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

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FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of

AT&T Corp.	)
	)
Petition for Preemption, Pursuant to Section 253 of the Communications Act And Common Law Principles, of South Carolina Statutes that Discriminate Against New Entrants	)

CC Docket 96-45

PETITION FOR PREEMPTION

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PETITION FOR PREEMPTION

AT&T Corp ("AT&T") respectfully petitions the Federal Communications Commission ("Commission") to preempt South Carolina statutes and administrative procedures that unlawfully establish an "Interim LEC Fund" that pays subsidies to incumbent LECs for reducing their intrastate access charges and that requires long distance carriers to fund these subsidies. Because this program is not competitively neutral, discriminates against new entrants and has the effect of deterring competitive entry, it violates Section 253 of the Communications Act of 1934, as amended (the "Act"), as well as traditional preemption principles, and must be preempted by the Commission.[1]

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[1] 47 U.S.C. § 253

INTRODUCTION AND SUMMARY

This case arises because South Carolina has implemented a program providing state subsidies to incumbent local exchange carriers ("incumbent LECs" or "ILECs") that reduce their intrastate access charges and requiring long distance carriers (but not other types of carriers) to pay for these subsidies This program is blatantly discriminatory and not competitively neutral in two important respects: (1) it provides a competitive advantage to ILECs by providing them, and them alone, with state support, and (2) it creates a competitive *dis*advantage for long distance providers – especially those who also provide competitive local exchange service – by requiring them, and them alone, to fund the support This scheme, which radically tilts the competitive playing field in favor of incumbents and against new entrants, is clearly unlawful and must be preempted

Section 253(a) of the Act requires the Commission to preempt state or local legal requirements that "may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service" South Carolina's subsidy scheme is precisely the sort of program that section 253 prohibits and that undermines the pro-competitive objectives of this key federal policy This program plainly gives ILECs a structural pricing advantage vis-à-vis new entrants Indeed, the Commission has opined that a similar Kansas scheme for providing state support to ILECs in the context of access charge reform would likely be prohibited by section 253. Moreover, the South Carolina scheme suffers from the additional flaw that it doubly disadvantages competitive LECs who also provide long distance by making them pay for the scheme (as well as rendering them ineligible for support)

Although section 253(b) saves from preemption competitively neutral state requirements that are necessary to advance universal service and serve certain other public policy goals, it does not apply here because the South Carolina program cannot be deemed competitively neutral under any measure Independently, section 253(b)'s safe harbor for state universal service programs cannot apply because it only saves state universal service programs that are consistent with the requirements for federal universal service programs, including the requirement that all telecommunications carriers contribute to universal service support. Because South Carolina's funding mechanism singles out long distance providers, and does not require contributions from all carriers, the subsidies cannot qualify as a universal service program protected from preemption under section 253(b)

Apart from section 253, the South Carolina program must be preempted under the traditional principle that preemption is required when there exists a conflict between federal and state law. The South Carolina program conflicts with section 254 of the Act Section 254 not only expressly requires that all telecommunications carriers contribute to federal universal service support, but subsection (f) of section 254 expressly requires *state* universal service programs to be funded by *all* telecommunications carriers who provide intrastate service South Carolina's discriminatory funding mechanism, which requires contributions only from long distance carriers, directly conflicts with these federal requirements and therefore must be preempted

BACKGROUND

In May 1996, the South Carolina General Assembly enacted legislation to "facilitate the change to a competitive market for local telephone services" *Porter* v *South Carolina Public Service Commission*, 525 S.E.2d 866, 867 (S.C. 2000). This legislation included provisions designed to "enable incumbent local exchange carriers to lower their intrastate toll-switched access rates, which are the rates paid by long distance carriers to access the local network, by providing a mechanism to offset the resulting loss of revenue to the local exchange carriers" *Id.* Specifically, the legislation provided that incumbent local exchange carriers could elect to "lower their access rates to the level of rates charged by the largest local exchange carrier, BellSouth," and established an Interim LEC Fund "[t]o help offset the local exchange carriers' resulting loss of revenue" *Id* [2]

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[2] The relevant provisions are subsections (L) and (M) of S.C Code Ann § 58-9-280, which provide

On October 10, 1996, the South Carolina Public Service Commission ("PSC") established a docket (No 96-318-C) to address the creation of the Interim LEC Fund Incumbent LECs electing to lower their intrastate access rates were required to notify the PSC of their intent, provide financial information pertaining to the access revenues that would be lost due to the rate reductions, and indicate the method of recovery they would use *Porter*, 525 S.E.2d at 867

> (L) Upon enactment of this section and the establishment of the Interim LEC Fund, as specified in subsection (M) of this section, the commission [South Carolina Public Service Commission] shall, subject to the requirements of federal law, require any electing incumbent LEC, other than an incumbent LEC operating under an alternative regulation plan approved by the commission before the effective date of this section, to immediately set its toll switched access rates at levels comparable to the toll switched access rate levels of the largest LEC operating within the State To offset the adverse effect on the revenues of the incumbent LEC, the commission shall allow adjustment of other rates not to exceed statewide average rates, weighted by the number of access lines, and shall allow distributions from the Interim LEC Fund, as may be necessary to recover those revenues lost through the concurrent reduction of the intrastate switched access rates
>
> (M) The commission shall, not later than December 31, 1996, establish an Interim LEC Fund The Interim LEC Fund shall initially be funded by those entities receiving an access or interconnection rate reduction from LEC's pursuant to subsection (L) in proportion to the amount of the rate reduction To the extent that affected LEC's are entitled to payments from the USF [South Carolina's universal service fund], the Interim LEC Fund must transition into the USF as outlined in Section 58-9-280(E) when funding for the USF is finalized and adequate to support the obligations of the Interim LEC Fund.

Twenty-five LECs elected to participate. The PSC held hearings on December 16 and 17, 1996 to address all issues relating to establishment of the Interim LEC Fund and proposed rate adjustments by the participating LECs. On December 31, 1996, the PSC issued its Order establishing the Interim LEC Fund, adopting administrative procedures for operation of the fund, and adjusting rates for the participating LECs. *See* South Carolina PSC, Order No. 96-882-C (Dec. 31, 1996).[3]

The Interim LEC Fund began operating in 1997. It is currently sized at more than $34 million. AT&T's current contributions exceed $9 million per year.

In the same legislation that created the Interim LEC Fund, the South Carolina General Assembly also ordered the PSC to "establish a universal service fund (USF) for distribution to a carrier(s) of last resort."[4] The PSC commenced a proceeding to establish a USF in 1997 and that proceeding lasted over four years. The PSC's final orders establishing and implementing South Carolina's USF were issued in 2001 and affirmed by the South Carolina

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[3] The Consumer Advocate appealed the PSC's Order on the ground that the rate increases were ordered without adequate notice to the public. The state circuit court affirmed the PSC, but the Supreme Court of South Carolina reversed, holding that the rate increases were ordered without adequate notice in violation of due process. *Porter*, 525 S.E.2d 866. The Supreme Court of South Carolina ordered the PSC to "hold hearings for each local exchange carrier after adequate notice to the affected customers, re-evaluate the total five-year rate increases, and adjust the future scheduled annual rate increases if necessary." *Id.* at 869. On remand, the PSC reaffirmed the previously-approved rate adjustments. South Carolina PSC, Order No. 2001-396 (May 16, 2001).

[4] S.C. Code Ann. § 58-9-280(E).

state court last week As of this date, the Interim LEC Fund has not been transitioned into the USF and no time frame for doing so has been established

ARGUMENT

I. THE COMMISSION MUST PREEMPT THE SOUTH CAROLINA STATUTES AND ADMINISTRATIVE PROCEDURES ESTABLISHING THE INTERIM LEC FUND PURSUANT TO SECTION 253 OF THE COMMUNICATIONS ACT.

Section 253 of the Act is a critical component of the congressional plan to promote extensive entry of new firms into local markets Entitled "Removal of barriers to entry," section 253 creates the legal framework for federal preemption by providing that no state or local statute, regulation, or legal requirement "may prohibit or have the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service"[5] Thus, section 253 was designed to level the playing field, previously monopolized by incumbent local exchange carriers as a consequence, in part, of state and local regulation protecting such monopolies, by requiring that any state or local regulation henceforward be "competitively neutral" and "nondiscriminatory"[6] "Through this provision, Congress sought to ensure that its national competition policy for the telecommunications industry would indeed be the law of the

[5] 47 U S C § 253(a)
[6] *Id* §§ 253(b), (c)

land and could not be frustrated by the isolated actions of individual municipal authorities or states."[7]

The Commission has broadly construed section 253(a) as commanding it "to sweep away not only those state or local requirements that explicitly and directly bar an entity from providing any telecommunications service, but also those state or local requirements that have the practical effect of prohibiting an entity from providing service."[8] With respect to this latter category of "indirect, effective prohibitions," the Commission considers "whether they materially inhibit or limit the ability of any competitor or potential competitor to compete in a fair and balanced legal and regulatory environment."[9] The Commission has also held that section 253 of the Act forbids barriers to entry whether they are "absolute" or "conditional," and on review the Tenth Circuit agreed that a barrier need not be "insurmountable" or complete to violate section 253(a).[10]

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[7] *In re Public Utility Commission of Texas*, 13 F.C.C.R. 3460, ¶ 4 (1997) ("*Texas Preemption Order*")

[8] *Id.* ¶ 22, *see also id.* ¶ 41 (section 253 "requires us to preempt not only express restrictions on entry, but also restrictions that indirectly produce that result").

[9] *Id.* ¶ 22.

[10] *Silver Star Telephone Co., Inc. Petition for Preemption and Declaratory Ruling*, 13 F.C.C.R. 16356, ¶ 8 (1998), *aff'd sub nom. RT Communications, Inc. v. FCC*, 201 F.3d 1264, 1268 (10th Cir. 2000); *see also New England Public Communications Council Petition for Preemption Pursuant to Section 253*, 11 F.C.C.R. 19713, ¶ 20 (1996) (statute or regulation violates section 253(a) if it "significantly affects, if not completely eliminates," the ability of telecommunications service providers other than incumbent LECs to enter a market)

Congress exempted from the general proscription of section 253(a) regulatory actions that meet the criteria of section 253(b) Specifically, section 253(b) preserves the states' authority "to impose, on a competitively neutral basis and consistent with section 254 of this section, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers."[11] With respect to state regulatory actions that address universal service issues, the Commission has held that a state program must meet "all three of these criteria – it must be 'competitively neutral,' 'consistent with section 254,' and 'necessary to preserve and enhance universal service' – to fall within the 'safe harbor' of section 253(b)."[12] Accordingly, the Commission has preempted state regulations for failure to satisfy even one of these criteria.[13]

The Commission has explained that the proper approach for analyzing preemption questions under section 253 is a two-step process The Commission first "determine[s] whether the challenged law, regulation or legal requirement violates the terms of section 253(a) standing

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[11] 47 U.S.C. § 253(b)

[12] *Western Wireless Corp.*, 15 FCC.R 16227, ¶ 9 (2000) ("*Western Wireless*"), citing *Pittencrieff Communications, Inc.*, 13 F.C.C.R 1735, ¶ 33 (1997), *aff'd sub nom. CTIA* v. *FCC*, 168 F.3d 1332 (D.C. Cir 1999) ("*Pittencrieff*").

[13] *See, e.g.*, *Silver Star Telephone Company*, 12 FCCR 15639, ¶¶ 42, 45 (1997) (preempting Wyoming statute for failure to satisfy the "competitive neutrality" criterion), *recon. denied*, 13 FCCR. 16356 (1998), *aff'd sub nom RT Communications, Inc* v *FCC*, 201 F.3d 1264 (10th Cir 2000)

alone."[14] If the Commission finds that the challenged law or regulation "violates section 253(a) considered in isolation," it then "determine[s] whether the requirement nevertheless is permissible under section 253(b)."[15] If a law "otherwise impermissible under subsection (a) does not satisfy the requirements of subsection (b)," the Commission must preempt it.[16] If, however, the challenged law satisfies subsection (b), the Commission "may not preempt it under section 253, even if it otherwise would violate subsection (a) considered in isolation."[17] Subsection 253(d) expressly empowers – "indeed, obligates"[18] – the Commission to preempt state laws that cannot survive this analysis, providing that "the Commission *shall* preempt the enforcement of such statute, regulation, or legal requirement to the extent necessary to correct such violation or inconsistency."[19]

A. THE SOUTH CAROLINA STATUTES AND ADMINISTRATIVE PROCEDURES ESTABLISHING THE INTERIM LEC FUND VIOLATE SECTION 253(a) BECAUSE THEY DISCRIMINATE AGAINST NEW ENTRANTS AND HAVE THE EFFECT OF PROHIBITING THEIR ABILITY TO PROVIDE TELECOMMUNICATIONS SERVICES.

South Carolina's discrimination against long distance carriers, especially those who also provide competitive local exchange service, in its Interim LEC Fund is precisely the

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[14] *Texas Preemption Order* ¶ 42
[15] *Id*
[16] *Id*
[17] *Id*
[18] *Id* ¶ 22
[19] 47 U.S.C. § 253(d) (emphasis added).

sort of scheme that section 253(a) prohibits The Commission has concluded that costs imposed only on new entrants are classic barriers to entry[20] Plainly, the imposition of substantial costs that are not borne equally by business rivals necessarily creates barriers to entry deterring the competitive provision of service Costs imposed only on particular types of carriers – and not on their direct competitors – violate section 253(a) because they "materially inhibit or limit the ability of" the disfavored carriers to "compete in a fair and balanced legal and regulatory environment"[21]

South Carolina's Interim LEC Fund discriminates against new entrants, and thereby materially limits their ability to compete, in two important respects. First, eligibility for receiving disbursements from the fund is limited to incumbent LECs[22] New entrants into the South Carolina market therefore face a substantial barrier to entry because their principal competitors (incumbent LECs) are receiving substantial support from the State of South Carolina that is not available to them A program that provides support only to incumbent LECs for

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[20] *See Implementation of Section 19 of the Cable Television Consumer Protection And Competition Act of 1992*, 9 F C C.R. 7442, Appendix H ¶ 29 (1994) defining a barrier to entry as "a cost of producing (at some or every rate of output) which must be borne by a firm which seeks to enter an industry but is not borne by firms already in the industry") (quoting G. Stigler, The Organization of Industry 67 (1968))

[21] *Texas Preemption Order* ¶ 22

[22] S.C. Ann § 58-9-280(L) ("To offset the adverse effect on the revenues of the *incumbent LEC*, the commission shall allow distributions from the Interim LEC Fund, as may be necessary to recover those revenues lost through the concurrent reduction of the intrastate switched access rates") (emphasis added)

access charge rate reduction effectively lowers the price for incumbent LEC-provided service relative to competitor-provided service As a consequence, other carriers cannot compete with incumbent LECs on a level playing field.

The Commission adopted precisely this analysis in addressing a similar Kansas scheme for providing support to incumbent LECs who reduced their intrastate access charges In the wake of the 1996 Act, Kansas (like South Carolina) passed legislation requiring all local exchange carriers in the state to reduce their intrastate access charges to interstate levels.[23] The Kansas legislation authorized the Kansas Corporation Commission ("KCC") to offset the resulting revenue loss to carriers by rebalancing local residential and business rates and by making payments directly to carriers from the Kansas Universal Service Fund ("KUSF"). In implementing this legislation, the KCC issued orders providing that incumbent LECs would be eligible for KUSF funding with respect to their operations statewide, while competing LECs would be eligible for KUSF funding only for service provided in exchanges with 10,000 or fewer access lines, *i e*., exchanges in rural areas[24] Western Wireless filed a petition for preemption under section 253, seeking to "preempt[] the provisions of the Kansas Act and the accompanying rules adopted by the KCC that served to limit the ability of carriers other than ILECs to receive

[23] *Western Wireless* ¶ 2
[24] *Id* ¶ 3

universal service support under the Rate Cut Funding program in exchange areas with more than 10.000 access lines."[25]

The Commission ultimately concluded that Western Wireless's petition was rendered moot by subsequent KCC orders that made all KUSF funding fully portable to competing carriers,[26] but it nevertheless addressed the original Kansas program because of concerns "that programs structured like the original Rate Cut Funding program could easily run afoul of section 253."[27] As the Commission concluded: "We would be concerned about a universal service fund mechanism that provides funding only to ILECs. A new entrant faces a substantial barrier to entry if its main competitor is receiving substantial support from the state government that is not available to the new entrant."[28] The Commission explained that such programs impose a structural pricing disadvantage on new entrants:

> A mechanism that makes only ILECs eligible for explicit support would effectively lower the price of ILEC-provided service relative to competitor-provided service by an amount equivalent to the amount of the support provided to ILECs that was not available to their competitors. Thus, non-ILECs would be left with two choices – match the ILEC's price charged to the customer, even if it means serving the customer at a loss, or offer the service to the customer

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[25] *Id.* ¶ 4

[26] *Id.* ¶ 6

[27] *Id.* ¶ 7

[28] *Id.* ¶ 8 (footnote omitted).

at a less attractive price based on the unsubsidized cost of providing such service[29]

As a result, "[a] mechanism that provides support to ILECs while denying funds to eligible prospective competitors thus may give customers a strong incentive to choose service from ILECs rather than competitors."[30] Ultimately, the Commission concluded, potential competitors are unlikely to enter the market

> Further, we believe that it is unreasonable to expect an unsupported carrier to enter a high-cost market and provide a service that its competitor already provides at a substantially supported price. In fact, such a carrier may be unable to secure financing or finalize business plans due to uncertainty surrounding its state government-imposed competitive disadvantage. Consequently, such a program may well have the effect of prohibiting such competitors from providing telecommunications service, in violation of section 253(a).[31]

Under the Commission's *Western Wireless* decision, the Interim LEC Fund's limitation of eligibility (and hence state support) to incumbent LECs is a barrier to entry that is prohibited by section 253(a). The South Carolina Interim LEC Fund has the same fundamental purpose as the Kansas Rate Cut Funding program: to provide state subsidies to incumbent LECs to offset their revenue loss from reducing intrastate access charges to competitive levels that reflect their costs (as opposed to the inflated, above-cost rates that they charged previously under

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[29] *Id.*
[30] *Id.*
[31] *Id.*

monopoly conditions). Although Kansas provided these subsidies through its universal service fund, while South Carolina established a separate fund for these subsidies (as an interim measure because it had no universal service fund in 1996), the discriminatory effect is precisely the same By providing disbursements "only to ILECs," the Interim LEC Fund creates a "state government-imposed competitive disadvantage" for competing carriers.[32] Because ILECs in South Carolina receive "substantial support from the state government that is not available" to competing carriers, this subsidy "effectively lower[s] the price of ILEC-provided service relative to competitor-provided service," to the competitive detriment of non-incumbents.[33] Accordingly, for the reasons that the Commission identified in its *Western Wireless* decision, the disbursement limitation of the Interim LEC Fund creates a barrier to entry that is prohibited by section 253(a)

The second aspect of the Interim LEC Fund that violates section 253(a) is its funding mechanism Pursuant to the statute, the Interim LEC Fund is "funded by those entities receiving an access or interconnection rate reduction from LEC's pursuant to subsection (L) in proportion to the amount of the rate reduction."[34] Since AT&T and other traditional long distance carriers pay the vast majority of access charges, they bear the principal burden of funding the subsidies for incumbent LECs AT&T in particular bears a heavy burden (currently

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[32] *Id*
[33] *Id*
[34] S C Code Ann § 58-9-280(M).

over $9 million per year) because it is the largest long distance carrier in the state Carriers who do not fall within the definition in subsection (M) pay nothing In particular, incumbent local exchange carriers who do not provide long distance service do not make contributions As a result, long distance carriers, especially those who are trying to introduce local service competition, effectively subsidize their entrenched competitors.

Under the Commission's *Western Wireless* decision, this funding mechanism is prohibited by section 253(a) Like the Kansas scheme's discriminatory distributions, it imposes a "state government-imposed competitive disadvantage" on the single category of telecommunications carriers who contribute to the Interim LEC Fund and thereby creates an unequal playing field that prevents these carriers from "compet[ing] in a fair and balanced legal and regulatory environment."[35] Carriers who pay into the fund bear an additional cost that their direct competitors do not This state-imposed cost differential requires the disfavored carriers to choose between raising their prices, or keeping their prices the same so as not to lose customers, but thereby earning less revenue (or even incurring a loss)[36] This is precisely the sort of state-imposed discrimination that section 253(a) prohibits because it undermines the development of true market-based competition

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[35] *Western* Wireless ¶ 8, *Texas Preemption Order* ¶ 22
[36] *Western Wireless* ¶ 8

Moreover, because South Carolina's Interim LEC Fund is discriminatory with respect to *both* its distributions and its funding mechanism, it imposes a far more powerful barrier to entry than the Kansas scheme.[37] Long distance providers are disadvantaged at both ends of the South Carolina program: they bear the burden of funding it, but are ineligible to receive distributions from it. In effect, they are forced to support their chief competitors, the incumbent LECs.

The South Carolina program also stands in stark contrast to the federal universal service program. The intrastate access charge reform and Interim LEC Fund implemented by the South Carolina General Assembly in 1996 are in effect a universal service program. Specifically, they mirror Congress's efforts to transition the federal universal service program from a monopolistic market to a competitive market. Under the 1996 Act, Congress provided that "the old regime of *implicit* subsidies – that is, 'the manipulation of rates for some customers to subsidize more affordable rates for others' – must be phased out and replaced with *explicit* universal service subsidies – government grants that cause no distortion to market prices – because a competitive market can bear only the latter."[38] The provisions of South Carolina's

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[37] In contrast to the Interim LEC Fund, the Kansas USF (which provided the subsidies under the Kansas scheme) is funded by all telecommunications carriers. *See Western Wireless* ¶ 2 (noting that "Section 66-2008(b) [of the Kansas Telecommunications Act] also requires all telecommunications providers, including wireless providers, to contribute to the KUSF on an equitable and nondiscriminatory basis")

[38] *Alenco v. FCC*, 201 F.3d 608, 616 (5th Cir. 2000) (emphasis in original) (quoting *Texas Office*

1996 legislation at issue here are designed to serve the same purpose They are designed to eliminate an implicit subsidy for universal service (inflated access charges that subsidize local rates in high-cost areas) and replace it with an explicit subsidy for providing universal local service Accordingly, the South Carolina General Assembly expressly provided that the Interim LEC Fund "must transition into the [South Carolina's] USF" when the state USF is established and fully funded [39]

Unlike the Interim LEC Fund, which requires long distance providers *alone* to fund South Carolina's explicit universal service subsidies, Congress required the federal USF to be funded by all telecommunications carriers [40] In implementing the statute, the Commission concluded that "the base of contributors to universal service should be construed broadly" pursuant to the statutory directive "to assess contributions to universal service on an equitable and nondiscriminatory basis." [41] As the Commission concluded

> By defining 'telecommunications' broadly, we will broaden the base of mandatory contributors and will reduce the burden and

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of Public Utility Counsel v *FCC*, 183 F 3d 393, 406 (5th Cir 1999)); *see also* 47 U S C. § 254(e) (universal service support "should be explicit")

[39] S C Code Ann. § 58-9-280(M)

[40] 47 U S C § 254(b)(4) ("All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service"). *id* § 254(d) ("Every telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service")

[41] *Federal-State Joint Board on Universal Service*, 12 F.C.C R 8776, ¶ 779 (1997) ("*Universal Service Order*")

> possible impact on individual carriers' prices It is also competitively neutral to require all carriers and 'other providers of interstate telecommunications' to contribute to the support mechanisms because it reduces the possibility that carriers with universal service obligations will compete directly with carriers without such obligations [42]

Thus, the Commission concluded that requiring all carriers to contribute to the federal USF was necessary to maintain competitive neutrality and to avoid imposing a competitive disadvantage on contributors The Interim LEC Fund imposes just such a competitive disadvantage on its contributors – long distance providers – because their direct competitors are not required to make contributions Thus, the fact that the Interim LEC Fund utilizes a funding mechanism that Congress and the Commission expressly rejected as detrimental to competition provides further evidence that it is a barrier to entry prohibited by section 253(a)

Finally, the fact that the Interim LEC Fund is nominally a temporary arrangement (which has been in effect since 1996) that will "transition into the USF,"[43] does not save it from preemption As the Commission has expressly held, a state requirement which otherwise violates section 253 "cannot be saved merely because it is transitional."[44]

B. THE SOUTH CAROLINA STATUTES AND ADMINISTRATIVE PROCEDURES ARE NOT PERMISSIBLE UNDER SECTION 253(b).

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[42] *Id* ¶ 783

[43] S C Code Ann § 58-9-280(M)

[44] *Western Wireless* ¶ 10 (citing *Silver Star*, 12 F C C R 15639, ¶ 39).

The Interim LEC Fund is not permissible under any of the "safe harbors" in section 253(b) That section provides that regulatory actions that are otherwise impermissible under section 253(a) can escape preemption if, and only if, they "impose, on a competitively neutral basis and consistent with section 254 of this section, requirements necessary to preserve and advance universal service, protect the public safety and welfare, ensure the continued quality of telecommunications services, and safeguard the rights of consumers." The Interim LEC Fund cannot escape preemption under section 253(b), either as a universal service program or under any of the other public policy rationales specified in the statute, because it is not competitively neutral As demonstrated above, failure to satisfy the competitive neutrality criterion is fatal to any attempt to satisfy the requirements of section 253(b) [45]

The Commission consistently has held that state and local regulations are not competitively neutral if they impose costs only on certain carriers [46] In particular, state and local regulations are not competitively neutral if they disadvantage new entrants relative to incumbents As the Commission has held,

> Neither the language of section 253(b) nor its legislative history suggests that the requirement of competitive neutrality applies only

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[45] *See, e g., Silver Star Telephone Company*, 12 F C C R. 15639, ¶¶ 42, 45 (1997) (preempting Wyoming statute for failure to satisfy the "competitive neutrality" criterion), *recon. denied*, 13 F C C.R 16356 (1998), *aff'd sub nom RT Communications, Inc.* v. *FCC*, 201 F.3d 1264 (10th Cir 2000)

[46] *See, e g , Classic Telephone, Inc.*, 11 F C C R 13082 ¶ 37 (1996) ("competitive neutrality requires the Cities to treat similarly situated entities in the same manner").

> to one portion of a local exchange market – new entrants – and not to the market as a whole, including the incumbent LEC Indeed, the plain meaning of section 253(b) and the predominant pro-competitive policy of the 1996 Act indicate just the opposite [47]

Indeed, favoritism of incumbents is one of the gravest threats to competition that section 253 combats, given the political power and strong relationships of incumbents with state and local governments Accordingly, "[l]ocal requirements imposed only on the operations of new entrants and not on existing operations of incumbents are quite likely to be neither competitively neutral nor nondiscriminatory "[48] In sum, section 253 requires that state and local regulatory actions must be neutral in their effect on the ability of all carriers to compete

The Interim LEC Fund is the antithesis of "competitive neutrality." It disburses revenue *only* to incumbent LECs As the Commission concluded with respect to the identical feature of the Kansas program, "[b]ecause a mechanism that offers non-portable support may give ILECs a substantial unfair price advantage in competing for customers, it is difficult to see how such a program could be considered competitively neutral "[49] In addition, the Interim LEC Fund is funded exclusively by carriers who pay intrastate access charges The net result is that the South Carolina program forces competing local exchange carriers who provide long distance

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[47] *Silver Star*, 13 F C C R 16356 ¶ 10, *see also id* ¶ 11 ("section 253(b) cannot 'save' a state legal requirement from preemption pursuant to sections 253(a) and (d) unless, inter alia, the requirement is competitively neutral with respect to, and as between, all of the participants and potential participants in the market at issue")

[48] *TCI Cablevision of Oakland County, Inc* , 12 F C C.R 21396, ¶¶ 107-08 (1997)