competitors will be forced to follow, either to avoid being placed at a competitive disadvantage or to respond to pressure from Wall Street to maximize revenues.[52] Commercial experience has proven this to be the case: eight months after the Wisconsin Public Service Commission designated its first wireless ETC, six more wireless carriers have pending applications for ETC designation.[53] The only way to end what one commenter termed the ETC "gold rush" is to limit high cost support to a single line.

If the Joint Board and the Commission fail to limit support to a single line, however, it will become even more critical that the Commission limit high cost support to those rural, insular and high cost areas that actually need subsidies to maintain affordable and reasonably comparable rates, consistent with GCI Principle No.1 and with the discussion in Section I.A. Otherwise, the upward spiral in USF will grow unabated because: (1) ETCs will receive high cost support for every line rather than the primary line connecting a residence or business to the PSTN; (2) lines that do not require any high cost support will be subsidized; and (3) lines that require only minimal high cost support will be subsidized to a greater extent than necessary to ensure reasonably comparable and affordable rates. None of these policies advances the universal service objectives of the Act. To the contrary, they threaten the integrity of the entire system by placing unnecessary demands on USF.

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51 *See Alltel Applications for Wireless ETC Status Raises Red Flags Among Rural Wirelines Carriers,* TR DAILY, Apr. 25, 2003.

52 *See* AT&T Comments at 8.

53 *See* CenturyTel Comments at 3.

The Joint Board and the Commission should not be dissuaded from limiting high cost support to a single line based on administrative complexity. If the Joint Board and the Commission adopt a rule limiting high cost support to a single residential or business connection, the Commission could then use an industry stakeholder process to resolve the details of implementation, provided that such a process could be moved quickly. However, a three-year process, such as the first Rural Task Force, would be too slow to address growing ETC demands on the Fund.

III. THE RECORD DEMONSTRATES COMPETITION IS IN THE PUBLIC INTEREST, EVEN IN RURAL AREAS

A. Competition, Not Monopoly, Will Assure that Consumers Receive the Most Innovative Services at the Lowest Total Cost.

Throughout their comments, the rural ILECs plead for the Joint Board to protect them from competitive entry by CETCs on the basis of their assertion that rural, insular and high cost areas cannot support multiple ETCs. The rural ILECs describe a "parade of horribles" that includes retail rate increases, declining network investment, bankruptcy, and at the end – the death of universal service.[54] OPASTCO, among others, asserts that all carriers' costs will increase based on decreased network efficiency that results when multiple carriers serve sparsely populated areas.[55] OPASTCO, NTCA, and their rural ILEC members, however, provide no economic analysis, or even cost data, to illustrate how the certification of multiple ETCs has decreased the efficiency and increased the cost of providing universal service to consumers in rural, insular and high cost areas.

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[54] *See, e.g.,* OPASTCO Comments at 3, 8, 49; ACS-F Comments at 7, 17; Alaska Telephone Association Comments at 7-8; NTCA Comments at 8.

[55] *See, e.g.,* OPASTCO Comments at 41; ACS-F Comments at 22; NTCA Comments at 22.

Of course, it is theoretically possible that dividing the pool of customers in a rural service area between two ETCs could increase the short-run average cost of serving each customer if there are economies of scale in the provision of universal service. However, a myopic focus on the scale diseconomies that additional ETCs may (or may not) introduce ignores the more dynamic benefits of competition. Competition will drive all competitors, both CETCs and ILECs, to seek out efficiencies and to bring new innovations quickly to market. In order for competition to have the net effect of increasing costs per customer, not only must one assume that there are, in fact, scale economies throughout the relevant range, but also that the ILEC already is providing service in the most efficient manner, and that it will continue to innovate on its own, such that there are no offsetting competitive benefits. There is no support in the record for any of these assumptions, which must be accepted to give credence to the argument that competition is harmful, and the ILECs provide no evidence to the contrary.[56]

In fact, as GCI described in its initial comments, the vast majority of rural ILECs are subject to rate-of-return regulation, a regulatory system that provides little, if any, incentive for ILECs to increase efficiency in order to reduce costs, and by extension, limit reliance on USF.[57] GCI agrees with Western Wireless that "rate of return regulation, which guarantees profits to the incumbent but not to competitive entrants, is a major impediment to competition and creates pernicious incentives for inefficient production."[58]

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[56] *See* GCI Comments at 16-21; Rural Cellular Association Comments at 6; Western Wireless Comments at 3.

[57] *See* GCI Comments at 16-21.

[58] Western Wireless Comments at 3.

Further, in the absence of competitive pressure, ILECs have much more limited incentives to deploy innovative services offerings, such as broadband access. GCI previously explained how it has deployed advanced telecommunications services – without high cost support or a guarantee on its investment – throughout Alaska.[59] Competition, not protection from dynamic market forces, has been and will continue to be the real catalyst for both efficient service delivery and broadband deployment in rural America.

It is these dynamic benefits of competition that ILECs deliberately ignore when they argue that competition is "not necessary for the protection of the public interest in ensuring that those rural, insular, and high-cost areas have access to telecommunications… services" that are reasonably comparable to those offered in urban areas, at rates comparable to urban rates.[60] Congress, however, was not so myopic. It was "competition and new technologies," not continued ILEC monopolies, that the Senate Commerce Committee foresaw would "greatly reduce the actual cost of universal service over time."[61] Congress clearly wanted to achieve universal service not through a blank check to rural ILECs, but at the lowest possible cost to society, as determined by the market. For these reasons, the ILECs are simply wrong when they argue "[designating] multiple carriers as CETCs… for the sole purpose of promoting competitive entry… by itself is not sufficient to justify providing federal high-cost support to all those carriers, under the public interest standard…."[62] Competitive entry

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59 *See* GCI Comments at 12.

60 USTA Comments at 4.

61 S. Rep. No. 104-23, at 26 (1995).

62 CenturyTel Comments at 18; *see also* ACS-F Comments at 18; BellSouth Comments at 5.

has demonstrable positive public interest benefits that cannot be achieved through regulation of monopolies.

The ILECs also appear to present as an article of faith that regulators can determine better than the market when additional competition will be in the public interest. However, they do not explain why regulators can be presumed to be omniscient, and why the teachings of economic luminaries such as Fredrich Hayek are inapplicable in these markets.[63] The "cost/benefit" analysis of multiple ETC entry advanced by rural ILECs is irrevocably skewed.[64] The rural ILEC will always exaggerate the costs. Thus, regulators cannot possibly have all the information necessary to fully anticipate competitive benefits, especially since the regulator cannot predict marketplace innovation or fully evaluate the extent to which the rural ILEC is operating inefficiently. And, if the regulator prevents entry, there is no way to verify whether the regulator's decision was correct.[65] Experience has, in fact, shown that regulators have unwisely stifled innovation and entry: regulators artificially foreclosed competition in rural service areas when they granted the rural ILECs a government-protected monopoly more than 80 years ago, demonstrating that regulators are notoriously bad at deciding how much competition is enough, and which competitors are the "best" competitors.[66]

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63 *See* GCI Comments at 22-24.

64 *See* OPASTCO Comments at 43; Alaska Telephone Association Comments at 8.

65 *See* GCI Comments at 24.

66 *See id.* at 25-26; *see also* J. Hausman, "Mobile Telephone," *reprinted in* M.E. Cave et. al. (ed.) *Handbook of Telecommunications Economics, Volume I* at 589-591 (estimating that FCC indecision about whether to make AT&T the monopoly cellular provider in each Metropolitan Statistical Area delayed the introduction of cellular telephone technology in the United States for 10 years, resulting in a consumer welfare loss of approximately $33.5 billion in 1994 dollars).

Finally, it is wholly inappropriate to use the ETC designation process – which is a blunt instrument that can stop all entry in rural areas – as a means to avoid subsidizing inefficient, uneconomic entry into rural telephone company service areas by CETCs. As GCI explained in its initial comments, to the extent the current mechanisms subsidize inefficient entry, that flaw stems directly from the upward spiral of USF created by guaranteeing ILEC revenues through high cost support.[67] The appropriate course is to reform the existing system by ending the ILEC revenue guarantees. This reform, by itself, will ensure that high cost support will not motivate uneconomic entry.

B. The Record Demonstrates that Competition Has Benefited Consumers.

In its comments, GCI described the significant consumer welfare gains that have been generated by GCI's designation as an ETC and its subsequent entry into the local market in Alaska. Since 1997, when GCI entered the competitive local exchange business in Anchorage, consumers in Anchorage alone have saved in excess of $19 million in local rates. In November 2001, when ACS persuaded the RCA to grant it both a retail rate and a UNE price increase in Anchorage, GCI held the line on its rates and gave consumers an alternative to the incumbent's business-as-usual approach. Consumers, in turn, have voted with their pocketbooks, showing overwhelming support for competition: GCI now serves more than 40 percent of Anchorage residential and business customers combined, as well as more than 20 percent of lines in Fairbanks and Juneau. And, Alaska consumers also benefit from non-price benefits generated by GCI's entry, such as improved service quality and innovative new service packages. In short,

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[67] *See id.* at 41-43.

competition in Alaska forces all carriers – both the incumbent and new entrants – to be more responsive to their customers' needs.

The record in this docket is replete with similar success stories from across the Nation. Western Wireless, like GCI, describes how it provides consumers in many rural communities with a broader service package at a lower rate than the ILEC.[68] Telephone penetration rates have increased from approximately 25 percent to 75 percent since Western Wireless began to provide service to the residents of the Oglala Sioux Tribe on the Pine Ridge reservation.[69] Smith Bagley's provision of wireless service on Native American lands in Arizona and New Mexico is adding new customers to the network: since Smith Bagley rolled out its wireless local service offering in June 2001, 28,000 subscribers have signed up, 76 percent of whom did not have prior telephone service.[70]

Competition in rural telephone company services areas, enabled by high cost support, provides numerous other benefits to consumers. Competition promotes economic development by driving the deployment of advanced telecommunications infrastructure in rural areas while keeping costs at a competitive level.[71] The availability of innovative, high-quality alternatives to the ILECs' traditional service offerings is important to economic development because, as described by several commenters, businesses in rural areas depend on such service offerings in order to compete with their urban counterparts.[72] Further, competitively neutral high cost support allows all ETCs to fill in gaps in their networks to provide greater reliability and ubiquity to emergency

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68 *See* Western Wireless Comments at Attachment F.

69 *See id.* at 13.

70 *See* Smith Bagley Comments at 4.

71 *See* Western Wireless Comments at 14.

72 *See* Rural Cellular Association Comments at 18; Western Wireless Comments at Attachment F.

services, such as 911 and E-911, while still harnessing the market to ensure that such infrastructure investments are made efficiently.[73]

These substantial consumer benefits would not be available if the Joint Board and the Commission had not developed universal service support policies based on the concepts of competitive neutrality and portability. Just because one provider – the ILEC – currently offers universal service does not mean that consumers would not benefit from the presence of other providers that can deliver universal service better, faster and cheaper. As the Washington Utilities and Transportation Commission correctly notes, the public interest focuses "on customers, not on companies."[74] Customers should not be foreclosed from the benefits of "increased attention to customer service, downward pressure on prices, and development of new products and services" based on a misguided attempt to protect a single competitor.[75]

IV. THE ACT DOES NOT PERMIT STATES TO IGNORE COMPETITIVE NEUTRALITY OR TO DISCRIMINATE IN ETC DESIGNATION DECISIONS

Section 214(e)(2) of the Act clearly gives state commissions a role in determining whether competitive entry in a rural telephone company's service area would be in the public interest. However, under the existing case law, Section 214(e)(2)'s public interest analysis must take into account Section 253(a) and (b)'s requirements that states act in a competitively neutral and nondiscriminatory manner, even when taking actions to preserve universal service.[76] GCI thus agrees with Western Wireless that the Joint Board

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73 *See* Rural Cellular Association Comments at 17.

74 Washington Utilities and Transportation Commission Comments at 21.

75 *Id.*

76 *See* GCI Comments at 14-16. Section 253(b) also requires states to act in a manner consistent with Section 254 when taking actions to preserve universal service.

should reject rural ILEC proposals to impose onerous minimum "principles" or "guidelines" on state commission and FCC review of ETC designations under Sections 214(e)(2) and (e)(6), respectively,[77] especially when those "guidelines" or "principles" are not competitively neutral and nondiscriminatory. Given that the ILECs have not been able to show how the public interest has been harmed by additional ETC designations, as discussed in the prior section, they have not demonstrated any need to impose such guidelines.

The rural ILECs' various "principles" and "guidelines" are nothing more than a backdoor attempt to shift the public interest analysis away from promoting the interests of consumers toward protecting the interests of rural ILECs. To accomplish this objective, the ILECs stretch Section 214(e)(2)'s public interest test into a presumption that competition is not viable in rural telephone company service areas.[78] There is no support for this interpretation in the statute itself or in the Commission's implementing orders. As the set forth in the Conference Committee Report to the 1996 Act, its goal was to establish "a pro-competitive, de-regulatory national policy framework designed to accelerate rapidly private sector deployment of advanced telecommunications and information technologies and services to all Americans *by opening all telecommunications markets to competition*…."[79] The federal courts have also held that a competitive universal service program is *required* by the Act:

> Alongside the universal service mandate is the directive that local telephone markets be opened to competition. The FCC must see to it that

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77 *See* Western Wireless Comments at 13.

78 *See, e.g.,* OPASTCO Comments at 40; Alaska Telephone Association Comments at 8; CenturyTel Comments at 8; ACS-F Comments at 17-18; USTA Comments at 10.

79 H.R. Conf. Rep. No. 104-458 at 1 (1996)(emphasis added).

> *both* universal service and local competition are realized; one cannot be sacrificed in favor of the other.[80]

The various public interest "principles" and "guidelines" proposed by the rural ILECs would require the government to substitute its judgment for the market. To date, the Commission properly has been leery of rural ILEC assertions that a market is "too small" to support more than one entrant without robust empirical support to demonstrate the potential harm.[81] As GCI's attempts to enter Fairbanks and Juneau demonstrate clearly, rural ILECs are quick to claim that a market is "too small" or a "natural monopoly," but they are short on the facts.[82] Indeed, many of the rural ILECs' "principles" – for example, high cost support "should not be used to incent uneconomic competition" and "the public interest is served only when the benefits from supporting multiple carriers exceed the costs of supporting multiple networks" – assume that regulators can readily identify the "correct" level of competition and the "best" competitors.[83] The Alaska Telephone Association, for example, argues that, "[d]esignating a new ETC may increase beneficial competition, it may not; but it is a

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80 *Alenco,* 201 F.3d at 615.

81 The Commission has "reject[ed] the general argument that rural areas . . . are not capable of sustaining competition for universal service support." *Federal-State Joint Board on Universal Service; Western Wireless Corporation Petition for Designation as an Eligible Telecommunications Carrier for the Pine Ridge Reservation in South Dakota*, Memorandum Opinion and Order, 16 FCC Rcd. 18133, 18138-9 (2001) ("*Western Wireless Pine Ridge Order"*). The Commission elaborated, "Although we recognize that some rural areas may in fact be incapable of sustaining more than one ETC, no evidence has been presented to demonstrate that this is the case on the Pine Ridge Reservation. . . . Moreover, the federal universal service support mechanisms support all lines served by ETCs in high-cost areas. Therefore, to the extent that Western Wireless provides new lines to currently unserved customers or second lines to existing wireline subscribers, it will have no impact on the amount of universal service support available to the incumbent rural telephone company for those lines that it continues to serve." *Id.*

82 *See* GCI Comments at 8.

83 *See* OPASTCO Comments at 43; NASUCA Comments at 9.

factor that cannot be dismissed by presumption."[84] As GCI has already explained in its initial comments and in Section II.A., *supra*, regulators do not have all the information required to determine whether a particular form of competition or a particular competitor is "beneficial."[85] Yet competition by its very nature is beneficial, even if it harms certain competitors. When regulators try to substitute their judgment for that of the market, the public interest will be harmed through the introduction of inefficiency, entry barriers and skewed investment incentives.[86]

Moreover, the Act did not leave unbounded state commission discretion in applying the public interest test under Section 214(e)(2), as the rural ILECs would suggest. Instead, the Commission has properly concluded that Section 253 limits state commissions' exercise of their statutory responsibility to determine whether designation of an additional ETC in an area served by a rural telephone company is in the public interest. Rejecting rural ILEC claims that Section 214(e)(2) grants state commissions unfettered power to condition, or even to deny, ETC designation for any reason, the Commission concluded:

> [A]lthough Congress granted to state commissions, under section 214(e)(2), the primary authority to make ETC designations, we do not agree that this authority is without any limitation. While state commissions clearly have the authority to deny requests for ETC designation without running afoul of section 253, the denials must be based on the application of competitively neutral criteria that are not so onerous as to effectively preclude a prospective entrant from providing service. We believe that this is consistent with sections 214(e), 253, and

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84 Alaska Telephone Association Comments at 6; *see also* OPASTCO Comments at 43 (arguing that high cost support should not be used to incent "uneconomic" competition in areas served by rural telephone companies.)

85 *See* GCI Comments at 22-23.

86 *See id.*

254, as well as the decision of the United States Court of Appeals for the Fifth Circuit in *Texas Office of Public Utility Counsel v. FCC*.[87]

State commissions must therefore exercise their discretionary authority to designate additional ETCs in areas served by rural telephone companies on a "competitively neutral basis and consistent with Section 254."[88] Importantly, whether a state commission's decision is competitively neutral will be judged by its effect.[89] This standard of review makes many facially neutral requirements (*e.g.*, ILEC service quality standards, reporting requirements and customer billing requirements, as proposed by OPASTCO) violations of Section 253, given the significant (and unnecessary) burdens these obligations will place on the CETC.[90]

Contrary to the assertions of some commenting parties, Section 253(f)[91] does not provide a general exemption from the requirements of Sections 253(a) and (b) in rural telephone company service areas.[92] Instead, Section 253(f) only applies to the requirements of Section 214(e)(1), notably an ETC's obligations to: (1) provide universal service throughout a service area and (2) advertise the availability of its universal service offering. Accordingly, many of the rural ILECs' so-called public interest "principles" and "guidelines" cannot be saved by Section 253(f)'s rural exemption.

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87 *Federal-State Joint Board on Universal Service; Western Wireless Corporation Petition for Preemption of an Order of the South Dakota Public Utilities Commission*, Declaratory Ruling, 15 FCC Rcd 15168, 15175 (¶ 18) (2000) ("*South Dakota Preemption Order"*) (citations omitted).

88 47 U.S.C. § 253(b).

89 *See South Dakota Preemption Order,* 15 FCC Rcd at 15177 (¶ 22), *citing Petition of the State of Minnesota for a Declaratory Ruling Regarding the Effect of Section 253 on an Agreement to Install Fiber Optic Wholesale Transport Capacity in State Freeway Rights-of-Way,* Memorandum Opinion and Order, 14 FCC Rcd 21697, 21724 (¶ 51) (1999).

90 *See* OPASTCO Comments at 47; *see also* CenturyTel Comments at 21-23.

91 47 U.S.C. § 253(f).

92 *See* CenturyTel Comments at 17.

Thus, consistent with Section 253 and with Congress' vision that competition and universal service would be complementary policies, the public interest test in Section 214(e)(2) should be applied narrowly. As GCI pointed out in its initial comments, excluding competition on the assumption that it is not sustainable has an asymmetric bias. If, for example, the state commission or the FCC is wrong in its determination that entry and competition would not be in the public interest, the market will never have the opportunity to prove that the regulator was incorrect. On the other hand, if the regulator permits entry into a market that cannot sustain two ETCs, eventually one will exit (at least as an ETC).

ILEC proposals to require a CETC to be "ready" to meet Carrier of Last Resort ("COLR") requirements, or similar obligations,[93] would particularly create a barrier to entry in violation of Sections 253(a) and (b) by requiring extensive construction of network facilities prior to ETC designation. Indeed, such proposals turn the process envisioned by Section 214(e) on its head by excluding the possibility, clearly contemplated by the Act, that two ETCs might provide service in the same territory without constructing two complete parallel networks that each reach every home and business in that service territory.[94]

In Section 214(e), Congress took care to specify when an ETC would be required to build its own facilities, and when it would not, to protect universal service in the event that an ETC chose to exit the market. Section 214(e)(1)(A), for example, requires all ETCs to provide universal service using their own facilities, or facilities in combination

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93 *See id.* at 21-22; OPASTCO Comments at 46-47; USTA Comments at 14.

94 47 U.S.C. § 214(e).

with resale.[95] It is clear from the plain terms of Section 214(e)(1)(A) both that an ETC cannot provide service solely through resale, and that an ETC is not required to serve its entire service territory over its own facilities. Section 214(e)(4) further specifies that in areas served by multiple ETCs, if one carrier seeks to relinquish its ETC status, the other ETCs in the market must "ensure that all customers served by the relinquishing carrier will continue to be served."[96] The remaining carrier must "purchase or construct[] . . . adequate facilities" to meet its ETC responsibilities, and to complete that purchase or construction within one year.[97]

Thus, Congress made it plain that an ETC in a territory served by multiple ETCs is not required to purchase or construct facilities to serve every customer within its service territory until one year after the other ETC seeks to relinquish its ETC designation. The Commission therefore could not lawfully require all ETCs to be ready, as a precondition to ETC designation, to act as COLRs for all potential subscribers within their service territory prior to the expiration of the one year period prescribed in Section 214(e)(4), despite what seem to be ILEC proposals to the contrary.[98] On the other hand, if the ILECs simply believe that, "CETCs should be prepared to step in as the carrier of last resort"[99] one year after an ILEC's petition for relinquishment is granted, the ILECs' suggestion is superfluous. Section 214(e)(4) already requires the CETC to be ready to take steps to construct or purchase the necessary facilities in the event the ILEC relinquishes its ETC status. Every new entrant that seeks ETC status statutorily accepts

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95 47 U.S.C. § 214(e)(1)(A).

96 47 U.S.C. § 214(e)(4).

97 *Id.*

98 *See* CenturyTel Comments at 21-22; OPASTCO Comments at 47; USTA Comments at 14.

99 CenturyTel Comments at 21.

the possibility that it might be asked to serve as the COLR at some future date – but not immediately.

GCI does believe that as CETCs gain market share, it makes sense for them to work out arrangements with the ILEC and any other ETC to share the responsibility of extending facilities to consumers who request universal service but whom no carrier wishes to serve voluntarily. GCI has made such a proposal to the RCA.[100] Under GCI's approach, the CETC would share COLR responsibilities with the ILEC where it provides service to at least 35 percent of lines in a study area through its own facilities or through UNEs.[101]

Unlike the ILEC proposals discussed above, which erect a significant barrier to entry by forcing a CETC to duplicate the ILEC's facilities, GCI's approach is competitively neutral and does not skew investment incentives. To the contrary, it permits the ILEC and the CETC to invest in new facilities when it is economic to do so, and rely on UNEs when it is not. Just as importantly, the shared COLR requirement is only triggered once the CETC earns substantial market share, not as a condition of ETC designation. At that point, the CETC should have the knowledge, resources and network infrastructure needed to undertake such an important obligation, unlike a new entrant. GCI's proposal is thus competitively neutral in effect.

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[100] GCI's proposal is summarized in Attachment A, "GCI Proposal to the Regulatory Commission of Alaska for Shared COLR and Pricing Flexibility In Competitive Local Markets."

[101] Comments of GCI, *Whether Interexchange Carriers Operating In the Anchorage Market Should be Allowed to Sell Interexchange and Local Services in a Bundle; Consideration of Revision to the Regulations Governing the Competitive Local Exchange Market in Alaska; Petition by GCI Communication Corp., d/b/a/ General Communication, Inc., and d/b/a/ GCI to Amend 3 AAC 53.290(g)*, Dockets No. R-02-12, R-02-6, R-02-7 (filed Jan. 31, 2003). GCI has proposed that when the CETC contributes capital to an ILEC network extension under shared COLR responsibilities, the CETC should receive appropriate discounts or credits on the price of unbundled elements that were financed, in whole or in part, by CETC capital.

V. THE RECORD DEMONSTRATES THAT A PER LINE FREEZE OF HIGH COST SUPPORT UPON CETC ENTRY IS NECESSARY TO ELIMINATE COMPETITIVE BIAS AND TO PREVENT UNNECESSARY FUND GROWTH

A. Diverse Parties Support Implementation of the RTF Recommendation for a Per Line Support Freeze for All ETCs Upon CETC Entry.

In its comments, GCI urged the Joint Board to restore economic sanity to USF by eliminating features of high cost support mechanisms that provide rural ILECs with revenue guarantees.[102] The Commission cannot afford to ensure rural ILECs' profitability when faced with skyrocketing USF and the obligation to foster competitive markets.[103] In fact, growth in USF from ILEC revenue guarantees illustrate that "the risk to the [universal service] fund stems not from competition, but from a desire to *insulate rural ILECs from the effects of competition.*"[104]

Specifically, GCI recommended that the Joint Board endorse the Rural Task Force's proposal to freeze per line HCLS upon competitive entry into a rural study area.[105] Without such a freeze, funding grows exponentially based on two significant flaws in the manner in which the high cost mechanisms are calculated. First, the rural ILEC's effective support per line – which is based on the ILEC's total, embedded costs – automatically increases as its access lines decrease.[106] This violates GCI Principle No. 1, because the ILEC receives excessive, not just adequate, high cost support. Second, the ILEC always recovers the cost of its entire network, so even after the ILEC loses a

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102 *See* GCI Comments at 31-45.

103 *See id.*

104 Dobson Comments at 11.

105 *See* GCI Comments at 41.

106 *See id.* at 40.

customer to a CETC, the ILEC still receives high cost support for the facilities once used to serve that customer. This violates Principle No. 4 (no double payments) and Principle No. 2 (deliver support to the service provider), because the ILEC receives high cost support even when it is not providing universal service to the customer. GCI therefore agrees with Dobson that, "[t]he current system clearly needs to be changed because it flips competition on its head, creating a perverse incentive whereby ILECs receive more money when they fail competitively."[107]

Moreover, such a system distorts the correct price signals that would occur in markets without high cost support, in violation of GCI Principle No. 5. First, as the ILEC loses customers, it does not lose all the revenue associated with service to those customers. Instead, the ILEC retains all high cost support for the lines that are no longer being used to provide universal service. This contrasts sharply with the results in an unsubsidized market, in which the ILEC would have no such revenue cushion. Second, under the Commission's rules, the CETC's costs are based on the ILEC's costs, [108] so as the ILEC loses market share, the CETC's per line funding also increases without any additional effort or ingenuity on the part of the CETC. Thus, the existing high cost support mechanisms for rural ILECs distort market-based price signals to both ILECs and CETCs. Eliminating ILEC revenue guarantees through a per line support freeze upon CETC entry and distributing all support on a per line basis would restore the proper market-based price signals to *all* ETCs, with the result that "[n]either the ILEC nor the CETC should enjoy greater revenues per line from universal service mechanisms simply

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107 Dobson Comments at 11.

108 *See* 47 C.F.R. § 54.307(a).

because of market entry;" rather, any revenue gains should be earned "through their application of superior skills, knowledge and foresight."[109]

Several commenting parties, from diverse segments of the telecommunications industry, agree with GCI. Sprint argues that, "No legitimate public policy goal is served by rewarding an incumbent carrier that loses customers to the competition by increasing the amount of per line support given to the incumbent."[110] Indeed, "[a] freeze on per line support upon entry makes imminent good common sense."[111] The nation's two largest ILECs – Verizon[112] and SBC[113] – similarly agree that the Joint Board should modify its high cost support rules to ensure that no more than one carrier receives support to serve a single end user, thereby eliminating excessive and duplicative support payments that threaten the integrity of USF. Importantly, several wireless CETCs also support a per line freeze on high cost support.[114] This is notable because under the current system, CETCs actually receive a revenue windfall from the increased per line support that is available as the ILEC loses market share.[115]

AT&T, another advocate of a per line freeze, demonstrates that per line high cost support can be implemented without jeopardizing the affordability and reasonable

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109 AT&T Comments at 22.

110 Sprint Comments at 14.

111 *Id.*

112 *See* Verizon Comments at 4-5.

113 *See* SBC Comments at 12.

114 *See* Western Wireless Comments, Attachment J at 8; Dobson Comments at 11; Nextel Comments at 17.

115 As discussed above, under the Commission's current rules, CETC per line high cost support is calculated based on the ILEC's costs, so when the ILEC's high cost support increases, the CETC's per line support follows.

comparability of retail rates between urban and rural areas.[116] Under AT&T's modified version of the Rural Task Force proposal, high cost support mechanisms for rural ILECs would be capped at the then-existing level of high cost support per ILEC line upon CETC entry.[117] AT&T would allow support to grow thereafter according to the inflation rate.[118]

GCI supports AT&T's proposal because it "eliminates both the upward spiral in support and its attendant market distortions."[119] As GCI described in its comments, this solution also is consistent with sound economic principles. By calculating support for both ILECs and CETCs on a per line basis, and then capping that per line support upon CETC entry, the upward spiral of support could be halted, and carriers would not enjoy undeserved revenue windfalls courtesy of USF, consistent with GCI Principle No. 1 (provide adequate, but not excessive, support). This solution also furthers GCI Principle No. 2 (deliver support to the service provider) and No. 4 (no double payments), because only one carrier – the carrier providing universal service to the consumer – receives high cost support. And, consistent with GCI Principle No. 3, support is provided in equal amounts to the ILEC and the CETC. The net result is that USF will remain intact and the market will push all carriers to deliver universal service at affordable and reasonably comparable rates for the lowest overall cost to society, consistent with GCI Principle No. 5 (let the market work as it would in the absence of subsidies).

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116 *See* AT&T Comments at 23-24.

117 *See id.* at 23.

118 *See id.* Nextel proposes a similar freeze that would be triggered after the ILEC loses a threshold number of lines, to be determined by the Commission. *See* Nextel Comments at 17. Western Wireless supports a freeze, though unlike AT&T, Western Wireless would "allow additional increases in the total amount of funds available in each area based on the rate of increase in teledensity (telephone penetration), as well as inflation and population growth." Western Wireless Comments, Attachment J at 8. GCI supports AT&T's proposal, and reserves judgment on the proposals advanced by Western Wireless and Nextel.

119 AT&T Comments at 24.

B. ILEC Arguments that Per Line Support Violates Sufficiency Turn the Statute on its Head, Attempting to Convert Consumer Protection into Provider Entitlement.

The ILECs reinterpret the universal service goals of the Act, arguing that the purpose of Section 254 was to ensure cost recovery for network infrastructure used to serve rural, insular and high cost areas, rather than to ensure that the rates paid by consumers for universal service are affordable and reasonably comparable.[120] OPASTCO goes so far to argue that, "[h]igh-cost support should never be confused with a program to simply reduce the rates for telecommunication services charged to an individual end-user."[121] In reality, OPASTCO is confused, because its self-serving interpretation of the universal service principles contained in the Act is in direct conflict with the plain language of the statute. Section 254(b)(3) states:

> Access in rural and high cost areas. *Consumers* in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at *rates* that are reasonably comparable to *rates* charged for similar services in urban areas.[122]

Note that Section 254(b)(3) makes no mention of infrastructure deployment, nor the cost recovery for infrastructure deployed by rural ILECs; to the contrary, the universal service principles outlined in Section 254(b)(3) focus on rates and services for *consumers*.

The consumer focus of the Act was affirmed by the Fifth Circuit Court of Appeals in *Alenco*, wherein the court held that the Commission's portability rules did not violate

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120 *See* OPASTCO Comments at 32; ACS-F Comments at 21; Verizon Comments at 4-5.

121 OPASTCO Comments at 32.

122 47 U.S.C. § 254(b)(3) (emphasis added).

Section 254(e)'s command to provide sufficient universal service support. According to the court:

> The Act only promises universal service, and that is a goal that requires sufficient funding of *customers*, not *providers*. So 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 provider as well.[123]

Rural ILECs cannot somehow transform Section 254(e)'s requirement that high cost support be used "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended," into a cost recovery guarantee given the Fifth Circuit's interpretation of the sufficiency requirement in this section of the Act.[124]

VI. EQUAL SUPPORT TO ALL ETCS IS LAWFUL AND THE ONLY COMPETITIVELY NEUTRAL MECHANISM FOR DISTRIBUTING HIGH COST SUPPORT

A. Distributing Equal Per Line Support to All ETCs Serving a Particular Area Is Consistent with Section 254(e)'s Sufficiency Requirement.

Throughout their comments, several ILECs and their representatives argue that paying CETCs per line high cost support based on the ILEC's high cost support (which, in turn, is based on the total embedded costs of the ILEC's network) violates the requirements of Section 254(e) by over-subsidizing CETC services when the CETC is a

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123 *Alenco,* 201 F.3d at 620 (emphasis in original).

124 Moreover, there is no reason to believe that the rural ILECs cannot recover their own costs in the absence of high cost support. As discussed in Section I.A., the Joint Board and the Commission should require state commissions to raise retail rates to a minimum affordable level as a pre-requisite for high cost support. This will permit the rural ILECs to recover their costs from their customers, not USF. In fact, many rural ILECs have this capability today. The majority of telephone cooperatives are not subject to rate regulation. NTCA and the Texas Statewide Telephone Cooperative in particular make no showing that their members could not immediately seek to recover any lost high cost support through rate increases, without jeopardizing the availability of affordable and reasonably comparable rates for universal service.

lower cost provider.[125] As a corollary, some commenting parties argue that excessive support, defined as per line support that is greater than the CETC's own costs, necessarily must be diverted away from the provision, maintenance, and upgrading of facilities used to provide universal service, in violation of the same statutory provision, because the amount of support exceeds that which is necessary to achieve these goals.[126] These parties misconstrue Section 254(e), apply too narrow an interpretation of the "provision, maintenance, and upgrading of facilities" requirement, and incorrectly assume (without evidence) that the CETC will always be a lower cost provider than the ILEC. Moreover, to the extent that a CETC is more efficient than the ILEC, however, the real problem, which these ILECs studiously ignore, is that the ILECs themselves are being over-subsidized, beyond the level that an efficient carrier needs to provide universal service at an affordable and reasonably comparable rate.

ILEC arguments that sufficiency – and therefore excessiveness of support – must be judged on a carrier-by-carrier basis ignore the central teaching of the Fifth Circuit's decision in *Alenco*. As previously discussed, the Fifth Circuit in *Alenco* expressly rejected ILEC arguments that sufficiency must be judged from the perspective of the *carrier*, holding that Section 254(e) requires only that there be sufficient support for "*customers* to receive basic telecommunications services."[127] When sufficiency is judged from the perspective of the customer, and not the perspective of "every local

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[125] *See, e.g.,* ACS-F Comments at 7-10; CenturyTel Comments at 5, 32; OPASTCO Comments at 16-17; SBC Comments at 10; NTCA Comments at 16.

[126] *See* Verizon Comments at 7, 9; ACS-F Comments at 10; NASUCA Comments at 11; OPASTCO Comments at 16.

[127] *Alenco,* 201 F.3d at 620 (emphasis added).

telephone provider as well,"[128] sufficiency has no logical relationship to an individual ILEC's or CETC's costs of service, but can only be judged with respect to the market rates among *competing* providers in the absence of high cost support. Equal support for carriers offering universal service to the same customer in the same market therefore cannot, consistent with Section 254(e)'s *customer* focus, violate the statutory command of sufficiency.

Indeed, under *Alenco*'s customer-focused sufficiency requirement, if high cost support in a particular *market* is excessive (*i.e.*, more support than is necessary to ensure affordable and reasonably comparable rates for consumers) in violation of Section 254(e), the proper remedy, consistent with *Alenco,* is not to reduce the support to only one ETC in the market (for instance, the CETC), but to reduce the support provided to all ETCs in that market. If the Joint Board and the Commission allocate greater support to an ETC with higher costs than to an ETC with lower costs, the customer of the higher cost ETC will receive more support than would be necessary for that customer to have universal service if that customer chose service from the lower cost ETC. Paying differential support to ETCs serving the same customer in the same market therefore not only violates competitive neutrality, but would do exactly what the Fifth Circuit rejected in *Alenco* – confuse the Act's command for universal service to provide "sufficient funding of *customers*" with "sufficient funding of every local telephone provider."[129]

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128 *Id*.

129 *Id.* (emphasis in original).

Several commenting parties – including some ILECs – agree with GCI that basing each ETC's high cost support on that ETC's own costs rather than paying all ETCs the same nominal support eliminates the incentive for all ETCs to operate more efficiently. Paying differential per line high cost support to ETCs serving the same customers in the same market cements the historical inefficiencies that rate-of-return regulation allowed to become embedded in rural ILEC cost structures, and then shields those historical inefficiencies from market discipline as competition develops. As noted by the Rural Cellular Association, "the outcome would be highly undesirable for consumers in the area and society at large: the ILEC would have no incentive to improve efficiency (if this is the cause of the higher cost), a high-cost technology might be perpetuated (if this is the cause of the higher cost), or both."[130] BellSouth agreed, saying, "the current methodology provides an incentive for both the incumbent and competitive ETCs to operate efficiently," adding, "the potential loss of customers would motivate the incumbent to conduct its business in a more efficient manner."[131] And, providing a lower cost CETC with high cost support based on its own costs places the CETC at a competitive disadvantage, since it "ha[s] the effect of punishing a competitor for being efficient – *and rewarding an incumbent for being inefficient."*[132]

Moreover, if sufficiency were really to be determined on a *carrier*, rather than a *customer*, basis, such an interpretation would truly subsidize competitive entry. As

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130 Rural Cellular Association Comments, Wood declaration at 13.

131 BellSouth Comments at 8.

132 Sprint Comments at 11 (emphasis in original); *see also* BellSouth Comments at 8 ("If a competitive ETC is able to serve a customer's line at a much lower cost than the incumbent, that ETC may be able to charge lower rates thereby winning customers away from the ILEC. The potential loss of customers would motivate the incumbent to conduct its business in a more efficient manner.") and Western Wireless Comments at 17 ("Funding… based upon the most efficient means to providing service… would result in funding that is competitively neutral and would encourage innovation and efficiency").

several commenters point out, in the early stages of competition, a CETC's per line costs are likely to be much greater than those of the ILEC, not lower, contrary to ILECs' assumptions.[133] A start-up CETC will not yet have achieved even its baseline operating scale, let alone be able to approach the ILEC's economies of scale and scope. Under the ILECs' proposal to pay CETCs based on CETC costs, USF might actually grow due to the increased per line high cost support amounts provided to CETCs. As one commenting party warned, providing CETCs with high cost support based on their own elevated costs upon entry might create a "gold rush" mentality that places additional stress on USF.[134] Such a policy would also dull the incentives of CETCs to minimize their operating costs.

Further, the ILECs' assumption that CETCs will necessarily have lower total costs of service than the ILEC is unfounded. As GCI described in its initial comments, GCI has loop costs that are roughly similar to the ILEC with which it competes, when the costs of collocation and feeder transport from GCI's switch to the ILEC's collocation site are included.[135] ILEC arguments that CETCs using UNEs have lower costs than the

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[133] *See* Rural Cellular Association Comments at 9; Smith Bagley Comments at 11. Indeed, the willingness of some commenting parties to use a "proxy" rate to determine CETC costs undermines this argument. *See, e.g.,* Texas Statewide Telephone Cooperative Comments at 7 ("For example, a simple surrogate methodology, assuming it is cost justified, could be one-third of the rural ILEC's support as the surrogate cost for the CETC's."). The rural ILECs do not want to make sure that CETC support is accurate – they only want to make sure that it is reduced.

[134] *See* Rural Cellular Association Comments at 25 ("Unfortunately for ILECs, if wireless carriers receive support based on a wireless cost model, the relative youth of wireless networks may lead to a gold-rush mentality as carriers sweep into rural areas on the promise of high-cost funding sustaining bad business decisions."); *see also* Smith Bagley Comments at 11 (arguing that if high cost support is calculated on the CETC's own costs that "it is possible, if not likely, that inefficient investments would be made based on the ability to obtain high-cost support, and not on prudent, customer-driven network development strategy.").

[135] For example, in Fairbanks, GCI pays ACS-F $19.19 per month for a UNE loop. However, the UNE loop represents only a portion of GCI's loop costs. GCI serves its customers using UNE loops from ACS-F in combination with GCI's own fiber feeder and transport facilities. As GCI explained in its Comments, the cost of these additional facilities add no less than $12.82 to GCI's loop costs. *See* GCI Comments at 55. Thus, ACS-F is incorrect when it asserts that, "While GCI complains that its loop costs

ILEC – as measured by a comparison of the UNE loop rate to the ILEC's embedded loop cost – do not consider the CETC's full costs to provide universal service.[136]

It bears reiterating that equal per line high cost support payments for ETCs competing to serve the same customers in the same markets – the only result consistent with the Commission's principle of competitive neutrality – does not mean that all ETCs must receive support based on the ILEC's embedded costs. It is just as consistent with competitive neutrality for no ETC – including the ILEC – to receive support based on the ILEC's embedded costs, as is the case for non-rural ETCs receiving support under the High Cost Model. Again, as *Alenco* directly held, the sufficiency requirement in Section 254(e) does not preclude the Joint Board and the Commission from reducing support below the level that would be calculated based on the ILEC's costs, so long as whatever support is provided is sufficient to ensure that rates for consumers remain affordable and reasonably comparable. If other ETCs can offer universal service with less high cost support than the ILEC, over time all rates in the market can be kept at affordable and reasonably comparable levels with high cost support that falls below the per line level that would be calculated solely on the ILEC's costs. Paying support to any ETC based on ILEC costs, when such costs to do not reflect the most efficient means of production,

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are higher than the UNE rate, GCI has not been able to justify these costs." ACS-F Comments at 10. In fact, GCI has demonstrated that its costs actually exceed ACS-F's average loop cost for 2003, which is $29.50. *See id.* at 5.

136 *See* ACS-F Comments at 5; CenturyTel Comments at 32, 36. NASUCA, unlike ACS-F, would allow a CETC to show that its UNE costs plus its non-UNE costs are sufficient to demonstrate the CETC's need for high cost support. *See* NASUCA Comments at 11. GCI believes this proposal still creates significant administrative burdens for the CETC and eliminates other benefits that result from equal per line high cost support, such as maintaining the price signals that would occur in a properly functioning market without subsidies.

"converts a means of ensuring service availability into a means of ensuring the operation of a given carrier,"[137] which is well beyond the requirements of Section 254(e).

Moreover, the Joint Board must reject assertions that rural ILECs "would no longer have the incentive or ability to continue investing in network infrastructure that provides all consumers in the service area with high-quality, reliable service, as well as access to advanced services" if their high cost support was lowered to reflect the per line costs of the most efficient provider in that service area.[138] Once again, these arguments presume that rural ILECs are already delivering services at optimal efficiency, incorporating the latest cost-effective innovations, notwithstanding the lack of incentives to do so within rate-of-return regulation. Competition from other ETCs will increase the ILECs' investment incentives by forcing the ILECs to provide excellent service to their customers rather than lose them to CETCs. Indeed, rather than generating a "race to the bottom," GCI's experience in Alaska shows that infrastructure investment was spurred by GCI's entry into the local market.[139] Similarly, the development of a competitive market forces all carriers to improve their service quality levels.

Accordingly, the Joint Board should reevaluate the use of the ILEC's embedded costs as the basis for determining any ETC's high cost support, and, at least in markets

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137 Rural Cellular Association Comments, Wood declaration at 13.

138 OPASTCO Comments at 28.

139 ACS-F claims that current universal service policies leave ACS-F no incentive to construct new network infrastructure "[b]ecause CETCs have lower overall costs [so] they can easily under-price the ILECs, which means the ILECs' investment is only benefiting their competitors." *See* ACS-F Comments at 23. This contention suggests that ACS-F believes its costs of constructing new access lines exceed the corresponding estimated costs of an efficient network provider (*i.e.,* UNE rates). Consequently, ACS-F appears to be arguing that it is not an efficient provider, even on a forward-looking basis.

with multiple ETCs, should determine per line support for all ETCs under a most efficient provider standard.[140]

B. ILECs Fail to Demonstrate How Distributing Unequal Support is Competitively Neutral.

ILECs proposing to provide unequal per line high cost support to competing ETCs offering service to the same customers in the same market utterly fail to demonstrate how such a mechanism would be competitively neutral. Competitive neutrality for high cost support should logically be determined by comparing the market dynamics created by the support mechanism with the market dynamics that would be in effect in the absence of support (a test embodied in GCI Principle No. 5). As GCI explained in its comments, in the absence of subsidies, GCI has an incentive to enter a market when it can do so profitably, as measured by the unsubsidized amount of revenue GCI would receive in competition with ACS' unsubsidized prices.[141] The market would dictate GCI's pricing in response to ACS' pricing and would dictate ACS' response to any price reductions implemented by GCI. Providing the same level of high cost support to both ETCs simply tends to reduce the price that customers will have to pay by the amount of the high cost support, as GCI and ACS compete vigorously for customer loyalty.

To the contrary, competitive incentives and market discipline would be greatly skewed if high cost support were provided to only one ETC but not another, or in a greater amount to one ETC than to another. If, for example, ACS were to receive high

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[140] *See* Sprint Comments at 11; *see also* GCI Comments at 65-66 (proposing that the Commission base high cost support on the costs of the most efficient LEC and step-down per line subsidies upon CETC entry).

[141] *See* GCI Comments at 46-47.

cost support, and GCI were to receive no high cost support for providing the same service to the same subscriber, GCI would have no incentive to enter the market unless it could somehow reduce its average cost sufficiently far below ACS' costs so as to at least offset the subsidy provided to ACS. A number of commenting parties concur. According to Sprint, "no competitive carrier (landline or wireless) can be expected to compete with an incumbent when the incumbent receives government subsidies that are not available to competitive firms" because the subsidies "distort the ability of [competitive] entrants to compete on the basis of price."[142] Similarly, the Rural Cellular Association notes that, "if any entrepreneur could make a business out of competing with subsidized ILECs in rural areas without high-cost support, surely after 100 years, it would have happened by now."[143]

Therefore, rural ILECs such as ACS-F, which argue that the provision of the same level of high cost support to ILECs and CETCs "violates the principle of competitive neutrality by giving CETCs the ability to earn super-competitive profits," confuse the concepts of competitive neutrality with profit equalization.[144] Competitively neutral policies, such as the Commission's current rules for high cost support, do not change the relative abilities of firms to compete in the marketplace. For example, if GCI's costs are $1 per unit lower than ACS' costs before a competitively neutral subsidy policy is implemented, then GCI's effective costs remain $1 per unit lower than ACS' costs after the policy is implemented. By contrast, profit equalization policies offset differences between the relative abilities of firms that would otherwise arise in the marketplace. For

142 Sprint Comments at 9.

143 Rural Cellular Association Comments at 4.

144 ACS-F Comments at 2; *see also* Texas Statewide Telephone Cooperative, Inc. at 6.

example, after a profit equalization policy is implemented in the setting described above, both GCI and ACS will have the same effective costs, because ACS will be provided $1 per unit more in subsidy than GCI to offset GCI's cost advantage. Competitively neutral policies benefit consumers by helping to ensure that services are provided by the least cost supplier. In contrast, profit equalization policies harm consumers and competition by subsidizing the operation of high cost suppliers and by limiting the incentives of all suppliers to reduce their operating costs.

For the foregoing reasons, calculating per line high cost support by the same ruler is the only means to replicate the price signals that would occur in a competitive market. Differential per line support for ILECs and CETCs will deprive the market of each carrier's superior skill, knowledge and foresight, because it will rob more efficient carriers of the benefits of their efficiency. Contrary to ACS-F's assertion that, "GCI's retail prices have been wholly dependent on the cost advantage GCI has obtained from these regulatory policies," the truth of the matter is that GCI beats ACS on price because it is a more efficient provider that competes on market prices, not from a position of guaranteed cost recovery, plus a profit.[145] Indeed, it is the prospect of short-run extra-normal profit that induces competitors to innovate and offer new and superior services to customers. Propping up inefficient rural ILECs with high cost support will eliminate this incentive, in violation of GCI Principle No. 5 (let the market work as it would in the absence of subsidies) and GCI Principle No. 1 (provide adequate, but not excessive, support). The inefficient ILEC will receive "extra" high cost support – beyond that which is necessary to provide universal service at affordable and reasonably comparable

[145] ACS-F Comments at 6.

rates – to ensure that its competitor does not exercise its well earned competitive advantage. At bottom, then, providing different levels of support to ETCs is nothing more than a form of regulatory socialism that limits incentives for cost reduction and innovation and substitutes the heavy hand of regulation for the invisible hand of the market.[146]

C. Western Wireless' Proposal for a Voucher System Merits Serious Consideration.

In its comments, Western Wireless suggests that high cost support could be allocated in rural telephone company service areas by giving customers vouchers, which the customer could then present to an ETC to receive a reduced rate for the supported universal services.[147] The ETC, in turn, would seek reimbursement from USAC.[148] Sprint similarly encourages the Joint Board to consider the possible use of a voucher-based high cost support program.[149]

A voucher mechanism would be fully consistent with Section 254(e)'s requirement that support be provided to telecommunications carriers. The voucher itself is not the provision of support, but merely a customer designation of the carrier to which support will be provided. Like reimbursements to telecommunications carriers for discounts provided to schools and libraries, the support would still be paid to the carrier, as Section 254(e) directs.

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146 *See* Sprint Comments at 4 ("…awarding support only to the incumbent carrier would discourage efficiency and technological innovation that is stimulated by competition, essentially guaranteeing indefinitely the need for continued large USF subsidies, rather than the economic provision of service").

147 *See* Western Wireless Comments, Attachment J at 7-8.

148 *See id.*

149 *See* Sprint Comments at 14-15.

GCI believes that Western Wireless' proposal could avoid many of the regulatory problems described herein. First, telephone vouchers for consumers will allow individuals to choose the type of service and the level of service quality they prefer, thereby limiting the need for regulatory micromanagement of the industry.[150] Second, telephone vouchers would permit support to be focused to a single line per residence or business, by actually or virtually providing the customer with a mechanism for designating its choice of first line provider. Third, when combined with a more clear definition of rate affordability and reasonable comparability, telephone vouchers would facilitate better targeting of high cost support to those areas – such as the Alaska Bush – for which federal high cost support is truly necessary to ensure that basic telecommunications services are provided to consumers at affordable and reasonably comparable rates.[151] Finally, a voucher program would help complete the transition from an ILEC-oriented high cost support system to one that, consistent with sound economics underlying GCI's five principles, truly embraces competition and universal service as mutually reinforcing policy objectives.

VII. ILECS FAIL TO DEMONSTRATE THAT UNE-BASED ETCS SHOULD BE TREATED DIFFERENTLY THAN OTHER ETCS

A. No ILEC that Advocates Basing CETC High Cost Support on UNE Prices Explains Why Such Discrimination is Appropriate.

In what is really a subset of the arguments that CETCs should receive high cost support based only on CETC costs of providing universal service, some rural ILECs urge

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150 *See* Sprint Comments at 15 ("Many of the large administrative costs associated with the current system (e.g., cost studies, reporting requirements) would be eliminated [under a voucher-based system], which might allow carriers to reduce the prices they charge customers for their services.").

151 *See* Sprint Comments at 15 ("A voucher system would also eliminate the concern of USF support being used to subsidize service to consumers that can well afford to pay cost-based rates.").

the Joint Board to provide lesser amounts of high cost support, or even eliminate high cost support altogether, for UNE-based CETCs whose loop costs (as defined by the UNE loop rate only) fall below the Commission's high cost loop benchmark.[152] These arguments must be rejected for all the reasons discussed in Section VI, *supra*. In addition, however, ILECs proposing to limit the high cost support of UNE-based ETCs offer no reason to treat UNE-based ETCs differently than ETCs that solely use their own facilities to provide universal service. UNE facilities leased by a CETC meet Section 214(e)(1)(A)'s requirement that an ETC provide service, at least in part, over "its own facilities."[153] UNEs are simply one means for completing last mile connectivity, and consistent with the principal of competitive neutrality, this mode of entry should not be treated differently for the purpose of calculating high cost support. To do so would violate competitive neutrality and sound economics.

As described in Section VI, *supra*, UNE loop rates do not reflect all of the costs a CETC must incur to provide universal service. UNEs are simply one of the CETCs loop costs, and one means for completing the last mile. Thus, measuring the UNE loop rate paid by the CETC against the ILEC's embedded costs will not provide an "apples to apples" comparison, because it understates the CETC's cost to provide universal service.

Indeed, issuing different levels of support for UNEs and "self-installed" facilities will skew carrier investment incentives and create a new source of increased demand on the high cost fund. Reducing high cost support to CETCs that employ UNEs would encourage CETCs to make uneconomic infrastructure investment for which full support

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152 *See* ACS-F Comments at 2; Verizon Comments at 7-8; OPASTCO Comments at 21.

153 *See Universal Service Report & Order,* 12 FCC Rcd at 8862-70 (¶¶ 154-168); *see also* 47 U.S.C. § 214(e)(1).

would be paid. Particularly if support is then paid to CETCs based on the CETC's costs, high cost support would be available to subsidize the construction of CETC facilities – precisely the result that ILECs elsewhere decry (and contrary to one of OPASTCO's "principles").[154]

In reality, the ILECs' attack on UNE-based CETCs has little to do with a desire to protect universal service or prevent "uneconomic" competition.[155] Instead, the ILECs' primary problem appears to be with the level at which UNE prices have been set, or more specifically, the fact that UNE rates are calculated based on forward-looking rather than embedded costs. But this proceeding, which concerns USF, is not the proper forum to address UNE pricing rules. Any proposals to revise the UNE pricing rules (which do not require revision) may only be considered in a separate proceeding applicable to all UNE pricing determinations. If states have misapplied the FCC's UNE rules, ILECs can raise those concerns on appeal to Federal district court. Attempting to use high cost support to reverse-engineer new UNE pricing rules for areas served by rural ILECs is both disingenuous and discriminatory.

It is important to recognize that the difference between a TELRIC-based UNE loop rate and an ILEC's embedded loop cost is a feature of both subsidized and unsubsidized markets. Alaska is no different than the rest of the country in this regard. [156]

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154 *See* OPASTCO Comments at 43.

155 *See* ACS-F Comments at 2.

156 *See* Attachment B, which compares RBOC UNE rates to RBOC embedded loop costs on a state-by state basis. The chart also compares ACS' UNE rates to its embedded loop costs for the Anchorage, Fairbanks and Juneau study areas. UNE rate data came from Billy Jack Gregg, Director Consumer Advocate Division, Public Service Commission of West Virginia, "A Survey of Unbundled Network Element Prices in the United States," published by the National Regulatory Research Institute (January 2003). This report is available at http://www.nrri.ohio-state.edu/index.html. Embedded loop cost data came from October 2002 NECA filings, which are based on 2001 data. This analysis shows that ACS'

In other words, the forward-looking cost of a UNE loop is almost always less than the ILEC's embedded loop cost, even in non-rural markets that do not receive high cost support, because it is based on the costs incurred by the most efficient provider.[157]

Contrary to the assertion of some rural ILECs,[158] the Commission's existing rules fully address any potential for any artificial "windfalls" to CETCs providing supported services using UNEs. Section 54.307 limits a CETC using UNEs to no more high cost support (other than Local Switching Support) than it pays the ILEC for a UNE loop.[159] Similarly, CETCs cannot receive Local Switching Support that exceeds the amount they pay ILECs for unbundled local switching.[160] These rules fully prevent a CETC from receiving high cost support that exceeds the amount it pays to the ILEC in UNE rates.[161] And, by extension, it also ensures that a UNE-based CETC always uses high cost support to defray the costs of providing universal service, which will always exceed the UNE

UNE loop rates are relatively high in Anchorage and Juneau, and typical for Fairbanks, when compared to RBOCs of comparable embedded cost.

157 Further, as GCI explained in its comments, there is no basis on which to assume that rural ILECs are operating efficiently, particularly given their historical status as a monopoly provider subject to rate-of-return regulation. *See* GCI Comments at 16-21. To the contrary, by asserting that its self-proclaimed embedded costs are greater than the costs of an efficient carrier (*i.e.,* UNE rates) ACS-F acknowledges that it is not operating efficiently.

158 *See* ACS-F Comments at 13-14; Alaska Telephone Association Comments at 11.

159 47 C.F.R. 54.307.

160 *See* 47 C.F.R. §54.307(a)(2); *see also Universal Service First Report & Order*, 12 FCC Rcd at 8892 (¶ 287). Any high cost support per line that exceeds the UNE price must be paid to the ILEC. *See id*.

161 GCI therefore believes that it is not necessary to impose additional reporting obligations on CETCs to ensure the proper use of high cost support, in conformance with Section 254(e)'s requirement that support can be used "only for the provision, maintenance and upgrading of facilities and services for which the support is intended." *See, e.g.,* CenturyTel Comments at 36-37 (arguing that "A CLEC that purchases UNE loops at a cost below the national high-cost standard, does not *have* high-cost loops, by definition" so it "must be using high-cost support other than for the purpose for which the high-cost funds were intended."). Under the Commission's rules, as discussed herein, GCI always receives less HCLS for a supported line than the price GCI pays for UNE loop, so there is no "excessive" support and thus no need to further document GCI's use of this support. With regard to switching, GCI has invested in its own switching facilities, so there also is no need for additional documentation concerning how GCI uses Local Switching Support.

price because UNEs are only a part of the cost of providing universal service.[162] Further, as discussed in greater detail below, deaveraging of UNE rates[163] and the ability to disaggregate high cost support[164] give the ILEC ample tools to ensure that a CETC cannot lease UNEs at rates that are averaged study area-wide, but receive disaggregated high cost support. To the extent the Joint Board and the Commission believe further safeguards are necessary, GCI suggests below two reforms that will prevent mismatches between UNE deaveraging and high cost support disaggregation.

B. ILECs that Are No Longer Exempt from Unbundling Requirements Should Be Required to Deaverage UNE Loop Rates According to the Same Zones as High Cost Support.

Section 54.315 of the Commission's rules, as adopted in the *Rural Task Force Order*, gave a rural ILEC three "paths" under which it can disaggregate its HCLS: under "Path One," the ILEC may choose not to disaggregate; under "Path Two," the ILEC can disaggregate based on a plan that has been approved by the appropriate state regulatory authority; and under "Path Three," the ILEC can self-certify a disaggregation plan, although support may not be disaggregated into more than two zones.[165] The three paths give a rural ILEC substantial flexibility to determine the appropriate number of zones

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[162] BellSouth's proposal to limit HCLS to 76 percent of the difference between the UNE price and the statewide average forward-looking costs or the amount of support the ILEC receives, whichever is less, is not appropriate for HCLS, LSS, LTS, and ICLS, all of which are not calculated on the basis of statewide-average forward-looking costs. *See* BellSouth Comments at 10. For rural carriers, § 54.307 fully ensures that a CETC using UNEs does not receive more in universal service support from all mechanism than it pays to the ILEC in UNE rates.

[163] *See* 47 C.F.R. § 51.507(f) (requiring state commissions to deaverage an ILEC's UNE rates into three zones within a state based on underlying cost differences).

[164] *See* 47 C.F.R. § 54.315.

[165] *See Federal-State Joint Board on Universal Service; Multi-Association Group ("MAG") Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers,* 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, 16 FCC Rcd 11244, 11302-11306 (¶¶ 144-55) (*"Rural Task Force Order"*).

within which to disaggregate support. Similarly, the Commission's rules require UNE rates to be deaveraged into at least three zones.

GCI believes that, when an ILEC is disaggregating high cost support because of the entry of a UNE-based CETC, there should be symmetry between the manner in which HCLS is disaggregated and the manner in which UNE loop rates are deaveraged. GCI is *not* advocating that ILECs *always* be required to use UNE zones to disaggregate support. In many areas, the ILEC is disaggregating in the face of entry by non-UNE-based CETCs, such as wireless carriers, and, indeed, may be exempt from unbundling pursuant to Section 251(f) of the Act.[166] In those areas, particularly where an ILEC is still exempt from UNE unbundling requirements, requiring disaggregation according to UNE zone would be unduly restrictive, as there are no UNE zones. GCI therefore urges the Joint Board to recommend that the Commission revise its rules to require a rural ILEC to deaverage UNE rates into the same zones that it has disaggregated its high cost support only in the limited circumstance in which the ILEC loses its rural exemption under Section 251(f) and the UNE-based competitor is a CETC.

GCI believes that matching UNE zones to high cost support disaggregation zones will prevent rural ILECs from choosing to disaggregate high cost support, but not UNEs, in order to raise barriers to entry in higher density (and lower cost) portions of the ILEC's study area.[167] In fact, GCI's proposal to match UNE zones and high cost support disaggregation zones when a UNE-based CETC is competing with the ILEC would have

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[166] 47 U.S.C. § 251(f).

[167] An ILEC might elect such a strategy, for example, to give itself a competitive advantage when competing against a UNE-based CETC for business customers.

precluded exactly the course of action that ACS-F took in Fairbanks – and which backfired on ACS-F.[168]

GCI's proposal also fully addresses ACS-F's complaint that its averaged UNE rates do not reflect the higher costs of service in less dense portions of its study area.[169] Synchronizing UNE zones and high cost support disaggregation zones eliminates any potential for arbitrage due to a mismatch between UNE rate deaveraging and high cost support disaggregation, providing rural ILECs like ACS-F with additional protection against regulatory distortions.

C. The Joint Board and the Commission Should Preclude ILECs from Assigning High Cost Loop Support to Zones with Average Loop Costs below the Support Threshold.

To preclude ILEC gamesmanship (and to save ILECs from themselves), the Joint Board and the Commission should also preclude ILECs from assigning HCLS to disaggregation zones where the ILEC's embedded costs fall below the applicable high cost support threshold. As GCI explained in its comments, ACS-F elected to use Path 3 under the *Rural Task Force Order*, which allows a rural ILEC to self-certify a disaggregation plan that allocates HCLS between two zones.[170] ACS-F did not allocate support to each zone based on the extent to which its embedded costs exceeded a specified level, for example, the Commission's $25 per month HCLS threshold.[171]

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168 *See* GCI Comments at 56. ACS-F's problems in the Fairbanks market have more to do with ACS-F's own regulatory choices than with the universal service rules. ACS-F did not seek deaveraged UNE loop rates in an arbitration with GCI before the RCA in 2000. ACS-F thus had the chance to remedy its own complaint that GCI can purchase UNE loops at prices averaged across the study area, but receive disaggregated high cost support for lines in higher cost Zone 2. While GCI does not know why ACS-F did not seek deaveraged UNE rates in the 2000 arbitration, one possible explanation is that ACS-F sought to keep its UNE loop rates relatively high in low-cost areas, making UNE-based entry less attractive.

169 *See* ACS-F Comments at 16.

170 *See* GCI Comments at 57-58.

171 *Id.* at 58.

Indeed, according to ACS-F's own disaggregation plan, the embedded costs of all density zones comprising its low-cost Zone 1 were below this benchmark. Nonetheless, ACS-F apportioned one-third of its study area support to Zone 1. In other words, ACS-F created a two-to-one ratio between per line high cost support in Zone 2 (high cost) and Zone 1 (low cost).[172] As such, ACS-F's disaggregation plan violates its own suggestion to eliminate high cost support for lines where the ETC's costs fall below the HCLS threshold of $25 per month.

If GCI's proposal had been in effect, ACS-F would have been forced to assign all high cost support to Zone 2, or redrawn its zone boundaries to place some moderate cost areas into Zone 1. When combined with GCI's proposal to require deaveraging of UNE rates along the same zone boundaries as the disaggregation of high cost support, GCI would have paid a lower UNE rate in Zone 1, but received no high cost support, whereas GCI would have paid a higher UNE rate in Zone 2 and received greater high cost support. This is an economically rational result.[173]

VIII. CONCLUSION

The benefits of competition and universal service – the dual goals of the 1996 Act – are finally being made available throughout the Nation. In fact, GCI's Alaska success story demonstrates that these goals are attainable even in rural America, despite ILEC protestations to the contrary. However, seven years after the passage of the 1996 Act, the

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[172] *Id.* Indeed, ACS-F's disaggregation methodology assigned far less than $25 in embedded cost per loop (the ILEC support threshold for HCLS) to all Zone 1 loops. By contrast, all Zone 2 loops were assigned embedded costs greater than $27 per loop. *See* ACS of Fairbanks, Inc. – Disaggregation and Targeting Plan, at 4 (attached as Exhibit B to GCI's comments).

[173] Of course, a well designed voucher policy for universal service, such as the system discussed in Section V.C., would vastly reduce the number of disputes between carriers about disaggregation of high costs support and deaveraging of UNE rates. It would also eliminate the administrative burdens placed on state and federal regulators, who are forced to resolve these disputes.

Commission's universal service policies for rural, insular and high cost areas are still a hodgepodge of mechanisms lacking a coherent, unifying framework. Indeed, it is the Commission's failure to reform its universal service policies to meet the needs of a dynamic, competitive telecommunications marketplace – not competition itself – that has jeopardized the very integrity of universal service.

The prescription for securing universal service into the future is not to sacrifice one goal – competition – to save universal service. The Joint Board should not, and cannot, turn back the clock and maintain, or even extend, ILEC protectionist measures such as revenue guarantees in an effort to maintain the status quo. Instead, the Commission, with recommendations from the Joint Board, must go "back to basics" and define its fundamental universal service objectives in conformance with sound economic theory and the goal of fostering competitive markets. As discussed herein, this will require the Commission to make difficult policy choices about the definition of reasonably comparable and affordable rates, the scope of high cost support (*i.e.,* a single line versus multiple lines), and the mechanisms for distributing support in a competitively neutral manner.

GCI proposed the five principles, grounded in the Act and sound economics, to guide these much needed reforms:

> **Principle No. 1: Provide adequate, but not excessive, support.** High cost support must be adequate to ensure that rates are affordable and reasonably comparable, but support should be the lowest amount necessary to achieve these objectives.
>
> **Principle No. 2: Deliver support to the service provider.** High cost support should be paid to the service provider that pays the cost of facilities employed to deliver the service to the end user customer. High cost support should not be paid to all potential providers of service, regardless of whether they are actually providing the supported service to the end user customer.

Principle No. 3: Ensure equal opportunity for support. The support paid to the appropriate provider should be the same for all competitors, regardless of the facilities they employ, the manner in which they procure facilities, or the metric used to determine the per line support level.

Principle No. 4: No double payments. If one carrier gets high cost support for providing a line to a household, another provider should not also get support for providing (or being able to provide) a line to the same household.

Principle No. 5: Let the market work as it would in the absence of subsidies. Other than permitting more consumers to purchase service, high cost support should not alter the competitive signals that the market would send to ILECs and CETCs in the absence of support payments.

Basing its recommendation on these principles will help the Joint Board and the Commission to ensure that universal service policies will neither preclude competitive entry where it is economically efficient, nor support entry where it is not. These policies will also help better target high cost support to areas and services that truly need it. And, competition itself, where the market determines it will be beneficial, will provide a self-correcting engine to ensure that universal service is delivered to all Americans at the lowest overall cost – just as the 1996 Act intended.

Respectfully submitted,

By: _____/s/_____

Tina Pidgeon
Vice President-
Federal Regulatory Affairs
GENERAL COMMUNICATION, INC.
1500 K Street, N.W., Suite 925
Washington, D.C. 20005

James R. Jackson
GENERAL COMMUNICATION, INC.
2550 Denali Street
Suite 1000
Anchorage, AK 99503

John T. Nakahata
Maureen K. Flood*
HARRIS WILTSHIRE & GRANNIS LLP
1200 Eighteenth Street, N.W.
Washington, D.C. 20036
(202) 730-1300

Counsel for General Communication, Inc.

*Telecom Policy Analyst

June 3, 2003

ATTACHMENT A

GCI PROPOSAL TO THE REGULATORY COMMISSION OF ALASKA FOR SHARED COLR AND PRICING FLEXIBILITY IN COMPETITIVE LOCAL MARKETS

GCI currently serves over 40 percent of the local market in Anchorage, Alaska. ACS, the incumbent local exchange carrier (ILEC), retains a monopoly over the loops that serve virtually all the customers in Anchorage. In accordance with these market conditions, GCI has submitted the following proposal to the Regulatory Commission of Alaska to revise local market regulations:

Carrier of last resort responsibilities: A competitive local exchange carrier (CLEC) would be required to share in carrier of last resort (COLR) responsibilities when that competitor serves more than 35 percent of the market over its own facilities and/or with UNEs obtained from the incumbent. Sharing COLR responsibility in some cases may involve the CLEC contributing capital to the ILEC to extend facilities or extending facilities itself to unserved areas such as a new subdivision. In addition, to the extent a CLEC contributes to COLR responsibilities, it would receive corresponding discounts or credits on UNEs purchased from the ILEC. *This balanced approach toward shared carrier responsibilities demonstrates that the advancement of competition need not place with ILECs the sole obligation to bear COLR responsibilities.*

Retail pricing flexibility: Retail rate flexibility (upward and downward) would be made available to any carrier that has a retail market share of less than 65 percent in a service area. This proposal would give ILECs in competitive retail markets greater flexibility to raise and lower rates, more quickly, with less regulatory burden. An ILEC that asserts a "rural exemption" from competition, however, would not be eligible for rate flexibility; by claiming exemption, the ILEC is challenging the very basis of the competition that supports the rate flexibility.

Two conditions apply for retail pricing flexibility: (1) the rate for basic residential dialtone is capped at the existing level, with increases permitted only upon a showing of good cause; and (2) the state commission may disapprove rates that are not just and reasonable. In addition, rate flexibility would not be available for access, wholesale resale, or UNE markets, because the ILEC retains a monopoly in these wholesale markets that is not diminished by competition for local retail services. In Anchorage (as in other markets), CLECs are dependent on ACS for loops for the vast majority of customers. *Without continued access to these loops, local exchange competition would virtually disappear.*

ATTACHMENT B

Comparison of RBOC UNE Loop Rates to Embedded Loop Costs

UNE Loop Rate data from January 2003 Version of WV UNE study.
See: http://www.cad.state.wv.us/2003%20Intro%20to%20Matrix.htm
Embedded Cost data from October 2002 NECA USF Filing.

No average UNE Loop Rate for Hawaii

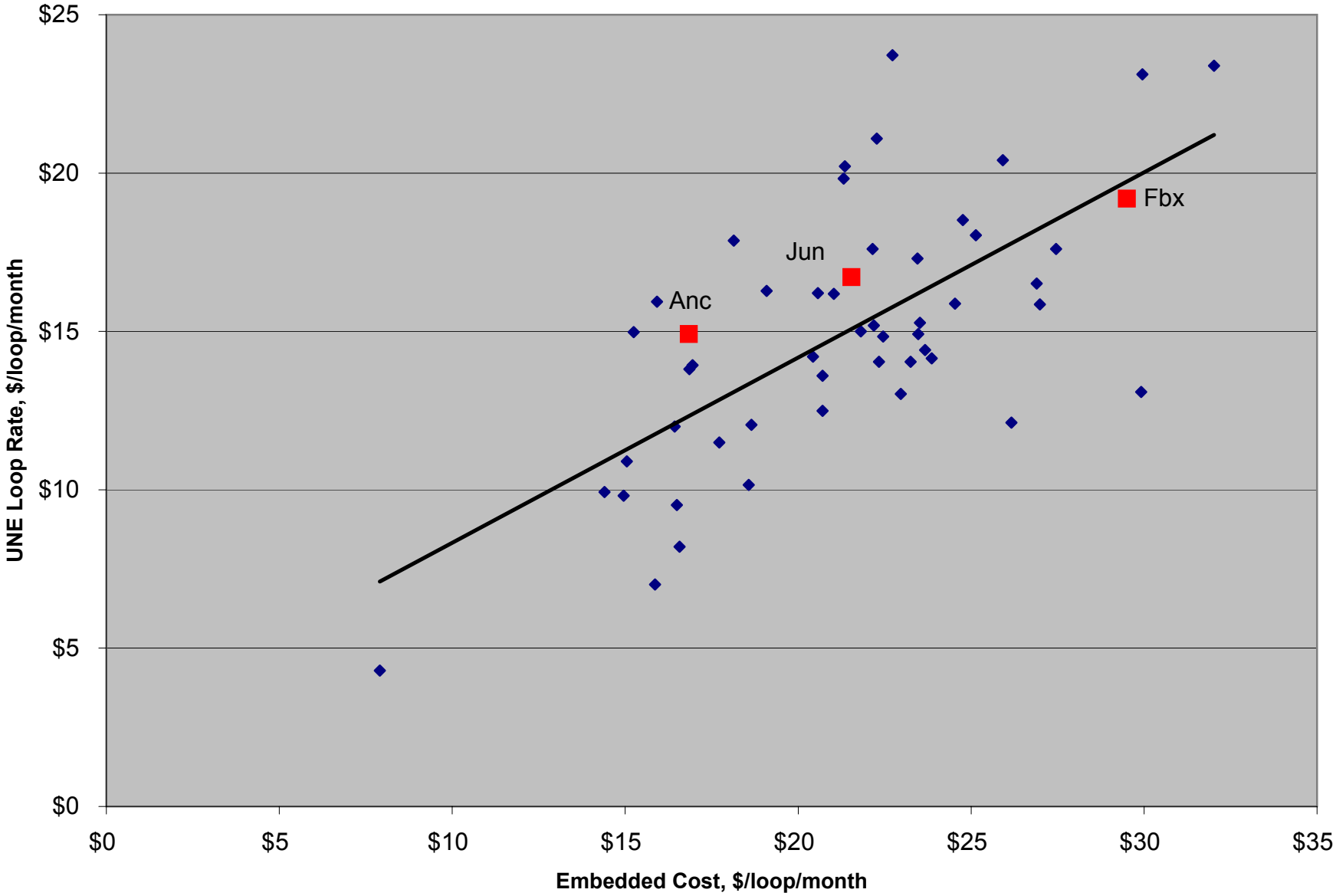
RBOC UNE Loop Rates and Embedded Cost

Access Lines	State	Embedded Loop Cost, 2001	Avg UNE Loop Rate	UNE / Embedded
1,964,890	AL	$22.15	$17.60	79.5%
2,873,044	AZ	$26.17	$12.12	46.3%
1,037,211	AR	$29.92	$13.09	43.8%
18,330,823	CA	$14.40	$9.93	69.0%
2,807,681	CO	$26.99	$15.85	58.7%
2,381,200	CT	$20.71	$12.49	60.3%
919,587	DC	$7.91	$4.29	54.3%
589,979	DE	$18.65	$12.05	64.6%
6,693,251	FL	$23.52	$15.27	64.9%
4,225,392	GA	$26.90	$16.51	61.4%
556,243	ID	$21.35	$20.21	94.7%
6,750,417	IL	$14.95	$9.81	65.6%
2,360,090	IN	$16.57	$8.20	49.5%
1,107,337	IA	$15.92	$15.94	100.1%
1,390,959	KS	$23.25	$14.04	60.4%
1,237,577	KY	$25.14	$18.04	71.8%
2,377,949	LA	$23.45	$17.30	73.8%
731,657	ME	$21.03	$16.19	77.0%
3,932,175	MD	$16.43	$12.00	73.1%
4,406,165	MA	$15.25	$14.98	98.3%
5,102,599	MI	$18.57	$10.15	54.7%
2,279,543	MN	$18.14	$17.87	98.5%
1,345,229	MS	$29.95	$23.12	77.2%
2,679,499	MO	$22.19	$15.19	68.5%
374,971	MT	$22.72	$23.72	104.4%
473,127	NE	$22.34	$14.04	62.8%
386,888	NV	$21.31	$19.83	93.0%
795,753	NH	$20.57	$16.21	78.8%
6,681,455	NJ	$16.49	$9.52	57.7%
854,785	NM	$24.76	$18.52	74.8%
11,857,572	NY	$17.72	$11.49	64.9%
2,526,805	NC	$24.54	$15.88	64.7%
211,961	ND	$19.09	$16.28	85.3%
4,184,185	OH	$15.86	$7.01	44.2%
1,663,280	OK	$22.46	$14.84	66.1%
1,424,151	OR	$21.81	$15.00	68.8%
6,283,372	PA	$16.85	$13.81	82.0%
641,977	RI	$16.95	$13.93	82.2%
1,503,098	SC	$27.45	$17.60	64.1%
257,651	SD	$22.27	$21.09	94.7%

2,673,375	TN	$23.47	$14.92	63.6%
10,128,429	TX	$23.86	$14.15	59.3%
1,076,872	UT	$22.97	$13.03	56.7%
360,161	VT	$23.67	$14.41	60.9%
3,583,082	VA	$20.71	$13.60	65.7%
2,496,763	WA	$20.43	$14.20	69.5%
862,638	WV	$25.92	$20.41	78.7%
2,207,651	WI	$15.05	$10.90	72.4%
261,260	WY	$32.02	$23.39	73.0%
Weighted Average:		**$19.57**	**$12.98**	**66.3%**

ACS Companies

Access Lines	State	Embedded Loop Cost, 2001	Avg UNE Loop Rate	UNE / Embedded
180,407	ACS-Anc	$16.84	$14.92	88.6%
44,825	ACS-Fbx	$29.50	$19.19	65.0%
27,502	ACS-Jun	$21.55	$16.71	77.6%


$25
$20
$15
$10
$5
$0
UNE Loop Rate, $/loop/month
Anc
Jun
Fbx
$0
$5
$10
$15
$20
$25
$30
$35
Embedded Cost, $/loop/month