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
	)	
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337

COMMENTS OF THE NATIONAL ASSOCIATION OF STATE UTILITY CONSUMER ADVOCATES

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EXECUTIVE SUMMARY

First in *Qwest I* in 2001, and then in *Qwest II* in 2005, the Tenth Circuit Court of Appeals rejected two versions of the Federal Communications Commission's ("Commission's") high-cost support mechanism for non-rural companies.[1] There is thus a desperate need for the Commission to adopt a mechanism that complies with 47 U.S.C. § 254.

In these comments, the National Association of State Utility Consumer Advocates ("NASUCA") presents two alternatives for the Commission's consideration. The first alternative strikes out in a new direction that simplifies the way in which high-cost support for non-rural carriers is determined. The second alternative retains much of the current mechanism, while attempting to meet the concerns on which the Tenth Circuit based its rejection and remand of prior Commission orders; in that respect it is more

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[1] *Qwest Corporation v. FCC*, 258 F.3d 1191 (10th Cir. 2001) ("*Qwest I*"); *Qwest Communications v. FCC*, 398 F.3d 1222 (10th Cir. 2005) ("*Qwest II*").

complicated than either the current mechanism that was overturned in *Qwest II* or the first NASUCA alternative. Both alternatives are based on the fact that the key purpose of the non-rural high-cost fund is to meet the statutory principle that non-rural companies' rates in the high-cost and rural portions of their service territories should be "reasonably comparable" to rates in urban areas. Having this as the key purpose is consistent with the requirement of *Qwest II* that the Federal Communications Commission ("FCC" or "Commission") shall consider each of the principles in 47 U.S.C. § 254(b) in developing universal service policies.[2] Both of NASUCA's proposals replace the current three pieces of the non-rural high-cost universal service fund ("USF") with a single fund.

In order to determine whether rural rates are reasonably comparable to urban rates, it is necessary to know what those rates are.[3] In these comments, NASUCA presents the Commission with data that encompasses rates as of February 2006 in more than 11,000 wire centers nationwide -- urban, rural, and in between -- that are served by the non-rural carriers under examination here.[4]

A key part of *Qwest II* was the Tenth Circuit's rejection of the Commission's "reasonably comparable" standard.[5] That standard was adopted in the *Order on*

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[2] *Qwest II*, 398 F.3d at 1234.

[3] It is also necessary to define urban "areas" and rural "areas," in order to know which rates are which. This is accomplished in these comments by using Census Bureau definitions.

[4] As expressed by NASUCA in comments on the high-cost mechanism for rural carriers, the differences between rural carriers as a whole and non-rural carriers are significant, and the Commission should exercise caution in addressing the question of whether and how to combine the two mechanisms. NASUCA Comments (October 15, 2004) at 7-9, 15-19. NASUCA has suggested moving the largest rural carriers onto the forward-looking cost test currently used for the non-rural carriers. Id. at 28-29. That change, if adopted by the Commission, would be sufficient unification for now.

[5] *Qwest II* , 398 F.3d at 1234-1237.

Remand,[6] which was designed to address the Tenth Circuit's decision in *Qwest I*. The reasonable comparability standard was adopted without any review of the universe of rates, whether rural, urban or otherwise. NASUCA's data allows the Commission to do such a review. NASUCA does not, however, propose a specific standard here.

A. The urban revenue/rural cost alternative

The current support mechanism takes a sample of 95 urban rates from around the nation, determines the national weighted urban average rate, and then establishes a rate comparability benchmark at two standard deviations above the average. A cost benchmark is set at two standard deviations above the national weighted average cost, based on the Commission's high-cost model ("HCM").[7] Then support is granted to states that have statewide average costs that are above the benchmark.

NASUCA's first alternative proposal begins by determining a benchmark based on the national urban average per-line **revenue**, being revenue from all sources, not just basic service. This includes basic service, subscriber line charges ("SLCs"), optional/vertical services, access charges, and advanced services, in recognition that the network is constructed to provide multiple services, both traditional and advanced. Then, the **costs** in all wire centers are compared to that national urban average revenue. Support is then awarded to all wire centers with costs that are higher than the national urban revenue

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[6] *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45 (hereafter "CC Docket No. 96-45"), Order on Remand, Further Notice of Proposed Rulemaking, and Memorandum Opinion and Order, 18 FCC Rcd 22559 (2003) ("*Order on Remand*"), *remanded*, *Qwest II*, 398 F.3d at 1222.

[7] NPRM, ¶ 5.

benchmark.[8] The presumption contained in this proposal is that areas with costs that are greater than the urban revenue benchmark **will find it impossible** to have basic service rates that are reasonably comparable to urban rates in the absence of support.

B. The rate-focused alternative

NASUCA's second alternative begins and ends by looking at the rates that federal support is intended to help make reasonably comparable to urban rates. NASUCA's second alternative consists of steps to be taken upon the initial application as a transition from the current mechanism, then followed by steps for the initial process that will be repeated annually. The mechanism is more complex than NASUCA's first alternative. The mechanism first determines **eligibility** for support through an examination of rates. This follows the law and the Tenth Circuit's rulings. Then, following the current mechanism, the **amount** of support is based on costs. That is the appropriate method for apportioning support from the federal USF, placing the primary responsibility for ratemaking on the states, while assisting with support for areas in states that have -- as a whole -- high costs that otherwise would be accounted for in rates. In the end, the support awarded is again compared to the local service rate, in order to judge whether the support produces reasonably comparable rates.

Backstopping the process throughout is a mechanism where individual states can set forth specific conditions that justify providing support in areas that -- through the standard operation of the mechanism -- would not receive support. Here again, NASUCA's second alternative builds on the current system.[9]

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[8] All rural and all high-cost wire centers are eligible for support. 47 U.S.C. § 254(b)(3). If an urban wire center happened to be high-cost enough that its costs were greater than the national urban average per-line revenues, it would likely need support to maintain reasonable comparability of rates.

[9] See *Order on Remand*, ¶ 93.

This proposal is designed as a gradual, iterative process where the industry, the Commission, the states and consumers learn as the process is implemented. This is consistent with the evolving nature of universal service.[10]

Under the current system, only ten states receive support for their non-rural companies explicitly based on their high costs.[11] Thirty-eight states, the District of Columbia and Puerto Rico receive no funding based on high costs, due to the fact that their statewide average costs do not exceed the Commission's benchmarks.[12] Non-rural ILECs in 39 jurisdictions receive interstate access or interstate common line support, which were designed as revenue replacement mechanisms, but fall under the high-cost rubric.[13]

Only Wyoming has requested additional support under the Commission's supplemental mechanism.[14] The state commissions in the other states have not requested funding under the Commission's supplemental mechanism. It would be safe to assume, then, that those commissions believe their rural rates to be reasonably comparable to urban rates under the current benchmark. That is borne out by the data compiled for NASUCA.

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[10] 47 U.S.C. § 254(c)(1).

[11] See Section IV., below.

[12] USAC filing for 1Q06, Appendix HC01.

[13] As discussed below, the support mechanisms should be combined such that there is a single "high cost" support mechanism.

[14] CC Docket No. 96-45, "Joint Petition of the Wyoming Public Service Commission and the Wyoming Office of Consumer Advocate for Supplemental Federal Universal Service Funds for Customers of Wyoming's Non-Rural Incumbent Local Exchange Carrier" ("Joint Wyoming Petition") (December 21, 2004). The Commission has taken no action on Wyoming's request -- other than requesting public comment -- in the more than a year since the Joint Wyoming Petition was filed.

NASUCA's second alternative proposes that the reform of the non-rural high-cost mechanism begin with states that currently have high rural rates for their non-rural carrier(s) but receive no high-cost funding, and then progress to states that currently receive high-cost funds but still have high rural rates. Then states that have reasonably comparable rates but receive large amounts of high cost funds would be reviewed, to determine whether the funding amount is appropriate. A next step would be to review the states that, without the current high-cost funding, would likely have rates that would nonetheless be reasonably comparable; this support would be deemed not needed and could be eliminated.

I. INTRODUCTION

In a Notice of Proposed Rulemaking ("NPRM") released December 9, 2005,[15] the Commission sought comment on issues raised by 47 U.S.C. § 254(b) and the Tenth Circuit's decision in *Qwest II* regarding high-cost support for non-rural carriers.[16] Specifically, the Commission seeks comment on how to define the statutory terms "sufficient" and "reasonably comparable" in light of *Qwest II*'s rejection of the Commission's definitions of those terms.[17] The Commission also seeks comment on the support mechanism for non-rural carriers, which the *Qwest II* court invalidated due to the

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[15] FCC 05-205.

[16] Consistent with NASUCA's prior comments, the issues for non-rural carriers should be kept separate from rural carrier issues.

[17] *Qwest II*, 398 F.3d at 1233.

Commission's reliance on an inadequate interpretation of statutory principles and failure to explain how a cost-based mechanism would address problems with rates.[18]

NASUCA[19] offers its comments on the issues raised by the NPRM.[20] NASUCA's comments begin with a discussion of the relevant legal background, including both *Qwest I* and *Qwest II*, and then set forth the issues on which the Commission requested comment.[21]

These comments present two crucial sets of data for the Commission's consideration: One is the current non-rural high-cost funding situation, including not only high-cost model ("HCM") funding but interstate access support ("IAS") and interstate common line ("ICL") funding. These data are used for "eyeball" purposes but

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[18] The term "non-rural carriers" refers to ILECs that do not meet the statutory definition of a rural telephone company. *See* 47 U.S.C. § 153(37). Under this definition, rural telephone companies are ILECs that either serve study areas with fewer than 100,000 access lines or meet one of three alternative criteria. *Id.* Thus, "non-rural carriers" are principally defined by study area size. Non-rural carriers serve the majority of access lines nationwide, including lines in rural, insular, and high-cost areas. Rural ILECs serve fewer than twelve percent of lines nationwide, and their operations tend to be focused in high-cost areas. *See* USAC Quarterly Administrative Filing 2006, First Quarter (1Q) Appendices, HC05, filed November 2, 2005, at http://www.universalservice.org/overview/filings.

[19] NASUCA is a voluntary association of 45 advocate offices in 42 states and the District of Columbia, incorporated in Florida as a non-profit corporation. NASUCA's members are designated by the laws of their respective jurisdictions to represent the interests of utility consumers before state and federal regulators and in the courts. *See, e.g.*, Ohio. Rev. Code Ch. 4911; 71 Pa. Cons. Stat. Ann. § 309-4(a); Md. Pub. Util. Code Ann. § 2-205; Minn. Stat. § 8.33; D.C. Code Ann. § 34-804(d). Members operate independently from state utility commissions as advocates primarily for residential ratepayers. Some NASUCA member offices are separately established advocate organizations while others are divisions of larger state agencies (*e.g.*, the state Attorney General's office). NASUCA's associate and affiliate members also serve utility consumers, but are not created by state law or do not have statewide authority.

[20] NASUCA's efforts in preparing these comments were supported by the work of Dr. David Gabel, Dr. Robert Loube and Scott Kennedy. They contributed the rate survey discussed in Section V. and the substance of NASUCA's first proposed alternative mechanism, and assisted with the discussion of multiple-use networks in Section IX., and the broadband network investment plan in Section XIV., along with more general input. Their vitae are included as Appendices G, H and I. Kathy Hagans of the Office of the Ohio Consumers' Counsel compiled Appendix F.

[21] The Commission also sought comment on a proposal by Puerto Rico Telephone Company, Inc. ("PRTC") that the Commission adopt a non-rural insular high-cost mechanism. NPRM, ¶¶ 30-38. NASUCA will not comment on PRTC's proposal at this time, but reserves the right to address the proposal in reply comments. For this and other reasons, Puerto Rico is not included in most of the analyses here.

also -- later in the comments, in the process of NASUCA's second alternative proposal -- to compare current rates with current funding in rural areas in order to assess whether that funding is necessary, or whether additional funding might be needed.

NASUCA also presents comprehensive data on the basic service rates of non-rural companies. This is the fundamental data starting point for any mechanism that is designed to produce rural rates that are reasonably comparable to urban rates. This data shows the range and variance of rural rates, of urban rates, and of all rates -- from more than 11,000 non-rural carrier wire centers around the country. This rate analysis should be used to propose a standard of reasonable comparability to be used on a going-forward basis, including in the process described in detail later in the comments. NASUCA does not propose a specific comparability standard here.

After dealing with the data, policy questions are addressed. In *Qwest II*, the Tenth Circuit faulted the Commission for failing to consider all of the principles set forth in 47 U.S.C. § 254(b) in its determination that the high-cost mechanism created in the *Order on Remand* was sufficient to meet the statutory purposes. NASUCA reviews the principles and shows that reasonable comparability remains the key principle for constructing the high-cost fund.

A number of other important policy issues are also addressed. These include:

- Consideration of local calling areas in determining whether rural rates are reasonably comparable to urban rates;
- Consideration of state rate deregulation, multiple-use networks, and support given to competitive eligible telecommunications

carriers ("CETCs") as they impact the non-rural high-cost mechanism;

- The need for gradualism in adopting a mechanism that will meet the concerns expressed by the Tenth Circuit;
- The need to ensure that state universal service support mechanisms -- explicit or implicit -- are in place to ensure that the states play their proper role in universal service; and
- The need to reform and update the Commission's high-cost model.

With that extensive policy and data discussion out of the way, NASUCA then presents its alternative proposals to reform the non-rural high-cost universal service support mechanism. The first proposal fundamentally changes the mechanism, by comparing urban revenues to rural costs; if rural costs are greater than urban revenues, then rural rates will have to be higher than urban rates.

The second proposal goes back to basics -- beginning and ending with consideration of rural rates -- but also includes much of the current mechanism by awarding support based on forward-looking costs. The proposal also contains a continuing opportunity for states to seek support beyond that permitted by operation of the cost model if, despite the best state and federal efforts, rates are not reasonably comparable absent the additional support. NASUCA also shows how the proposals meet

the statutory requirements and the directives of the Tenth Circuit to preserve and advance universal service.[22]

Finally, NASUCA also presents additional proposals for "advancing" universal service. These include 1) investigating the reasons behind the recent apparent general declines in telephone subscribership; 2) increasing efforts to advance subscribership among low-income consumers; and 3) adopting specific measures to enlarge the offering of advanced services in rural areas served by non-rural companies.

II. LEGAL BACKGROUND

The Telecommunications Act of 1996 ("1996 Act") codified the historical commitment of the Commission and state regulators to promote universal service by ensuring that consumers in all regions of the nation have access to affordable, quality telecommunications services.[23] In § 254 of the 1996 Act, Congress directed the Commission, after consultation with the Federal-State Joint Board on Universal Service ("Joint Board"), to adopt "policies for the preservation and advancement of universal service" based on a set of six "principles."[24] Of those principles, the Commission has

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[22] In the NPRM at ¶ 29, the Commission asked "commenters to address the universal service aspects of the comprehensive plan proposed by the National Association of Regulatory Utility Commissioners (NARUC) Task Force in the Intercarrier Compensation proceeding." As seen here, NASUCA supports "combining the support contained in all of the federal high-cost support mechanisms" (id.) (or rather, supports establishing a single support mechanism); however, NASUCA submits that "giving the states discretion, within guidelines set by the Commission, to determine how the support should be distributed among carriers serving the state." (id.) is not necessary and is, actually contrary to the statutory purposes. See CC Docket No. 96-45, NASUCA Comments on Joint Board High-Cost Support Proposals (September 30, 2005) at 27-30.

[23] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996). The 1996 Act amended the Communications Act of 1934. 47 U.S.C. §§ 151, *et seq*.

[24] 47 U.S.C. § 254(b). The Commission was also permitted to adopt "additional principles…." 47 U.S.C. § 254(b)(7).

focused on § 254(b), which provides that consumers in "rural, insular, and high-cost areas" should have access to telecommunications services at rates that are "reasonably comparable to rates charged for similar services in urban areas."[25] The Commission has also focused on § 254(e), which provides that federal universal service support "should be explicit and sufficient to achieve the purposes of this section."[26]

In the *Ninth Report and Order*, the Commission established a federal high-cost universal service support mechanism for non-rural carriers based on forward-looking economic costs.[27] The Commission based the mechanism on costs, rather than on rates, for reasons discussed in the *First Report and Order*.[28]

The non-rural mechanism from the *Ninth Report and Order* overturned by *Qwest I* determined the amount of federal high-cost support to be provided to non-rural carriers by comparing the statewide average non-rural, forward-looking **cost** per line to a nationwide cost benchmark that was set at 135 percent of the national average cost per line. Federal support was provided to non-rural carriers in states with costs that exceed the national benchmark. The Commission determined that this mechanism would produce rural rates that were "reasonably comparable" to urban rates, and that as a result the non-rural high cost fund would be "sufficient."[29]

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[25] 47 U.S.C. § 254(b)(3).

[26] 47 U.S.C. § 254(e).

[27] CC Docket No. 96-45, Ninth Report & Order and Eighteenth Order on Reconsideration, FCC 99-306, 14 FCC Rcd 20432 (1999) ("*Ninth Report and Order*"), ¶ 2.

[28] CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776 (1997) ("*First Report and Order*"), ¶¶ 224-226.

[29] *Ninth Report and Order*, ¶ 2.

The *Qwest I* court directed the Commission on remand to define more precisely the statutory terms "sufficient" and "reasonably comparable" and then to assess whether the non-rural mechanism would be sufficient to achieve the statutory principle of making rural and urban rates reasonably comparable.[30] In addition, the court found that the Commission failed to explain how its 135 percent nationwide cost benchmark would help achieve the goal of reasonable comparability or sufficiency.[31]

In response to the court and the recommendations of the Joint Board, the Commission modified the high-cost universal service support mechanism for non-rural carriers, and adopted a rate review and expanded certification process to induce states to ensure reasonable comparability of rural and urban rates in areas served by non-rural carriers. In particular, the Commission defined the statutory term "sufficient" as "enough federal support to enable states to achieve reasonable comparability of rural and urban rates in high-cost areas served by non-rural carriers,"[32] and defined "reasonably comparable" in terms of a national urban residential rate benchmark,[33] set at two standard deviations above the average urban residential rate in an annual Wireline Competition Bureau rate survey.[34] In addition, the Commission modified the 135 percent cost benchmark by adopting a cost benchmark based on two standard deviations above the national average cost.[35]

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[30] *Qwest I*, 258 F.3d at 1202.

[31] Id. at 1202-03.

[32] *Order on Remand*, ¶ 30; *see also* id., ¶ 36.

[33] Id., ¶¶ 30, 40-42.

[34] Id., ¶¶ 80-82; *see also* id., ¶¶ 40-42.

[35] Id., ¶¶ 49, 55-69.

In the meantime, the Commission had also added two other forms of "high-cost" support to the HCM given to non-rural carriers. IAS came out of the *CALLS Order*.[36] And ICL support came from the *MAG Order*.[37] These two forms of support substantially increased the number of non-rural ILECs receiving high-cost support, such that only fourteen non-rural ILECs in thirteen states **do not** currently receive any high-cost support.[38]

The *Order on Remand* was also appealed. The Tenth Circuit again reversed and remanded the non-rural high-cost issues to the Commission.[39]

The court held that the Commission had once more failed to reasonably define the terms "sufficient" and "reasonably comparable."[40] The court directed the Commission on remand to articulate a definition of "sufficient" that appropriately considers the full range of principles in § 254(b), and to define "reasonably comparable" in a manner that comports with the Commission's duty to preserve and advance universal service.[41]

Because the non-rural high-cost support mechanism rested on the application of the definition of "reasonably comparable" rates that was invalidated by the court, the court also deemed the support mechanism invalid.[42] The court also noted that the Commission based the two standard deviations **cost** benchmark on a finding that **rates**

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[36] *In the Matter of Access Charge Reform*, CC Docket No 96-262, *et al.*, Sixth Report and Order, 15 FCC Rcd 12962 (2000) ("*CALLS Order*").

[37] *In the Matter of Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, *et al.*, 16 FCC Rcd 19613, Second Report and Order, *et al.*, (2001) ("*MAG Order*").

[38] See Section IV., below.

[39] *Qwest II*, 398 F.3d 1222.

[40] Id. at 1233.

[41] Id. at 1237.

[42] Id.

were reasonably comparable, without empirically demonstrating a relationship between costs and the rates in the record.[43]

The court directed the Commission on remand to "utilize its unique expertise to craft a support mechanism taking into account all the factors that Congress identified in drafting the Act and its statutory obligation to preserve *and* advance universal service."[44] The NPRM is the Commission's attempt to respond to the court's directives.

III. THE ISSUES FOR COMMENT

The Commission seeks "comment on a number of issues that will enable the Commission to craft a non-rural high-cost support mechanism consistent with the court's decision and the statute."[45] The Commission characterized the issues as follows:

> Specifically, we seek comment on: (1) how the Commission should define the statutory term "sufficient" to take into account all the principles enumerated in section 254(b); (2) how the Commission should define "reasonably comparable" under section 254(b)(3), consistent with its concurrent duties to preserve and advance universal service; [and] (3) how, in light of the interpretation of the key statutory terms, the Commission should modify the high-cost funding mechanism for non-rural carriers….[46]

The NPRM sets forth a wide range of "sub-issues" that fit into these three areas. Most of these are addressed here, but not necessarily in the order presented in the NPRM. In

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[43] Id.

[44] Id. (emphasis in original).

[45] NPRM, ¶ 7.

[46] Id. As previously noted, the Commission also asked for comment on PRTC's proposal for a non-rural insular mechanism. NASUCA is limiting these comments to the issues on remand from *Qwest II*.

order to allow the Commission's determinations to be based upon a factual record, however, NASUCA first presents information on the current high-cost funding mechanism for non-rural carriers and then, most importantly, discusses the findings of the national survey of non-rural carrier rates that covers urban and rural areas.

IV. THE CURRENT NON-RURAL CARRIER HIGH-COST FUNDING SITUATION

Appendix A to these comments -- derived from USAC reports and the FCC monitoring report[47] -- lists, by state, the non-rural carriers in each state and shows the amount of high-cost support that each carrier received in 2005 and is projected to receive in the first quarter of 2006 ("1Q06"). This high-cost support includes not only HCM support but also the "high-cost" support that was designed to replace access charge revenues -- that is, IAS and ICL --which has a limited relationship to costs.[48]

Appendix A shows that in 2005, fifteen non-rural companies in ten states received high-cost model funding. On the other hand, non-rural carriers in forty-seven jurisdictions received either interstate access or interstate common line support in 2005, but no HCM support.[49] In the District of Columbia, Idaho, Minnesota, New Jersey, and Wisconsin, non-rural carriers received no high-cost funding. Further, ten non-rural carriers in eight states received no high-cost funding, even though other non-rural carriers in those states did receive such funding. The states, companies, their total 2005 HCM

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[47] Support amounts are from Monitoring Report Tables 3.25, 3.27, 3.28 and 3.30. Line counts are from Monitoring Report Table 3.31.

[48] The *CALLS* universal service support was supposed to have lasted five years (*CALLS Order*, ¶ 198). The five years ended July 1, 2005. The *MAG Order* had no end date for its universal service support.

[49] Of the non-rural ILECs, only ACS in Alaska, SureWest in California, North State in North Carolina, and the Puerto Rico companies received ICL support in 2005.

and other "high-cost" funding, and that funding expressed on per loop per month basis[50]

are:

State	Non-rural carrier(s)	2005 HCM support ($ millions)	2005 IAS/ICL support ($ millions)	2005 total support ($ millions)[51]	Total support / loop / month
Alabama	South Central Bell	25.2	9.9	35.1	$1.65
	CenturyTel (Southern)	5.4	4.0	9.4	$5.14
	CenturyTel (Northern)	8.7	2.0	10.7	$7.23
Alaska	ACS of Anchorage	0	4.6	4.6	$2.53
Arizona	Qwest	0	12.7	12.7	$0.45
Arkansas	Southwestern Bell	0	5.5	5.5	$0.50
California	Verizon (Contel)	0	5.9	5.9	$1.20
	Verizon (GTE)	0	18.9	18.9	$0.40
	SureWest	0	3.7	3.7	$2.38
	Pacific Bell	0	0	0	0
Colorado	Qwest	0	20.2	20.2	$0.68
Connecticut	SNET	0	0.5	0.5	$0.02
DC	Verizon	0	0	0	0
Delaware	Verizon	0	0.3	0.3	$0.04
Florida	Verizon	0	28.1	28.1	$1.10
	Southern Bell	0	10.2	10.2	$0.14
Georgia	Southern Bell	0	15.8	15.8	$0.35
Hawaii	Verizon	0	6.8	6.8	$0.28
Idaho	Qwest	0	0	0	0
Iowa	Qwest	0	0.6	0.6	$0.05
Illinois	Verizon	0	6.8	6.8	$0.93
	Verizon (Contel)	0	3.9	3.9	$2.60
	Illinois Bell	0	0	0	0

[50] In this chart, intended only to give a gauge on the current situation, funding is spread across all of the non-rural carrier's line within the state. Not all of these lines are rural, of course. In Section XIII., below, NASUCA imputes this current support to the non-rural ILECs' rural wire centers that receive support.

[51] Totals may not be exact due to rounding.

State	Non-rural carrier(s)	2005 HCM support ($ millions)	2005 IAS/ICL support ($ millions)	2005 total support ($ millions)	Total support / loop / month
Indiana	Verizon	0	15.7	15.7	$1.80
	Verizon (Contel)	0	5.3	5.3	$2.28
	Indiana Bell	0	0	0	0
Kansas	Southwestern Bell	0	9.6	9.6	$0.39
Kentucky	Cincinnati Bell	0.7	0.2	1.0	$0.39
	South Central Bell	10.4	6.8	17.2	$1.31
	ALLTEL	5.7	9.0	14.7	$2.95
Louisiana	South Central Bell	0	9.6	9.6	$0.39
Maine	Verizon	1.8	0.3	2.1	$0.27
Massachusetts	Verizon	0	1.9	1.9	$0.04
Maryland	Verizon	0	2.3	2.3	$0.05
Michigan	Verizon	0	0.4	0.4	$0.04
	Michigan Bell	0	0	0	0
Minnesota	Qwest	0	0	0	0
Mississippi	South Central Bell	99.7	14.0	113.7	$7.69
Missouri	Southwestern Bell	0	3.5	3.5	$0.12
	CenturyTel (Central)	0	0.8	0.8	$0.76
	CenturyTel (Southwest)	0	2.9	2.9	$1.10
Montana	Qwest	15.9	0.8	16.7	$4.19
Nebraska	ALLTEL[52]	3.9	0	3.9	$1.21
	Qwest	2.8	3.0	5.8	$1.31
North Carolina	Verizon	0	7.5	7.5	$3.34
	North State	0	4.9	4.9	$3.40
	Verizon (Contel)	0	5.0	5.0	$2.92
	Southern Bell	0	10.0	10.0	$0.37
North Dakota	Qwest	0	0.5	0.5	$0.22
Nevada	Central	0	1.5	1.5	$0.15
	Nevada Bell	0	3.9	3.0	$0.88

[52] ALLTEL in Nevada is the only carrier to receive only HCM support and no access support.

State	Non-rural carrier(s)	2005 HCM support ($ millions)	2005 IAS/ICL support ($ millions)	2005 total support ($ millions)	Total support / loop / month
New Hampshire	Verizon	0	1.9	1.9	$0.22
New Jersey	Verizon	0	0	0	0
New Mexico	Qwest	0	4.2	4.2	$0.44
New York	Verizon	0	8.4	8.4	$0.07
	Frontier Rochester	0	0	0	0
Ohio	Verizon	0	8.1	8.1	$0.76
	Cincinnati Bell	0	0	0	0
	Ohio Bell	0	0	0	0
Oklahoma	Southwestern Bell	0	3.8	3.8	$0.23
Oregon	Verizon	0	13.9	13.9	$2.71
	Qwest	0	2.6	2.6	$0.17
Pennsylvania	Verizon North	0	3.4	3.4	$0.53
	Verizon	0	0	0	0
Puerto Rico	PRTC Central	0	9.0	9.0	$4.56
	PRTC	0	58.2	58.2	$4.78
Rhode Island	Verizon		0.06	0.06	$0.01
South Carolina	Verizon	0	6.0	6.0	$3.01
	Southern Bell		5.2	5.2	$0.32
South Dakota	Qwest	1.5	0.1	1.6	$0.67
Tennessee	South Central Bell	0	7.3	7.3	$0.25
Texas	GTE	0	19.2	19.2	$1.12
	Contel	0	3.3	3.3	$2.38
	Southwestern Bell	0	0	0	0
Utah	Qwest	0	1.1	1.1	$1.16
Vermont	Verizon	8.3	2.0	10.3	$2.50
Virginia	Contel	0	38.2	38.2	$5.32
	Verizon	0	11.6	11.6	$0.31
Washington	Verizon	0	15.9	15.9	$1.81
	Contel	0	4.9	4.9	$4.53
	Qwest	0	0	0	0
West Virginia	Verizon	22.6	8.0	30.6	$3.15

State	Non-rural carrier(s)	2005 HCM support ($ millions)	2005 IAS/ICL support ($ millions)	2005 total support ($ millions)	Total support / loop / month
Wisconsin	Verizon	0	0	0	0
	Wisconsin Bell	0	0	0	0
Wyoming	Qwest	9.4	5.2	14.6	$5.10

Appendix B shows this information ranked according to the amount of support received by each ILEC in each state. In total in 2005, there was $222 million in HCM funding, $427 million in IAS funding for non-rural carriers, and $81 million in ICL funding for non-rural carriers, for a total of $730 million.[53]

Under the Commission's current non-rural mechanism, then, these carriers receive a total of $730 million in funds paid by consumers without any actual requirement to show that the funds result in reasonably comparable rates or -- conversely -- that without the funds rates would no longer be reasonably comparable. (The currently-required state certifications[54] that follow the determination of support under the current mechanism do little to provide this assurance.) The mechanism must be fixed so that the statutory connection is made.

[53] To put this into perspective, in the first quarter of 2006 rural carriers received three times as much in high-cost funding. USAC 1Q06 Appx. HC01.

[54] *Order on Remand*, ¶ 89.

V. THE DATA ON URBAN AND RURAL RATES OF NON-RURAL CARRIERS

The Commission invited commenters to submit rate data.[55] NASUCA does so, comprehensively, in Appendix C.

The first piece of the puzzle in comparing urban and rural rates is to define "urban" and "rural." The second piece is defining "rates."

In determining high-cost funding, the Commission currently looks at only part of the national picture: The current rate benchmark is based on an annual survey of rates in 95 "urban" areas, as reported in the annual *Reference Book of Rates, Price Indices, and Household Expenditures* ("*Reference Book*").[56] The most recent result of the survey (rates as of October 15, 2004) is a weighted average monthly urban residential charge of $24.31,[57] with a low of $16.05 and a high of $34.47.[58] "Rates," as evaluated in that survey, includes the monthly rate for residential flat-rate service; federal and state SLCs; the federal USF ("FUSF") assessments on the SLCs; and taxes, 911 and other charges, assessed by the ILEC.[59]

For its initial rate comparison, NASUCA adopts a somewhat more limited definition, that includes the monthly rate for residential flat-rate service, the SLC, and the

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[55] NPRM, ¶ 18.

[56] *Order on Remand*, ¶ 80.

[57] *Reference Book*, Table 1.13.

[58] Id., Table 1.3.

[59] Id., Table 1.1. NASUCA's proposal focuses on residential service, and provides support for residential rates.

FUSF assessment on the SLC.[60] Charges for 9-1-1, taxes and other surcharges do not appear to be available on a wire center basis. On a national level, however, these represent an average of $3.97 per month.[61] This should not significantly impact the results, given that NASUCA's rate comparison is apples-to-apples, rate-plus-SLC-plus-FUSF to rate-plus-SLC-plus-FUSF.[62]

As to the urban/rural distinction, it is important to recognize how the terms are used by the Commission *in the context of the non-rural high-cost fund*. The Commission's rules define "rural areas" in this context, but only as a consideration for the states.[63] NASUCA submits that the definition is inadequate for this purpose.

By contrast, the Commission's definition of "urban" is encompassed by the 95 "urban" areas used for the FCC's determination of the national average urban rate. The 95 areas were a sample used by the Bureau of Labor Statistics ("BLS") in the calculation of the consumer price index in 1986.[64] This "definition" also has its limitations.

NASUCA submits that the Commission should follow the U.S. Census Bureau

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[60] The sources for the rate numbers are found in Appendix C. It should be noted that for some states -- Vermont, Connecticut and Pennsylvania in particular -- some assumptions were made in assigning rates to wire centers. Even in the state-specific analysis, changing the assumption would not have a significant impact. Further, given that Puerto Rico is seeking its own insular high-cost mechanism, it is not included in this national data. It must be noted at this point that, given the volume of the data and the time allotted to prepare this review, there are a few gaps in the data. NASUCA intends to present the Commission with the complete dataset when it is complete.

[61] *Reference Book*, Table 1.2.

[62] In addition, many of the taxes and surcharges are state-specific, and should be supported through state -- not national --efforts. In Richmond, Virginia, for example, state taxes total $6.89 and the 9-1-1 charge is $3.00, both substantially higher than such charges elsewhere. See http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/ratesrvy03-04.zip.

[63] 47 C.F.R. § 316(c); see also 47 C.F.R. §§ 54.5, 54.316(c), and 54.505(b)(3)(ii), which contain more detailed definitions.

[64] *Reference Book*, page I-2. It is not clear whether these 95 urban areas selected in 1986 remain the best sampling some twenty years later, but that does not appear to make much difference.

definitions. The Census Bureau defines "urban" as follows:

> **Urban -** All territory, population and housing units in urban areas, which include urbanized areas and urban clusters. An urban area generally consists of a large central place and adjacent densely settled census blocks that together have a total population of at least 2,500 for urban clusters, or at least 50,000 for urbanized areas. Urban classification cuts across other hierarchies and can be in metropolitan or non-metropolitan areas.[65]

Rural is defined by the Census Bureau in the negative, being "territory, population and housing units not classified as urban."[66]

The distinction between urban and rural is also discussed on the website of the Economic Research Service ("ERS") of the U.S. Department of Agriculture:

> According to official U.S. Census Bureau definitions, rural areas comprise open country and settlements with fewer than 2,500 residents. Urban areas comprise larger places and densely settled areas around them. Urban areas do not necessarily follow municipal boundaries. They are essentially densely settled territory as it might appear from the air. Most counties, whether metropolitan or nonmetropolitan, contain a combination of urban and rural populations.
>
> Urban areas are of two types -- **urbanized areas** and **urban clusters --** identical in the criteria used to delineate them but different in size. The Census Bureau defines an urbanized area wherever it finds an urban nucleus of 50,000 or more people. They may or may not contain any individual cities of 50,000 or more (152 currently do not). In general, they must have a core with a population density of 1,000 persons per square mile and may contain adjoining territory with at least 500 persons per square mile. Urbanized areas have been delineated using the same basic threshold (50,000 population) for each decennial census since 1950, but procedures for delineating the urban fringe are more

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[65] http://ask.census.gov/cgi-bin/askcensus.cfg/php/enduser/std_adp.php?p_faqid=623&p_created=1092150238&p_sid=RK3ozT1i&p_lva=&p_sp=cF9zcmNoPTEmcF9zb3J0X2J5PSZwX2dyaWRzb3J0PSZwX3Jvd19jbnQ9NTEmcF9wcm9kcz0mcF9jYXRzPSZwX3B2PSZwX2N2PSZwX3BhZ2U9MSZwX3NlYXJjaF90ZXh0PXVyYmFuIGRlZmluaXRpb24*&p_li=&p_topview=1 (accessed March 7, 2006).

[66] Id.

> liberal today. In 2000, 68 percent of Americans lived in 452 urbanized areas.
>
> The same computerized procedures and population density criteria are used to identify urban clusters of at least 2,500 but less than 50,000 persons. This delineation of built-up territory around small towns and cities is new for the 2000 census. In 2000, 11 percent of the U.S. population lived in 3,158 urban clusters.
>
> According to this system, rural areas consist of all territory located outside of urbanized areas and urban clusters. The U.S. rural population was 59 million (21 percent) in 2000.[67]

The key information in the ERS' discussion can be displayed as follows:

	Number	2000 Population	% of Population
Urbanized areas	452	191 million	68%
Urban clusters	3,158	31 million	11%
Rural areas	N/A	59 million	21%
TOTAL		281 million	100%

As used by the Census Bureau and noted by the ERS, areas are either rural or urban, with nothing in between. For our rate comparison purposes here, however, it is possible to recognize "rural" wire centers as those serving no population classified as urban ("0% urban") and urban wire centers as those serving entirely urban areas ("100% urban"), recognizing that there are many areas that lie between.

This is shown by the wire center data:

[67] http://www.ers.usda.gov/Briefing/Rurality/WhatisRural/ (emphasis in original) (accessed February 5, 2006).

Percent of the population living in urban areas	Number of Wire Centers	Average Population	Total population[68]	Percent of total population[69]
0%	1,808	2,611	4,721,471	1.8%
0-20%	3,979	3,332	13,259,982	5.1%
20-40%	545	10,295	5,610,606	2.1%
40-60%	1057	12,291	12,991,492	5.0%
60-80%	1,393	16,876	23,507,836	9.0%
80-100%	4,278	48,134	205,915,241	78.8%
100%	1092	58,861	64,275,873	24.6%
Sample avg. (0-100%)	11,252	23,221	261,285,167	100.0%

It is crucial to remember at this juncture that "urban" and "rural" are defined here for very different purposes. "Urban" is used to determine the average urban revenue, in NASUCA's first proposal, or the urban average rate, in NASUCA's second proposal. Therefore, it is reasonable to use wire centers that are 100% urban according to the Census Bureau. This does not mean that the rest of the wire centers (some 10,160 of them) are all "rural." Likewise, "rural" is used here as designating areas that may need support. Using the 0% urban to 20% urban range makes 35% of the wire centers in the

[68] Recall that this is the total population served by non-rural carriers and thus does not include the population served by rural carriers.

[69] The 0 and 100 % urban row values are included in the 0-20% and 80-100% rows, respectively.

country eligible, serving 5.1% of the population. Importantly, this does not make the rest of the wire centers (65%) "urban."

Another view would take the 21% rural population of the country and assume that 21% of the nation's 169 million working loops[70] -- or 35.5 million -- are rural. It is safe to assume that most of the 23.5 million working loops served by rural carriers[71] are in rural territory. If that is 20 million, then 15.5 million rural lines are served by non-rural carriers.[72] That would fall into the 20-40% urban quintile in the chart, and mean that 7.2% of the non-rural companies' population is served by these lines.

As discussed below, NASUCA's samplings took all the wire centers that are 0% urban, and those that are 100% urban, according to the Census Bureau.[73] NASUCA also sampled wire centers that were up to 20% urban (not entirely rural, but close). NASUCA also looked at wire centers that were more than 80% urban (not entirely urban, but close). The sampling is shown graphically on the maps on the next two pages. The first map shows the territory that is 0-20% urban and the territory that is 80-100% urban. The second map shows the territory that is 0% urban and the territory that is 100% urban.

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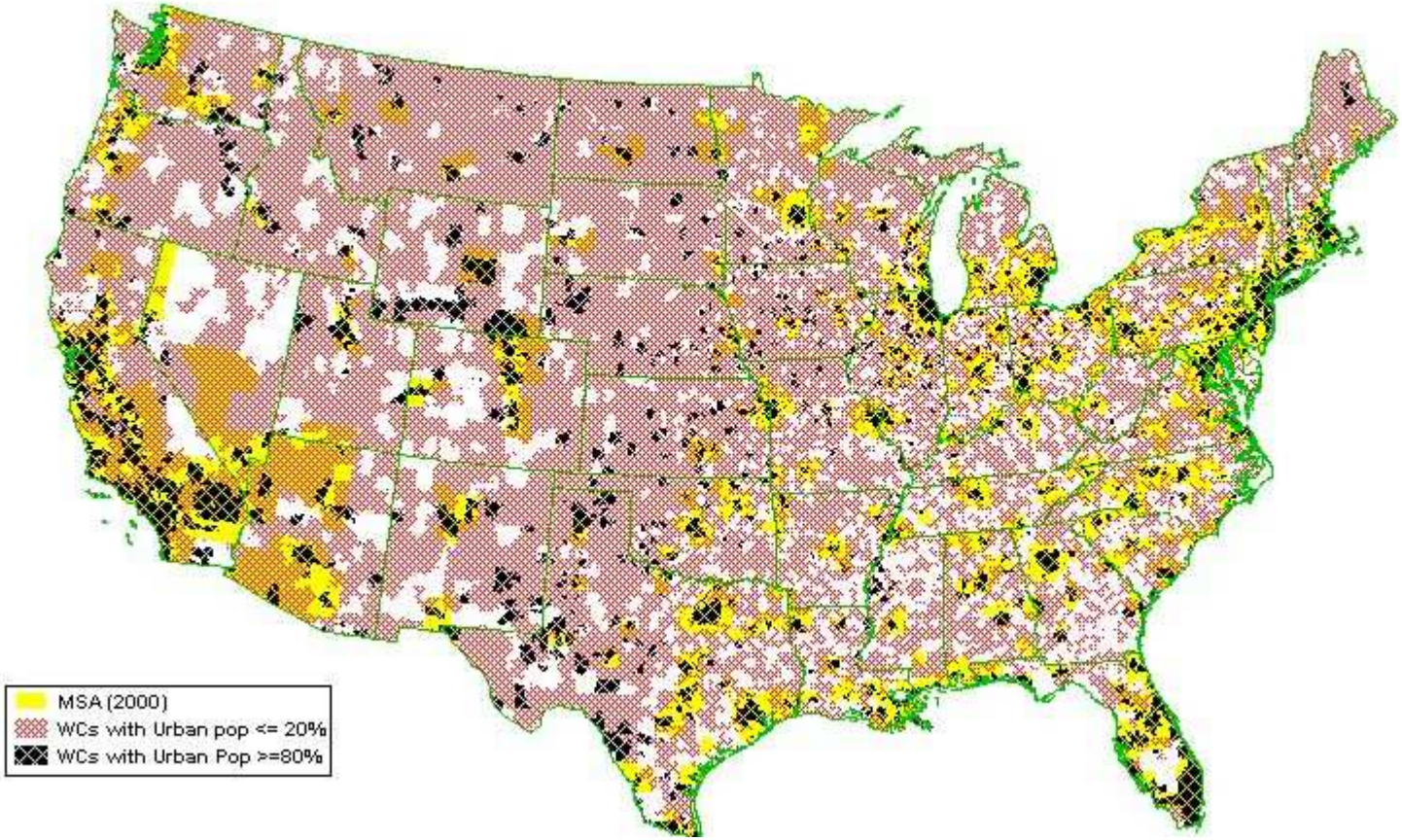
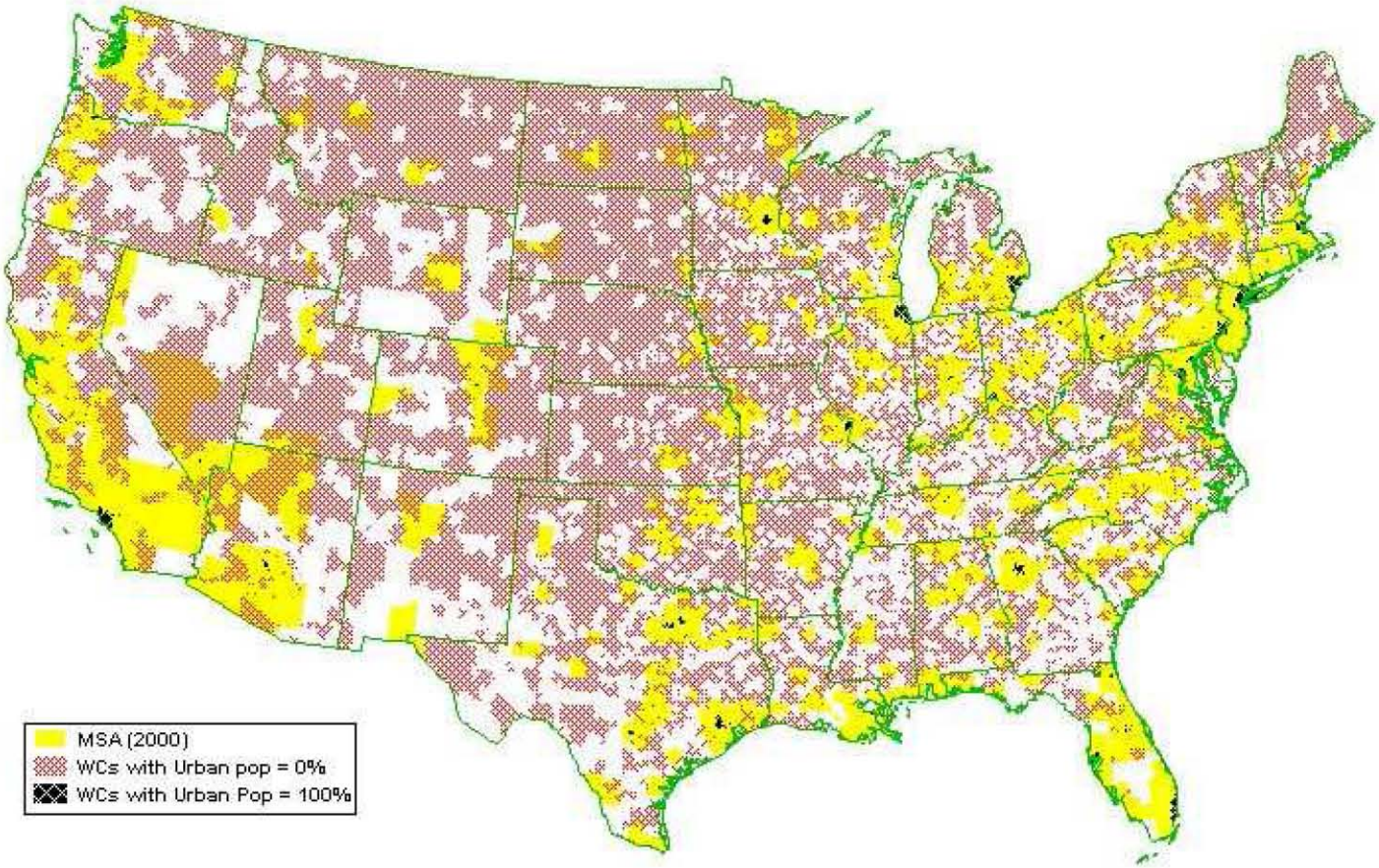
[70] USAC 1Q06 Appx. HC05.

[71] Id.

[72] I.e., 35.5 - 20.0 = 15.5.

[73] As mentioned, this material is presented in Appendix C and more extensively discussed in Section VII.


MSA (2000)
WCs with Urban pop <= 20%
WCs with Urban Pop >=80%


MSA (2000)
WCs with Urban pop = 0%
WCs with Urban Pop = 100%

It should be recalled that these maps use the Census Bureau definitions, which include "urban clusters" (i.e., areas "of at least 2,500 but less than 50,000 persons"[74]) as urban. The inclusion of "built-up territory around small towns and cities"[75] is the cause of "urbanity" in what may appear to counterintuitive areas.

The data presented by NASUCA -- based on the Census Bureau definitions -- gives the Commission its most complete gathering to date of rates for non-rural carriers. The urban data shows the relative validity of the current 95-urban area sample; given its simplicity and history the Commission may decide to continue using it. As discussed above, the Commission's sampling yields a weighted average monthly urban residential charge of $24.31, with a low of $16.05 and a high of $34.47. NASUCA's urban sample has an average of $19.57, with a low of $9.29 and a high of $31.82. With $3.97 in other fees added in, the average becomes $23.54, the low $13.26, and the high $33.64.

As to rural rates charged by non-rural ILECs, however, NASUCA's data provides detailed information that the Commission has never examined before. This information is vital to establishing a universal service fund that "preserves and advances" the principle that rural rates should be "reasonably comparable" to urban rates.

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[74] See footnote 67, supra.

[75] Id.

VI. "REASONABLE COMPARABILITY" OF RATES IS THE KEY STATUTORY PRINCIPLE FOR JUDGING THE SUFFICIENCY OF HIGH-COST UNIVERSAL SERVICE SUPPORT FOR NON-RURAL CARRIERS.

A. Introduction

The *Qwest II* court based its remand of the *Order on Remand* on the fact that the Commission had considered only reasonable comparability, out of the six principles in § 254 of the 1996 Act, in determining the sufficiency of the non-rural high cost fund.[76] The Commission's failure to even discuss the other principles doomed the *Order on Remand*.

The court indicated, however, that the Commission would have considerable leeway in considering each of the principles, stating, "The FCC may exercise its discretion to balance the principles against one another when they conflict, but may not depart from them altogether to achieve some other goal."[77] *Qwest I* had stated that the Commission "must work to achieve each [principle] unless there is a direct conflict between it and either another listed principle or some other obligation or limitation on the FCC's authority."[78] NASUCA submits that when the Commission does its review here, it will still find reasonable comparability to be the most important and most effective principle. This requires no departure from the principles and no abandonment of any of the principles.

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[76] *Qwest II*, 398 F.3d at 1234.

[77] Id., citing *Qwest I*, 258 F.3d at 1200.

[78] *Qwest I*, 258 F.3d at 1199.

Section 254(b) of the Act states that the Commission and Joint Board "shall base policies for the preservation and advancement of universal service" on the following principles:

> (1) Quality and rates. Quality services should be available at just, reasonable, and affordable rates.
>
> (2) Access to advanced services. Access to advanced telecommunications and information services should be provided in all regions of the Nation.
>
> (3) 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.
>
> (4) Equitable and nondiscriminatory contributions. All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.
>
> (5) Specific and predictable support mechanisms. There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.
>
> (6) Access to advanced telecommunications services for schools, health care, and libraries. Elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services as described in subsection (h).[79]

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[79] 47 U.S.C. § 254(b)(1)-(6). In addition, 47 U.S.C. § 254(b)(7) allows the Commission to adopt additional principles. Pursuant to this authority the Commission adopted a principle of competitive neutrality. *First Report and Order*, ¶ 47.

It should be noted that when the *Qwest I* court discussed § 254(b), it mentioned only (b)(3) and (b)(5).[80] Even *Qwest II* first discussed only (b)(1), (b)(3) and b(5).[81]

Qwest I had noted that, although § 254(b) directs that the Commission "shall" consider the principles,

> each of the principles in § 254(b) internally is phrased in terms of "should." "The term 'should' indicates a recommended course of action, but does not itself imply the obligation associated with 'shall.'"[82]

The Commission seeks comment on how to balance the principles.[83] NASUCA submits its views below.

B. Reasonable comparability

Reasonable comparability of rates is the only one of the principles that is both relevant to this issue and capable of a resolution at the federal level. "Reasonable comparability," on the national level, can only be evaluated, preserved and advanced by this Commission.

Reasonable comparability is a standard that is capable of objective review and determination, as is accomplished by NASUCA through review of rate data for more than 11,000 wire centers nationwide, which includes 1,808 wire centers that are 0% urban according to Census Bureau criteria and 1,092 wire centers that are 100% urban according to those same criteria. Despite the disparity in the number of wire centers, the rural wire centers serve only 1.8% of the population while the urban wire centers serve

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[80] *Qwest I*, 258 F.3d at 1199.

[81] *Qwest II*, 398 F.3d at 1226-1227.

[82] *Qwest I*, 258 F.3d at 1200 (citation omitted).

[83] NPRM, ¶ 8.

24.6%. This leaves 74.6% "in the middle."[84] This wire center-by-wire center review can be contrasted with a review of affordability, which would have to occur on a customer-by-customer basis, as discussed in the next section.

The Tenth Circuit did not reject the Commission's reliance on reasonable comparability, or its mechanism; rather the court objected to the Commission's failure to address the other principles, and found the Commission's specific benchmarks to be arbitrary. NASUCA's comments are designed to give the Commission the basis to address both of the court's objections.

C. Affordability

The Tenth Circuit allowed that the Commission could make one principle subsidiary to another, as long as it considered all the principles.[85] The principle of affordability should be subsidiary to the principle of reasonable comparability, for a number of reasons.[86]

First, the Commission has found that "section 254(b)(3) reflects a legislative judgment that all Americans, regardless of income, should have access to the network at reasonably comparable rates."[87] If affordability is the primary standard, as some have argued,[88] then in high-income rural areas, rates will not be reasonably comparable to

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[84] When the definition of "rural" is expanded to include wire centers that are up to 20% urban, the range and average do not materially change. The same is true when "urban" includes wire centers that are 80%-100% urban..

[85] *Qwest II*, 398 F.3d at 1234.

[86] The Commission should not make the affordability of universal service assessments a measure of the sufficiency (NPRM, ¶ 11); the fund will be sufficient well before USF contributions would become unaffordable. On the other hand, it would be unreasonable to allow USF contributions to increase merely because the increased amount was affordable.

[87] CC Docket No. 96-45, Seventh Report and Order and Thirteenth Order on Reconsideration, FCC 99-119, 14 FCC Rcd 8078 (1999) ("*Seventh Report and Order*"), ¶ 39; *see also Order on Remand*, ¶ 45.

[88] NPRM, ¶ 10, citing SBC's arguments.

urban rates. On the other hand, given the current level of urban rates, rural rates that are reasonably comparable to urban rates are likely to be affordable.

For low-income consumers who might find local service rates unaffordable, the Commission has created the Lifeline and Link-up programs. The Commission previously determined that it was better to address affordability issues unique to low-income consumers through the federal low-income programs specifically designed for this purpose rather than through the high-cost support programs.[89] *Qwest II* does not undermine that conclusion at all.

There may be some consumers with incomes above the eligibility standards for Lifeline who nonetheless may find local service unaffordable. Perhaps the Commission should investigate this issue.

In any event, one thing that would not enhance the affordability of service, that would neither preserve nor advance universal service, would be to adopt an affordability standard like that proposed by SBC. SBC's proposal was "to adopt an affordability benchmark for local telephone service … based on the median household income of a particular geographic area."[90] The Commission correctly rejected the proposal.

The median household income of a wire center is "[t]he middle value in a distribution, above and below which lie an equal number of values."[91] Thus in a particular wire center, half of the population will have incomes above the median, and half will have incomes below. Failure to support service in high-median-income areas

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[89] *See Seventh Report and Order*, ¶ 39; *First Report and Order*, ¶ 124.

[90] *Order on Remand*, ¶ 45.

[91] http://dictionary.reference.com/search?q=median (accessed February 23, 2005).

will disadvantage many consumers with incomes below the median.

Affordability cannot take precedence over reasonable comparability. As discussed above, achieving reasonable comparability also advances affordability. Unfortunately, the reverse is not necessarily true.

D. The other statutory principles

As noted above, the *Qwest II* court indicated that the Commission would have considerable leeway in considering each of the principles, stating: "The FCC may exercise its discretion to balance the principles against one another when they conflict, but may not depart from them altogether to achieve some other goal."[92] *Qwest I* had stated that the Commission "must work to achieve each one unless there is a direct conflict between it and either another listed principle or some other obligation or limitation on the FCC's authority."[93]

It can easily be seen that the principles other than 254(b)(3) cannot and should not overwhelm the need for reasonable comparability. Taking them one by one:

Section 254(b)(1) calls for rates for "quality" service to be just and reasonable, in addition to being affordable. Here the primary responsibility lies with the states, which have a multitude of standards by which to judge service quality, and to judge the justness and reasonableness of rates.[94] It is also fair to say that there are real limitations on the Commission's authority in this area.

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[92] Id., citing *Qwest I*, 258 F.3d at 1200.

[93] See *Ninth Report and Order*, ¶ 37; *Qwest I*, 258 F.3d at 1200.

[94] *See Order on Remand*, ¶ 47 (rejecting NASUCA proposal to consider service quality and finding that states are in the best position to address service quality issues and will have ample opportunity to do so in the rate review and expanded certification process).

Section 254(b)(2) provides that "[a]ccess to advanced telecommunications and information services should be provided in all regions of the Nation." The Commission has done much to promote consumers' access to these services, consistent with this principle and 47 U.S.C. § 706. But the Commission cannot provide support for advanced services at this point because they have not been found to meet the test for support in 47 U.S.C. § 254(c)(1). As discussed in Section IX., below, however, the support that the high-cost fund gives to multiple-use rural networks not only enhances access to basic service but makes it more feasible for non-rural carriers to provide advanced services.

Section 254(b)(4) provides for equitable and nondiscriminatory contribution to the USF. The method of contribution has little to do with the actual needs of the fund, so this principle is basically irrelevant for determining what the support should be used for or whether the fund is sufficient.[95]

Section 254(b)(5) provides that "[t]here should be specific, predictable, and sufficient Federal and state mechanisms to preserve and advance universal service." The Tenth Circuit rejected the Commission's definition of "sufficient" (as found in § 254(e)) because it did not consider all of the statutory policies.[96] There is no reason why "sufficient" in § 254(b)(5) should be viewed any differently. Further, NASUCA submits that the Commission can find the proposals set forth in Section XII. and XIII., below, to be both specific and predictable.

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[95] As the Commission notes, the *Qwest II* court rejected the carriers' arguments that Section 254 -- in any of its parts -- requires the elimination of implicit state support. NPRM, ¶ 14, citing *Qwest II*, 398 F.3d at 1233.

[96] *Qwest II*, 398 F.3d at 1233-1234. The Court found that the state inducement mechanism created in the Order on Remand adequately addressed the need for state mechanisms, as indicated in § (b)(5). Id. at 1238.

Section 254(b)(6) provides for access to advanced telecommunications services "as described in subsection (h)" for elementary and secondary schools and classrooms, health care providers, and libraries. As the Commission notes, it has established separate programs to accomplish this goal.[97] Further, as mentioned above, the support that the high-cost fund gives to multiple-use rural networks makes it more feasible for non-rural carriers to provide advanced services to schools, libraries, and health care providers, among others, in rural areas.

Finally, **Section 254(b)(7)** provides that the Joint Board and the Commission may adopt additional principles that "are necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with [the 1996 Act]." The Commission established "competitive neutrality" as an additional principle upon which to base policies for the preservation and advancement of universal service.[98] As discussed in Section IX.C. below, if the Commission properly refocuses the non-rural high-cost mechanism on reasonably comparable rates for reasonably comparable services, and then applies that focus consistently to competitive carriers, the "universal service support mechanisms and rules [will] neither unfairly advantage nor disadvantage one provider over another, and neither unfairly favor nor disfavor one technology over another."[99] But overall, competitive neutrality does not really address whether non-rural high-cost support is sufficient; to that extent, the Commission's additional principle does not need to be considered in the same context as the other statutory principles.

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[97] NPRM, ¶ 16.

[98] *See First Report and Order*, ¶ 47.

[99] Id.

The Tenth Circuit did not direct any particular result from the Commission's consideration of these principles, nor did it require any particular weight to be given one principle or another. The discussion here should guide the Commission to considering all of the principles in their proper context; that consideration should be made explicit and obvious in the next order. In the end, however, NASUCA submits that the Commission will come to the conclusion set forth here: reasonable comparability is the principle that should be most prominent in fashioning a mechanism to "preserve and advance" universal service in rural areas served by non-rural carriers.

VII. WHAT ARE "REASONABLY COMPARABLE" RURAL RATES?

The rate data submitted by NASUCA should be sufficient to allow the Commission to determine which rural rates are not reasonably comparable to urban rates, and thus should be supported by the FUSF. NASUCA has not yet developed a proposed standard in this regard, however.

In order to arrive at a proper definition of "reasonably comparable," however, the views of the Tenth Circuit in its two rejections of the definition must be considered. Indeed, it might be easier to approach a definition by reviewing what the Tenth Circuit said about what makes rates **not** reasonably comparable.[100] Of course, part of the problem with the Tenth Circuit's analysis was that it was based, perforce, on the Commission's **lack** of rural rate analysis.

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[100] In the NPRM, the Commission asks, "Should the Commission compare rural rates to a national average urban rate, rather than some benchmark above the average?" NPRM, ¶ 20, citing *Qwest II*, 398 F.3d at 1237. This is a distinction without a difference: for example, whether to support rates above a benchmark set at 150% of the urban average, or to support rates that exceed 150% of the urban average benchmark.

Qwest I rejected the Commission's first definition of "reasonably comparable," which was "a fair range of urban/rural rates both within a state's borders, and among states nationwide."[101] That "fair" range triggered a standard that supported only areas where **costs** were 135% of the national urban cost.[102]

In *Qwest I*, the court's key criticism was that the FCC had picked the 135% number without reviewing any actual rates. Despite parties having submitted rate data, the court complained, "There is no record of the FCC's evaluation of this data; it apparently adopted the benchmark without explicit empirical findings in this regard."[103] NASUCA urges the Commission not to commit that error again.

To make matters worse, the *Qwest I* court found that the Commission's selection of the 135% was arbitrary. The court stated,

> The FCC is not a mediator whose job is to pick the "midpoint" of a range or to come to a "reasonable compromise" among competing positions. As an expert agency, its job is to make rational and informed decisions on the record before it in order to achieve the principles set by Congress. Merely identifying some range and then picking a compromise figure is not rational decision-making.[104]

The *Qwest I* court did say that it would likely have supported the 135% benchmark if "the FCC's 135% benchmark [had] actually produced urban and rural rates that were reasonably comparable, however those terms are defined…."[105] In *Qwest I*, the court sympathized with Vermont and Montana, however, which had asserted that some rural

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[101] *Qwest I*, 258 F.3d at 1201, citing *Ninth Report and Order*, ¶ 54, n.8.

[102] *Qwest I*, 258 F.3d at 1197.

[103] Id. at 1202.

[104] Id. at 1203.

[105] Id.

rates would be 70-80% higher than urban rates under the funding mechanism set out in the *Ninth Report and Order*.[106] The court stated, "We doubt that the statutory principle of 'reasonable comparability' can be stretched that far."[107] It is not clear, however, *which* urban rates were being referred to by the court.

The *Qwest II* court noted that in the *Order on Remand*,

> the FCC … found it reasonable to assume that Congress was aware of the variance in urban rates at the time, on the basis of then available WCB survey information, and that Congress would not have required rural rates to be any closer to a national urban average than other urban rates. Underlying this assumption is the FCC's determination that Congress considered rural and urban rates reasonably comparable in 1996.[108]

In response to the *Qwest I* remand, "[t]he Commission then defined 'reasonably comparable' in terms of a national urban rate benchmark, i.e., rural rates are deemed reasonably comparable if they fall within two standard deviations, or roughly 138%, of the national urban average."[109] The court reviewed the rates allowed under the "two standard deviations" benchmark, however, and found that the benchmark did not meet the Commission's duty to advance universal service.[110]

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[106] *Qwest I*, 258 F.3d at 1201.

[107] Id.

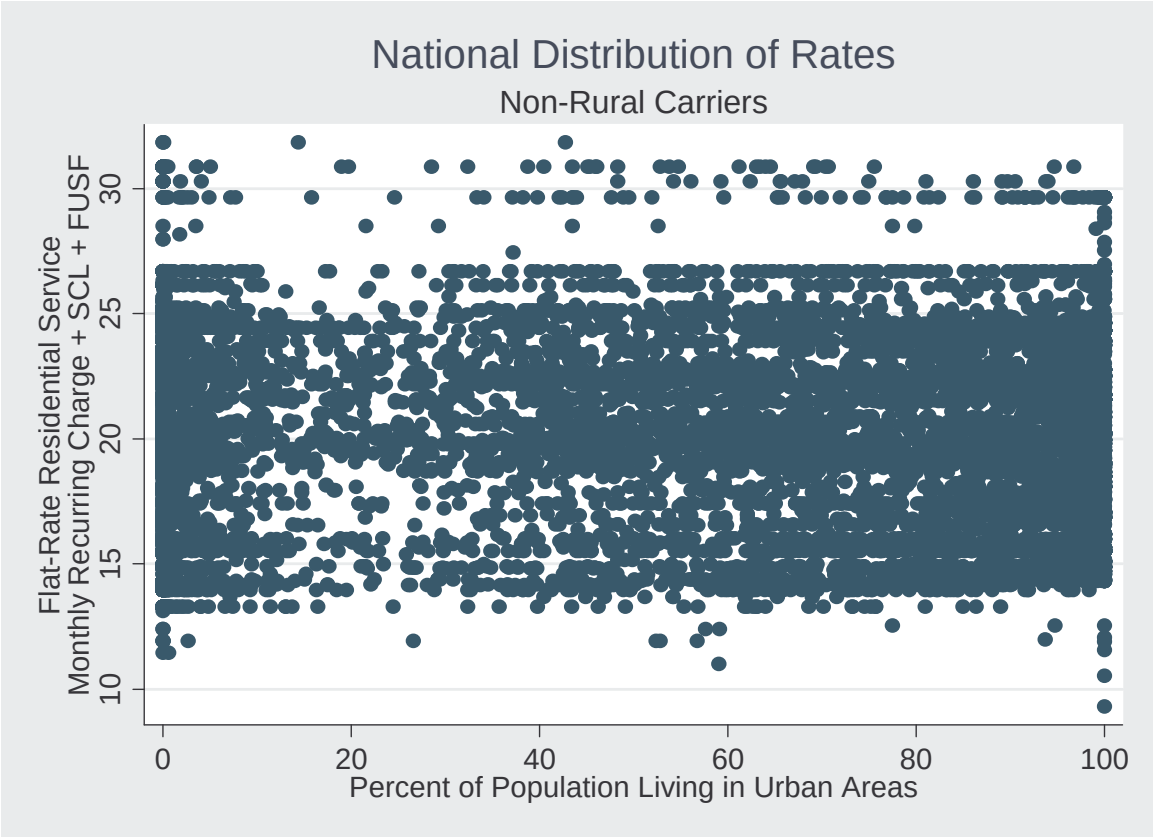
[108] *Qwest II*, 398 F.3d at 1235, citing *Order on Remand*, ¶¶ 39-40.

[109] *Qwest II*, 398 F.3d at 1228, citing *Order on Remand*, ¶ 38. Also in the Court's words, "A standard deviation is a statistical term representing the difference between input values in a range and the mean or average. One standard deviation encompasses 68.27% of the values in a given range. Two standard deviations encompasses 95.45% of the same values. In a hypothetical survey of 100 varying rates charged by telecommunications carriers, two standard deviations from the mean will encompass nearly 96 of the rates in the range, leaving roughly 4 rates outside the grouping." Id. at 1228, n.2. It should be noted that the "4 rates outside the grouping" include two that are below the mean and two rates at the high end. Thus under the FCC's analysis, only two rates out of the hundred would be deemed high enough not to be reasonably comparable to the mean.

[110] Id. at 1236-1237 (internal citations omitted).

It certainly appears that if a two standard deviation benchmark had been shown to preserve and advance universal service, the Tenth Circuit would have approved its use. It is clear that the Commission's prior lack of consideration of statutory principles and language doomed the prior reasonable comparability standards. The Commission must now look at the data and follow the dictates of the statute.

To assist the Commission, NASUCA presents a rate census that includes over 11,000 wire centers.[111] The variety of rates charged by non-rural carriers is depicted in the following scatter diagram:



The following chart simplifies the many points on the scatter diagram:

[111] See Appendix C.

Percent of wire center population living in urban areas	Number of Wire Centers	Average price of flat-rate residential service + SLC + FUSF	Standard deviation	Minimum	Maximum
0%	1,808	21.00	3.79	11.43	31.82
0-20%	3,979	20.81	3.76	11.43	31.82
20-40%	545	20.47	3.56	11.91	30.86
40-60%	1057	20.42	3.72	10.99	31.82
60-80%	1,393	20.34	3.71	12.54	30.86
80-100%	4,278	19.40	3.86	9.29	30.86
100%	1092	19.57	4.20	9.29	29.64
Sample avg. (0-100%)	11,252	19.63	3.85	9.29	31.82

The data show that there is not that much difference between current rural rates and current urban rates. The rural minimum rate is 23% greater than the urban minimum rate, but the average rural rate is only 7% greater than the average urban rate. Most importantly, the highest rural rate is only 7% higher than the highest urban rate. Further, there are only about 245 wire centers that have current rates greater than two standard deviations above the urban average.[112] Most of these are rural, but some are urban. On the other hand, there are fifteen jurisdictions where no non-rural carrier rate is greater than one standard deviation from the urban average.[113] **The extent to which the current**

[112] They are served by Cincinnati Bell in Kentucky, Verizon in Vermont, Qwest in Wyoming, Verizon in New York, CenturyTel in Alabama, and BellSouth in Georgia.

[113] Alaska, Arizona, Delaware, District of Columbia, Florida, Iowa, Louisiana, New Jersey, Nevada, Oregon, Pennsylvania, Tennessee, Texas, Utah and Washington. Of course, local calling areas do not figure in to this comparison.

comparability of rates has occurred as a result of the Commission's current non-rural high-cost mechanism is, of course, uncertain.

The data suggest that little beyond the level of support currently awarded is necessary to maintain this level of comparability. As discussed in Section XIV.C., below, however, there does not appear to be any correlation between the level of support received and the degree of comparability. That correlation is provided by both of NASUCA's proposed alternatives.

Looked at from another direction, the highest urban rate is 151% of the urban average and the highest urban rate is only 8.7% higher than a rate two standard deviations above the average ($27.27). It seems clear that the Tenth Circuit's view of reasonable comparability was overly constricted -- due to the Commission's failure to have assessed a complete record -- especially because following such a view would require support for rural rates that are **below** the highest urban rate.

The Tenth Circuit compared high rural rates allowed under the previous support mechanisms to the lowest urban rates, finding the difference disturbing.[114] Yet NASUCA's survey shows that the highest urban rates are not even reasonably comparable to the lowest urban rates, under any of the views of the Tenth Circuit.

The existence of these ranges -- which, as previously noted, the Commission correctly assessed were within Congress' contemplation in putting together the 1996 Act[115] -- argues strongly for the use of the weighted average urban rate as the starting point for any rate benchmark. There was no indication that Congress intended the

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[114] Id. at 1237, citing *Qwest I*, 258 F.3d at 1201.

[115] *Order on Remand*, ¶¶ 39-40.

comparison to be to the lowest urban rates; if so, there would be support for a multitude of rural customers without any support for urban customers paying the same -- or higher --rates.

It would appear that if all rural rates were lowered to be no higher than the highest urban rate, then there would be no significant difference between urban and rural rates. Certainly that action would lower the rural average rate to be even closer to the urban average. It could be argued, however, that this would result in rural rates being **equal** to urban rates, which does not appear to comport with Congress' use of the term "reasonably comparable," rather than "equal," in § 254(b)(3). Therefore, it would seem appropriate to adopt some range above the highest urban rate that would still enable rural rates to be "reasonably comparable" to urban rates. On the other hand, moving toward equality would certainly be "advancing" universal service.

A typical dictionary defines "comparable" as:

> 1 Admitting of comparison with another or others: "The satellite revolution is comparable to Gutenberg's invention of movable type" (Irvin Molotsky).
>
> 2. Similar or equivalent: pianists of comparable ability.[116]

"Comparable" does not mean "equal." If Congress had intended rural rates to be equal to urban rates, the 1996 Act would have said so. Congress even added the qualifier, "reasonably," so that rural rates were supposed to be only "reasonably comparable" to urban rates.

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[116] The American Heritage® Dictionary of the English Language, Fourth Edition (2000), accessed at http://dictionary.reference.com/search?q=comparable on February 20, 2006.

As noted, Congress was generally aware of the range of rates in 1996.[117] So was the Commission in the *Ninth Report and Order* and the *Order on Remand*. Yet the Commission did not review a comprehensive database of urban and rural rates before establishing the benchmark. (And, according to *Qwest I*, the Commission did not address any of the data it had apart from the 95-city urban rate sample.[118])

NASUCA submits that its database is comprehensive. The Commission should use the database to determine what is reasonably comparable.

These data show that the range of urban rates is $6.75 to $19.26, with a weighted average of $12.76. With this information in hand, it is unreasonable to give any relevance to the lowest urban rates without considering the range of rates as it existed when the Act was passed.[119] Unfortunately, it appears that this is what the Tenth Circuit did, based on the record before it.

A review of NASUCA's database shows as follows:

Standard deviation of rural rates from rural average	Rate	Rural rate as % of rural average	Rural rate as % of urban average
0	21.00	100%	107%
1	24.79	118%	127%
2	27.27	130%	139%
3	32.37	154%	165%

It would appear, however, that the Tenth Circuit might prefer the issue to be looked at as follows:

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[117] The legislative history, however, does not contain reference to a rate study.

[118] Qwest I, 258 F.3d at 1202.

[119] The Commission asks, "How should the Commission interpret the *Qwest II* court's rejection of the Commission's reliance on the range of urban rates?" NPRM, ¶ 20. As explained above, that is not an accurate description of the Tenth Circuit's holdings.

Percentages of rural (0-20% urban) average ($20.81)	Rural rate	Rural rate as % of urban average: $19.40	**Rural = 0% urban** Estimated number of lines "needing support" (i.e., above, e.g., 120% of rural average)[120]	**Rural = 0-20% urban** Estimated number of lines "needing support" (i.e., above, e.g., 120% of rural average)	**Rural = 0-40% urban** Estimated number of lines "needing support" (i.e., above, e.g., 120% of rural average)
(1)	(2) = $20.81 * (1)	(3) = (2) / $19.40			
120%	$24.97	128%	261,546	674,858	889,571
125%	$26.01	133%	139,487	381,345	515,511
133%	$27.68	142%	52,376	132,227	185,414
140%	$29.13	149%	50,709	126,511	171,157
150%	$31.22	160%	2,899	13,694	13,694
166%	$34.54	177%	0	0	0

Thus with a rural average of $20.81, 125% of the average is $26.01. If "rural" is defined as 0% urban, there are about 140,000 rural lines served by non-rural carriers that would be eligible for support, i.e., that have rates above $26.01. Likewise, 140% of the rural average is $29.13. If "rural" includes wire centers that are up to 40% urban, there are about 170,000 lines that would be eligible for support.

Based on all of this data, the specific concerns raised by the Tenth Circuit can be addressed here:

- In *Qwest I*, the court expressed its "concern that a discrepancy of 70-80% between some rural rates and urban rates might impermissibly stretch the boundaries of rate comparability."[121] Yet

[120] Line forecasts: 0.868396 lines/household; 0.395881 lines/employee.

[121] *Qwest I*, 258 F.3d at 1201.

- the data show that the discrepancy among urban rates is just as great as the discrepancy between urban and rural rates. Even so, NASUCA's proposed second alternative includes a process to gradually reduce the comparability standard, such that the range of rural rates above urban rates will be lowered and eventually eliminated.
- In *Qwest II*, the court first complained that "rural rates falling just below the comparability benchmark may exceed the lowest urban rates by over 100%."[122] The highest urban rate ($29.64) is more than three times the lowest urban rate; while the highest rural rate ($31.82) is somewhat less than three times the lowest rural rate. Congress did not, in fact, say that rural rates would be reasonably comparable to the **lowest** urban rate. Rather, § 254(b) directs that rural rates be reasonably comparable to urban rates generally. The best reflection of the general urban rate is the national weighted average urban rate.
- In *Qwest II*, the court also worried that "[e]ven if such rural rates are compared against the national urban average, we fail to see how they could be deemed reasonably comparable, especially in light of our previous consideration."[123] Looking at the entire universe of non-rural carriers' rates, rather than the selection

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[122] *Qwest II*, 398 F.3d at 1237.

[123] Id.

> presented to the Tenth Circuit, rural rates appear to be reasonably comparable to urban rates. Under NASUCA's proposed second alternative, however, the initial focus is on reducing high rural rates. And the continuing focus will be on further reducing the comparability threshold.

A reasonable comparability standard can be constructed based on the record here, and should meet the Tenth Circuit's concerns.

Thus far, we have discussed using the national urban average as a benchmark (or the basis for a benchmark). The Commission also asked for comment "on whether the Commission should compare rural and urban rates within each state instead of, or in addition to, comparing rural rates in all states to a national urban rate benchmark."[124] NASUCA submits that the Commission should compare rural and urban rates within each state as a subsequent step, i.e., "in addition to" the comparison to the national benchmark.

Appendix D sets out scatter diagrams for rates within each state, derived from the national data in Appendix C. This shows that in some states, all rates, including urban rates, have been set at levels above the national urban average.[125] This is the result of state-specific ratemaking. For example, in a particular state, rural rates might be 150% of the national urban average but only 125% of the state urban average. NASUCA submits that in this situation, it should be primarily the state's responsibility to provide support

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[124] NPRM, ¶ 19.

[125] This includes Alabama, Colorado, Massachusetts, Maine, Montana, North Dakota, New Mexico, Rhode Island, Vermont and Wyoming

for those rural rates.[126] This is reflected in Step Four of NASUCA's second alternative proposal.

On the other hand, many states have maintained statewide averaged urban and rural rates.[127] States that have done so for non-rural carriers and receive no or minimal federal support for those carriers should be able to continue this practice. States with carriers with averaged rates that receive federal support will be addressed in the early stages of NASUCA's second alternative proposal.[128]

As the Commission states, the Tenth Circuit rejected the Commission's use of a range because the range merely preserved "the disparity of rates existing in 1996" while doing nothing to "advance" universal service.[129] The non-rural high cost mechanism must both preserve **and** advance universal service. This does not mean that there can be no benchmarks; it means that the application of the Commission's benchmarks is required to advance universal service.[130] NASUCA's second proposal here does so by -- over time -- narrowing the range of "acceptable" (i.e., non-supported) rural rates, and by expanding

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[126] The Commission also asks, "Would a state-specific urban rate benchmark provide states more flexibility in designing state rates?" Id. Not exactly; a state-specific benchmark would give the Commission more flexibility to deal with existing state ratemaking flexibility.

[127] Based on eyeballing the state scatter diagrams, that appears to be the case in Arizona, Colorado, Delaware, Idaho, Illinois, Indiana, Massachusetts, Maryland, Maine, Michigan, Minnesota, Montana, North Dakota, New Hampshire, New Jersey, New Mexico, Nevada, Oregon, Utah, Washington, Wisconsin and West Virginia.

[128] Efforts of the states to restructure rates to maximize their share of the USF should be rejected. One such rejectable effort would be deaveraging, i.e., increasing rural rates and decreasing urban rates, in the expectation of receiving federal support as a result.

[129] NPRM, ¶ 19.

[130] *Qwest II*, 398 F.3d at 1236.

the definition of rural areas to include more territory.[131]

VIII. CONSIDERATION OF LOCAL CALLING AREAS MUST BE PART OF THE PROCESS OF EVALUATING RATES.

The Commission understands that the extent of the local calling area may influence whether rural rates are reasonably comparable to urban rates:

> [W]hile some states may want to keep local rates in rural areas very low, customers in such states may have very small calling areas and, consequently, make more toll calls. Other states may want rural customers to have very large calling areas so they do not have to make as many intrastate toll calls, but that may require higher local rates to offset the revenues the carrier would lose from toll calls. If rural rates in the second group of states were no higher than urban rates in the state, should they be considered to be reasonably comparable even though they may be higher than the rural rates in the first group of states?[132]

Unfortunately, the Commission has posed the question incorrectly. The real issue is whether the total "local" rate in the rural exchange is reasonably comparable to the total local rate in the urban exchange. The typical urban exchange has an expansive local calling area; upon paying the basic rate customers are able to reach many, many other customers, including neighbors, businesses and governments. If a rural customer's local calling area is as extensive as the urban customer's, then the comparison of local rates is fair. If the rural customer must make numerous toll calls in order to have the same reach of calling within what is often referred to as a "community of interest," then the comparison must be between the urban rate and the rural local rate plus some amount of toll calling.

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[131] See Section X. and XIV.D., below.

[132] NPRM, ¶ 18.

It is a difficult task to determine what that equivalent local calling area should be. (In this respect, the task is no different from the others facing the Commission here.) NASUCA submits that the task can be undertaken in two fundamentally different ways.

The first, establishing equivalent functional local calling areas, is something that may have to be done by the states. The second, measuring the cost of calling an equivalent number of customers, could be done on a state-by-state basis by the Commission. But for the immediate purposes here -- determining eligibility for support -- a simplified version of the second method could be used.

A. Equivalent functional areas

Under the functional approach, a "reasonably comparable" local calling area for a rural exchange would be defined as the ability to reach, as a local call: 1) each contiguous exchange; 2) the exchanges for any county seat that serves any part of the exchange; and 3) a metropolitan exchange, if the wire center is within the metropolitan statistical area ("MSA") of a metropolitan exchange and/or within a state-specified distance from the metropolitan exchange.[133] Almost all urban exchanges have local calling areas that meet this standard. Each portion of the standard is discussed more fully below.

As to contiguous exchanges, for urban consumers, a call across the street, or to a neighbor, is always a local call. Unless contiguous rural exchanges are included in the local calling area, there will always be situations where calls that cross the artificial line that is the exchange boundary -- including calls to neighbors or across the street -- will be

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[133] For example, in Ohio, the Ohio Consumers' Counsel has proposed that exchanges within 22 miles of a metro exchange should have local calling to the metro exchange. See *In the Matter of the Commission's Extended Area Service Rules Found in Chapter 4901:1-7, Ohio Administrative Code*, PUCO Case No 01-2253-TP-ORD, Comments of the Ohio Consumers' Counsel (January 29, 2002) at 13-14 (accessible at http://dis.puc.state.oh.us/dis.nsf/0/C48592B95461E14985256B52006D97CD?OpenDocument).

“long distance” toll calls. Each rural exchange, in order to have service reasonably comparable to that in urban exchanges, should, at a minimum, have all contiguous exchanges included in its local calling area.

The next level involves county seat calling. There are three basic levels of government in most states: local (city, village or township), county and state. In most instances, local government is within a consumer’s home exchange. Where local government is not within the home exchange, it is most likely within the contiguous exchange. Thus local calling to contiguous exchanges will typically allow consumers local telephone access to their local government.

Depending on the size of the state, however, the state capital can be a true “long distance” call for most of the state. County government, although much closer than the state capital, may not be within a contiguous exchange for many rural customers. All citizens should be able to call their county government as a local call, and county government should be able to call its constituents as a local call. This is particularly important for rural counties.

Finally, “rural” customers who live near a metropolitan area -- in terms of absolute distance as determined by the state -- or within the MSA of the metropolitan exchange should be able to call the metro exchange as a local call, just as the residents within that metro exchange are able to. Among other things, this -- like the other standards proposed here -- will also ensure rural exchanges will remain or will become reasonably comparable to each other.

This sort of analysis would be difficult for the Commission to perform, and is better suited to the local expertise of the state commission. A state could be required to

certify -- in its annual universal service certification -- that its rural wire centers served by non-rural carriers have the minimum local calling area described here. But for the purposes of this Commission process, i.e., to determine whether a non-rural carrier can be eligible for federal support, a simpler approach would be more useful, as described in the next section.

B. Number of lines reachable with a local call

Where, as in most of the country, local calling is available on a "flat rate," or unlimited usage for a fixed monthly charge, basis, the incremental cost to a customer of an additional call within the local calling area is zero. With a constricted local calling area, the customer's decision to make calls outside the calling area is measured against the incremental cost of the toll call, usually billed at intraLATA toll rates.[134] Consumers' reactions to this incremental cost will vary from consumer to consumer and month to month. It would be difficult to pin down a customer-specific "normal" **cost** of a constricted local calling area.

As described in Appendix F, NASUCA's methodology included an analysis of the local calling areas of wire centers. The results of the analysis can be displayed as follows:

Percent of the population living in urban areas	Number of Wire Centers	Average price of flat-rate residential service + SLC + FUSF	Number in calling area	People who can be called for dollar of price	Natural log of people who can be called for dollar of price

[134] Or the call is made with a wireless phone on an "all distance" plan.

	(a)	(b)	(c)	(d) = (c)/(b)	(e) = ln [(c)/(b)]
0	1,808	21.00	200,850	9,564	0.58
0-20%	3,979	20.81	672,781	32,325	0.64
20-40%	545	20.47	645,037	31,507	0.65
40-60%	1,057	20.42	896,842	43,914	0.67
60-80%	1,393	20.34	775,582	38,132	0.67
80-100%	4,278	19.40	2,924,367	150,715	0.77
100%	1,092	19.57	4,624,126	236,246	0.78
Sample avg. (0-100%)	11,252	19.63	2,454,104	125,001	0.75

The fourth column is a measure of the potential benefit from subscribing to flat-rate residential service. Column 4 shows that consumers in 100% urban areas can reach almost 25 times as many other customers per dollar as those in the most rural areas.

This provides a measure of the value of local telephone service. Arguably, however, the numerator in this calculation is overstated because no recognition is made of the diminishing benefit of being able to reach certain places or persons. For example, a customer in a city has a need to reach a few dry cleaners, but not one hundred dry cleaners. The fifth column in the chart reflects an adjustment for these diminishing returns by taking the natural logarithm of the number of reachable persons. This table shows that even after controlling for diminishing benefits from the wider calling area, it is still the case that rates in rural areas are not reasonably comparable to urban areas.

For the purposes of NASUCA's second alternative here, that is, determining eligibility for consideration for support rather than calculating support, a "rough justice" would be achieved if it were assumed that a 35% adder to rural rates would simulate the

cost of an equivalent to urban rates.[135] This criterion would not award support to any wire center that does not have high costs.

IX. THE ISSUES OF DEREGULATED RATES, MULTIPLE-USE NETWORKS, AND CETC SUPPORT.

There are three distinct but demonstrably related issues that should give the Commission pause in formulating its policies here. The first of the issues is the number of basic service rates around the country that have been deregulated by the states. The second issue is the extent to which the telecommunications network is used to provide services other than basic service. And the third issue is the extent to which CETCs are receiving high-cost universal service funds.

A. How Can Universal Service Support Ensure Reasonably Comparable Rural Rates When Rates Are Deregulated?

It is safe to say that when Congress tasked the Commission with ensuring that rural rates were reasonably comparable to urban rates, basic service rates were regulated -- that is, set with the approval of or within limits set by state regulators. Congress reasonably assumed that there would be oversight to ensure that the federal assistance actually resulted on reasonably comparable rates.[136]

Such oversight is increasingly absent, however. From state to state, the constraints that once applied to the rates for basic service are diminishing, as a result of state legislative action or state regulatory initiative.[137]

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[135] That is, 0.78/0.58 ~= 1.35.

[136] State commissions continue to affirm this to the Commission each year.

[137] E.g., Indiana. See http://www.upi.com/Hi-Tech/view.php?StoryID=20060301-110338-4271r.

This is one area among many in which the states must be responsible for their decisions. A state that has given its non-rural carrier(s) discretion to set their own rates for basic service cannot certify that universal service support is being applied so as to ensure reasonably comparable rates.[138] That state should certainly not be able to apply for supplemental federal support under the back-stop mechanism described in NASUCA's proposal.

The trend toward deregulated rates demands even closer examination by the Commission in determining whether those rates are affordable and whether rural rates are reasonably comparable to urban rates. It also demands closer examination of whether federal funds are used to make those rural rates reasonably comparable to urban rates. Indeed, it would be reasonable for the Commission to determine that a state, having deregulated its retail basic service rates, can have no control over whether those rates are reasonable or reasonably comparable, and thus should not receive any high-cost support.[139]

B. If Universal Service Is to Support Networks, It Must Be Recognized that Networks Have Multiple Uses.

It is often argued by ILECs -- most often rural ILECs -- that universal service supports networks, not just basic service.[140] NASUCA's response has typically been that

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[138] Such states have typically made the decision that (allegedly) "market-based" rates are per se just and reasonable.

[139] Of course, if rates are deregulated but do not increase, support should continue.

[140] See CC Docket No. 96-45, NASUCA Reply Comments on Joint Board High-cost Support Proposals and Other Universal Service Issues (October 31, 2005) at 14.

the law allows only the services designated by the Commission to be supported by the USF.[141] For now, those services are limited to basic service.[142]

Yet the Commission has acknowledged that

> [a]lthough advanced telecommunications and information services currently are not supported by the non-rural high-cost mechanism, the public switched telephone network is not a single-use network, and modern network infrastructure can provide access not only to voice services, but also to data, graphics, video, and other services. The Commission has found that the use of high-cost support to invest in infrastructure capable of providing access to advanced services is not inconsistent with the requirement in section 254(e) that support be used "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."[143]

However, there is also the question looked at in the other direction: Is basic service -- and thereby federal support -- the only service whose revenues will support the networks? That answer is clearly no, especially as the networks evolve to provide more and more advanced services.

As discussed in Section XIII.A., the network has multiple uses. The increasing multiple uses of the networks demands closer scrutiny from the Commission to ensure that federal support is used to support basic service. The other corresponding obligation is to ensure that the advanced services also provide support for the networks over which they travel.[144]

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[141] Id.

[142] 47 C.F.R. § 54.101.

[143] NPRM, ¶ 12, citing 47 U.S.C. § 254(e) and *MAG Order*, ¶ 200.

[144] The prices for advanced services are, by and large, deregulated by order of this Commission. There does not appear to be any way to ensure that the rates for advanced services in rural areas are reasonably comparable to those in urban areas.

C. The Method for Supporting Incumbent Carriers Should Be Used for CETCs; CETCs Should Not Simply Receive Support Based on the ILECs' Support.

These comments have so far addressed universal service support for non-rural ILECs. As extensively discussed above, federal support should be applied so as to ensure that ILECs' rural rates are reasonably comparable to their urban rates.

It is recognized that CETCs are consuming an increasing share of the federal USF.[145] And most of the CETC payments go to wireless carriers.[146] The Commission determined in the *Ninth Report and Order* that support going to CETCs serving in non-rural ILECs' territories would be based, like support for the non-rural ILECs, on the forward-looking cost of service coming from the HCM, rather than on the ILECs' rates.[147] Yet those costs are the costs of a wireline network, not a wireless network. Thus the support going to wireless ETCs is even more divorced than is ILEC support from the carriers' rates, and it is even less certain than for ILECs that the support given to CETCs (especially wireless ETCs) produces rural rates that are reasonably comparable to urban rates.

Then there is the question of which rates are to be compared. Is the comparison between rural wireless rates and urban wireless rates, or between rural wireless rates and urban wireline rates? Under the Commission's previous high-cost mechanism, this question was to some extent irrelevant, but the question is central to a mechanism -- like NASUCA's second alternative -- that appropriately and, as legally required, begins and

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[145] Compare USAC 2004 Annual Report at 27 to USAC 2003 Annual Report at 26.

[146] Id.

[147] *Ninth Report and Order*, ¶ 90.

ends with looking at rates rather than costs. NASUCA suggests that the comparison would continue to be to the national urban wireline average rate.[148]

In the *ETC Designation Order*, the Commission required an ETC applicant (wireless, wireline or other) "to demonstrate that it offers a local usage plan comparable to the one offered by the incumbent LEC in the service areas for which the applicant seeks designation."[149] The rate including that "local usage plan" would, therefore, be subject to the reasonable comparability test.

The Commission's principle of competitive neutrality[150] was not compelled by § 254 of the 1996 Act. NASUCA submits that the process of rethinking the support mechanism for ILECs -- taking it back to the requirements of the law, as directed by the Tenth Circuit -- need not be overly constrained by the notion of competitive neutrality. Likewise, rethinking the support mechanism for CETCs should not be overly constrained by this principle.

This is especially the case because, as the Commission knows, "competitive neutrality" is very much in the eye of the competitor: Most participants view as not competitively neutral whatever disadvantages them or advantages the competition, while arguing that measures that advantage them or disadvantage the competition are completely neutral.

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[148] Yet similar to the portion of NASUCA's second alternative proposal discussed in Section XIV.F., below, there should also be a comparison to the urban rate charged by the ETC in that state. For example, if the wireline urban average is $23, a wireless rural rate of $45 might not seem to be reasonably comparable. But if the urban wireless rate in that state is also $45, then there is no reason to support the rural wireless rate.

[149] CC Docket No, 96-45, Report and Order, FCC No. 05-46 (rel. March 17, 2005) ("*ETC Designation Order*"), ¶ 32. The Commission said that it would review this "comparability" on a case-by-case basis. Id., ¶ 34.

[150] See footnote 98, supra.

X. GRADUALISM SHOULD BE A KEY PART OF THE PROCESS IN MODIFYING THE HIGH-COST SUPPORT MECHANISM FOR NON-RURAL CARRIERS.

The non-rural high-cost mechanism -- at least the HCM piece of it -- has been in effect since adopted in the *Ninth Report and Order* in 1999. *The Order on Remand* in 2003 basically "tweaked" the HCM, changing the reasonable comparability benchmark based on costs from 135% to two standard deviations.[151] NASUCA proposes here substantial changes to the mechanism such that it will either be based on a comparison of costs to revenues or will be based from the outset on reasonable comparability of *rates*. The high-cost mechanism will now subsume the IAS and ICL support mechanisms (dating from 2000 and 2001 respectively) which have never included any consideration of rates.

These factors, among many others, including the local calling area issues discussed in Section VIII., argue for a gradual transition to the new mechanism rather than a flash-cut change. This is true under either of NASUCA's alternative proposals, where a phase-out of current support (where support is eliminated or materially decreased) or a phase-in of new support (where there is no current support or there is a material increase to the current support) would be appropriate.[152] No ILEC will see a flash-cut reduction to zero (unless its current support is minimal); neither will any ILEC see a huge influx of support where currently it receives little or no support. This transition should ease the burden on customers, carriers and the USF itself.

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[151] The adoption of a rate benchmark in the *Order on Remand* was new, but had no real impact on the level of support.

[152] NASUCA's proposals include HCM and IAS/ICL as current support; the likelihood that either of NASUCA's single-support alternative mechanisms will yield results identical to the current two-part support is small.

NASUCA's second alternative proposal also promotes gradualism by focusing first on the rural wire centers where rates are highest and least comparable, and where support is not currently made available.[153] The process would then move to states and carriers that currently receive high-cost funds but still have high rural rates that are not reasonably comparable, even with the support. Also considered early in the proposal would be rural wire centers that currently receive support where loss of the support would not likely result in rates that are not reasonably comparable. NASUCA's proposal thus prioritizes the areas for review, leaving for last the areas that currently receive no support and have reasonably comparable rates -- specifically because none of the state commissions in those states have asserted that their rural rates are **not** reasonably comparable to urban rates given the current lack of support.

The other piece of gradualism that is built into NASUCA's second alternative is the continuing and continual availability of the state backstop mechanism. There, if the results at any point of the mechanical implementation of the process do not adequately reflect state-specific conditions, the state will be able to plead its case to the Commission and seek additional support.[154]

XI. THE NEED FOR STATE SUPPORT MECHANISMS

The *Qwest I* court noted the Commission's argument that it did not have jurisdiction to set intrastate rates, but stated, "The FCC may not have jurisdiction with

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[153] As noted in NASUCA's proposal, if the high rural rates are the result of state ratemaking decisions that have also produced high **urban** rates, then the primary responsibility for support should rest with the states.

[154] Given the importance of the backstop mechanism, it will be necessary for the Commission to act on requests more expeditiously than it has on Wyoming's under the current mechanism. See footnote 14, supra.

respect to intrastate rates, but it is nevertheless obligated to formulate its policies so as to achieve the goal of reasonable comparability by inducing 'sufficient ... State mechanisms' to do so."[155] The court further stated,

> The FCC acknowledges that the *Ninth Order* will result in reasonably comparable rates only if the states implement their own universal-service policies. E.g., *Ninth Order* ¶ 56 ("We believe that this level of [federal] support will provide states with the ability to provide for a 'fair range' of urban and rural rates within their borders ...."). Yet there is nothing in the *Ninth Order* to induce such state mechanisms, and there is nothing in the Order requiring such inducements in the future if the states fail to provide for reasonable comparability between urban and rural rates as required by the statute. To the contrary, the *Ninth Order* expressly adopts the Joint Board's recommendation that the FCC "abstain from requiring any state action as a condition for receiving federal high-cost universal service support" other than the certifications required by § 254(e). *Ninth Order* ¶ 67. As noted above, the Act requires the FCC to base its policies on the principle that there should be sufficient state mechanisms to promote universal service. Thus, the FCC must ensure that these mechanisms exist.[156]

The court acknowledged the dual federal/state responsibility for universal service, which creates the need for a "partnership between the federal and state governments" to preserve and advance universal service.[157] As the court stated,

> Thus, it is appropriate -- even necessary -- for the FCC to rely on state action in this area. We therefore reject Qwest's argument that the FCC alone must support the full costs of universal service.
>
> Nevertheless, the FCC may not simply assume that the states will act on their own to preserve and advance universal service. It remains obligated to create some inducement - a "carrot" or a "stick," for example, or simply a binding cooperative agreement

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[155] *Qwest I*, 258 F.3d at 1200.

[156] Id. at 1203 (footnotes omitted).

[157] Id.

> with the states -- for the states to assist in implementing the goals of universal service.[158]

In the *Order on Remand*, the Commission adopted just such an inducement mechanism, which the *Qwest II* court found to be adequate. As the *Qwest II* court stated,

> [T]he FCC has drafted a requirement into its support mechanism for non-rural carriers requiring states to certify that rural rates within their boundaries are reasonably comparable. If they are not, the states must develop and present an action plan to the FCC indicating the state's response. If the state fails to do so, federal funds will be withheld. …
>
> We are satisfied that the inducement mechanism contained in the *Order on Remand* adequately responds to the concerns we expressed in *Qwest I*. The mechanism requires a careful yearly review, and the prospect of withheld funds will certainly bring pressure to bear on the states. Petitioners have failed to proffer any evidence to suggest that the Commission's inducement mechanism will prove inadequate. As with any such mechanism, experience may indeed prove the best judge of its efficacy. The Commission is in a unique position to determine what inducements are necessary to effectuate the goals of the Act. While we can envision various approaches to more effectively induce state action, given our deferential standard of review, we cannot say that the Commission's determination in this case was arbitrary or capricious.[159]

The fact that the Tenth Circuit found the inducement mechanism in the *Order on Remand* to be reasonable does not, of course, mean that this mechanism is the only appropriate mechanism. NASUCA submits that the requirement in its second alternative proposal for state action -- detailed below -- reasonably goes beyond the mechanism created in the *Order on Remand* because of the broader scope of the proposal, which focuses more on the rates that the *Qwest I* court acknowledged were primarily states' responsibility.

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[158] Id. at 1203-1204.

[159] *Qwest II*, 398 F.3d at 1238.

One action that NASUCA's proposal does *not* require of the states is transforming implicit support into explicit support. The *Qwest II* court definitively found that such was not required under the 1996 Act, given that the Act explicitly makes explicitness a condition for federal support but not for state support.[160] This principle clearly allows the existence of statewide averaged rates, as seen in many states.[161] The Commission's non-rural high-cost mechanism cannot interfere with these state decisions, and should not create incentives that would cause states to move away from statewide averaged rates.

XII. THE NEED TO FIX THE HIGH-COST MODEL

There is a desperate need to update and improve the FCC's forward-looking high-cost model, also referred to as the Synthesis Model. It has been many years since the Synthesis Model was last substantially revised. It is possible that there have been improvements that have been developed in cost modeling that should be considered and be applied to the Synthesis Model. At this point, however, it does not appear that there are any available alternatives that are superior to the FCC's Synthesis Model.

Three crucial updates need to be made to the model: First, switch and special access line counts must be brought up-to-date. Second, the allocation of special access lines among wire centers must also be updated. The current allocation relies on a 1999 data request. The deployment of special access lines has changed significantly in the intervening years, and it is clear that the model, as it now exists, includes a serious misallocation of special access lines. This must be corrected. Third, the customer

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[160] Id. at 1232-1233; see also id. at 1238.

[161] See footnote 127, supra.

location files should be updated to accurately locate customers and design the network. There should be more accurate means of mapping customer locations today so as to better approximate customer locations and the cost of constructing networks to reach such customers. Securing these data are not burdensome on the carriers and updated data could be integrated into the model in a relatively short period of time.

Another aspect of the model is also outdated. As designed, the model derives costs for narrowband service. Of course, the network now and for the foreseeable future will also be constructed to provide broadband service. (The arguments above on multiple-use networks are relevant here.) Especially for use with NASUCA's first alternative proposal, which considers revenues from all services in establishing the urban benchmark, it will be necessary to consider the costs for all of those services. On the rural side, since the costs to be reviewed are only the costs of the supported services, it will be necessary to **exclude**, for example, the costs of broadband.[162]

Finally, NASUCA's data allows the Commission to correct a fundamental problem with the current HCM: Whether it be rates or price, the relevant comparison for determining reasonable comparability is **urban** rates or prices. The HCM determines support based on the national average cost, not the national **urban** average cost. The Commission can use the urban areas identified by NASUCA -- whether the standard be 100% or 100%-80% urban -- in order to develop a benchmark that provides the proper perspective.

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[162] Costs of broadband would be considered separately in the context of NASUCA's proposed broadband incentive program. See Section XVI.

XIII. NASUCA'S FIRST ALTERNATIVE PROPOSED NON-RURAL HIGH-COST SUPPORT MECHANISM

The standard for preserving and advancing universal service is based on a comparison of urban and rural rates. Reconciling cost and rates is, therefore, the prerequisite for adopting any cost-based mechanism. In *Qwest I*, the court found that the Commission could use a cost-based mechanism if it could show that such a mechanism would lead to urban and rural rate comparability.[163] In *Qwest II*, the court reiterated and expanded on its finding by stating:

> On a separate note, we did intimate in *Qwest I* that we would be inclined to affirm the FCC's cost-based mechanism if it indeed resulted in reasonably comparable rates. However, we expected the Commission to return to us with empirical findings supporting this conclusion. Once again, we find no evidence in the record before us to support the FCC's pairing of rates to costs in this context. In other word, the FCC based the two standard deviations *cost* benchmark on a finding that rates were reasonably comparable, without empirically demonstrating a relationship between costs and rates surveyed in this context.[164]

Rates can be paired to costs. To do so, however, it is first necessary to understand what type of costs the cost model is estimating. Second, it is not necessary for support to equal the difference between the local rate and the estimated cost in order to ensure that support is sufficient. Urban revenues can be compared to costs in high-cost areas, thus minimizing the need to specifically identify rural areas under this alternative.

A. The Cost Model

The FCC's cost model is a forward-looking economic cost model of a network with the capability to provide the designated universal services. The early debate over

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[163] *Qwest I*, 258 F.3d at 1202.

[164] *Qwest II*, 398 F.3d at 1237.

the model centered on its forward-looking definition, that is, the model's use of current technology, efficient design and current prices rather than what has been called the actual plant used to provide services. The *Qwest I* court found the use of the model to be reasonable.[165] The Supreme Court, moreover, has approved the use of forward-looking costs under the Act.[166]

Overlooked in that debate was the fact that model is actually a model of a network that can provide multiple services in addition to the supported services. The services provided by the network include local exchange service, special access service, access to interexchange service, high-speed service capability, and switched services such as Call Waiting and Caller ID. The fact that the network provides multiple services is clearly demonstrated in the basic criteria the Commission propounded for the development of the model. For example, the FCC held that the model must be able to estimate the cost of not only residential and business basic service but also special access and private line services.[167] The simultaneous estimation of the cost of special and basic (switched service) allows these services to share facilities such as poles, trenches and conduit and transmission equipment. This sharing reduces the individual costs of both basic and special access services.

The FCC also required that the model not impede the provision of advanced services.[168] The FCC implemented this mandate by requiring the maximum copper loop

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[165] *Qwest I*, 258 F.3d at 1206.

[166] *Verizon Communications v.* FCC, 535 U.S. 467 (2002).

[167] *First Report and Order*, ¶ 250.

[168] Id.

length to be no longer than 18,000 feet.[169] This requirement constructs a network that can provide high-speed services, such asymmetric digital subscriber line service ("ADSL").[170]

In addition, the FCC requires that the network constructed by the model be capable of providing all of the designated services included in the universe service package.[171] Among those services is access to interexchange carriers.[172] The provision of that access uses the same network equipment and facilities that are used to provide local service, as the Commission noted: "The cost of local loops and their associated line cards in local switches, for example, are common with respect to interstate access service and local exchange service, because once these facilities are installed to provide one service they are able to provide the other at no additional cost."[173]

The provision of local exchange and access service requires the use of a switch to connect customers to each other and to interexchange carriers. The cost of the switch includes the cost of the processor and the switch software. Therefore, the cost of the switch includes the cost of providing custom calling services such as Call Waiting. In addition, the signaling system that connects the switches and customers depends on

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[169] CC Docket No. 96-45, *Fifth Report and Order*, FCC 98-279 (rel. October 28, 1998) ("*Platform Order*"), ¶ 68-70.

[170] The Commission determined that high-speed services are services with over 200 kbps in at least one direction. See Second Section 206 Report, 15 FCC Recd at 20920; The FCC Synthesis model is not designed to support video services. To provide video service, AT&T Project LightSpeed requires fiber-to-the-node technology, where fiber is brought to within 3,000 feet of the home. "SBC Communications Details Plan for new IP-Based Advanced Television , Data and Voice," San Antonio, Texas (November 11, 2004), http://att.sbc.com/gen/press-room?pid=4800&cdvn=news&newsarticleid=21458. Verizon's "FiOS" network constructs fiber to the customer's premise. See http://www22.Verizon.com/FiOSforhome/channels/FiOS/root/faq.asp#fios_q1.

[171] *First Report and Order*, ¶ 223.

[172] Id., ¶ 56.

[173] *In the Matter of Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, *First Report and Order*, FCC 96-325 (rel. August 8, 1996), ¶ 678.

Signaling System 7 ("SS7"). This implies that the forward-looking model can also provide services dependent on SS7, such as CallerID.[174]

B. The Determination of a Cost Benchmark

The purpose of a cost benchmark is to determine a standard for providing support. That is, the Commission will support costs that are above the benchmark. The Commission has previously adopted two cost benchmarks. Neither of these benchmarks, however, was directly related to the ability of a carrier to provide the services supported by the USF. That ability is marked by the relationship between the total revenue that the carrier receives and the cost of the network that provides the supported services. If the revenue is equal to or greater than the cost of service, then the carrier can provide the services. Early on, the Commission looked to revenues as the key to determining universal service support.[175]

The HCM results show clearly that the cost of providing the supported services is higher in rural areas than in urban areas.[176] A carrier can provide the same or comparable services in urban and in rural and high-cost areas under a number of different conditions. First, the carrier can charge the same rate in both areas. The rate would be higher than cost in low-cost urban areas and lower than cost in rural and high-cost areas. This scenario, therefore, uses implicit support through the rate-making process to provide the same services at the same rates. Second, the carrier can charge higher rates in the rural or high-cost areas. Given the extent of the higher costs in those areas, rates in those areas

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[174] *Platform Order*, ¶ 79.

[175] *First Report and Order*, ¶

[176] See the model results files, http://www.fcc.gov/wcb/tapd/hcpm/welcome.html.

will have to be increased, making it likely that the rural or high-cost rates will no longer be comparable with urban low-cost rates.

Support needed to produce reasonably comparable rates, however, does not have to equal the difference between the low-cost urban basic exchange rate and the rural or high costs in order to maintain the rural or high-cost basic exchange rate at a level comparable to the low-cost urban basic exchange rate. Rather, the support levels can recognize that urban customers, on average, provide the carrier with revenue in excess of the local rate. As noted above, the network provides multiple services. Therefore, the revenue that supports the network should reflect the expected revenue from those multiple services. These revenues include those from basic service, the SLC, switched access, vertical features and ADSL service.

The following example illustrates these relationships. First, assume that the cost in a low-cost urban area is $20 and that the rural cost is $35.[177] Second, set the urban rate at $10, and assume that the average urban customer purchases a combination of other services that generate an additional $10 in revenue, thus meeting its costs. The carrier should be able to obtain, on average, the same additional $10 in revenue from the rural customer. Therefore, in order to maintain the same rate in the urban and rural areas, the carrier only needs $15 in support, the difference between the urban average revenue per customer and the rural cost. The carrier does not need the difference between the urban rate and rural cost, an amount equal to $25. Providing the carrier with $25 in support would be excessive because it would allow the carrier to obtain revenue twice, first from the customer for additional services and again from the universal service fund.

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[177] It is assumed here that "cost" includes a return on investment.

The Joint Board recognized that the network provides multiple services and that the benchmark should not be established as the difference between the [low-cost urban] rate and rural costs. It noted:

> We also do not support tying the benchmark to average rates for residential and single line business services because residential and single line business service are only two of the services provided over the facilities for which costs are included in the proxy model cost estimates. Therefore, a rate benchmark would be inconsistent with the method we are recommending for determining the cost of providing the network used to provide the supported services. The average rate benchmark ignores the revenue generated from the customer that contributes to the joint and common costs of providing both that service and those services designated for support.[178]

In 1997, the Commission estimated that a revenue benchmark would be approximately $31 for residential customers.[179] That estimate was based on average (urban and rural) residential revenue. Since that time, per-minute access revenue has decreased and revenue from other sources has increased.

A current revenue benchmark should start from the average urban rate, estimated by NASUCA to be $19.57.[180] Estimates of other revenue sources are much harder to generate. One reasonable estimation is that, for urban customers vertical services generate between $4 to $7, switched access between $2 to $3, and DSL services between $5 to $7 per month.[181] Therefore, the average urban customer provides the carrier with approximately $31 to $37 in monthly revenue. NASUCA recommends that the

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[178] CC Docket No. 96-45, *Recommended Decision*, FCC 96J-3 (rel. November 8, 1996), ¶ 315.

[179] *First Report and Order*, ¶ 267.

[180] On average, urban areas have low costs. This does not mean that there are no high-cost urban areas under the Census Bureau's definitions that NASUCA recommends here.

[181] Urban customers' expansive local calling areas mean that they generate less access charge revenue for the non-rural carrier than do rural customers with limited local calling.

Commission obtain reasonable comprehensive estimates of these revenue flows and determine an average urban revenue benchmark to be used in comparison to the costs in rural and high-cost areas for the purposes of determining universal service support to rural areas.

Under NASUCA's proposed first alternative, states would continue to be required to certify that their rural rates were reasonably comparable to urban rates.[182] This would allow states -- that have much greater power over local rates than does the Commission -- more say in assessing comparability.

NASUCA's first alternative proposal removes the arbitrary foundations of previous benchmarks.[183] The benchmark directly links revenue, rate and cost, and thus, the mechanism is sufficient, as § 254(e) requires. Under this proposal, there is no incentive for state commissions to de-average their local rates to qualify for additional support.[184]

XIV. NASUCA'S SECOND ALTERNATIVE PROPOSED NON-RURAL HIGH-COST SUPPORT MECHANISM

NASUCA proposes a mechanism here that would pass the Tenth Circuit's scrutiny. Fundamentally, the proposal begins and ends with an examination of rates, per § 254(b)(3). The mechanism is designed to create the proper inducements for states to

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[182] There might also be a need for some states to certify that the rates in their high-cost urban areas are reasonably comparable to national urban rates.

[183] NASUCA's second alternative proposal requires the Commission to set a number of benchmarks, primary among which is a rate comparability benchmark **against which rural rates will actually be tested**. Throughout the process, protection from arbitrariness comes from the backstop state mechanism.

[184] Under NASUCA's second alternative, increased rural rates could make a state eligible for support, but the actual support award will still be determined based on costs.

take shared responsibility for universal service[185] and would yield rural rates for non-rural companies that are reasonably comparable to urban rates.[186] And this mechanism -- which starts with the current comparability benchmark and then gradually narrows the range of unsupported rates -- thereby takes specific steps to "advance" universal service, as the *Qwest II* court insisted.[187] The mechanism would be "sufficient" for universal service purposes, as also required by the *Qwest II* court.[188] The Commission's present high-cost support mechanism for non-rural carriers can provide no such assurance.

Under NASUCA's second alternative proposal, rates are used to determine eligibility for support and the effectiveness of support, but they are not used to calculate the amount of support.[189] Determination of support occurs using the high-cost model; as previously discussed, NASUCA reiterates here that updating the model must be a high

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[185] 47 U.S.C. § 254(b)(5); *Qwest I*, 258 F.3d at 1203-1204; *Qwest II*, 398 F.3d at 1238.

[186] This proposal focuses on "rural" rates to begin with, addressing "high cost" later in the process, as distinguished from NASUCA's first alternative, which focuses on high-cost areas whether they are rural or not.

[187] *Qwest II*, 398 F.3d at 1235-1236.

[188] Id. at 1233-1234.

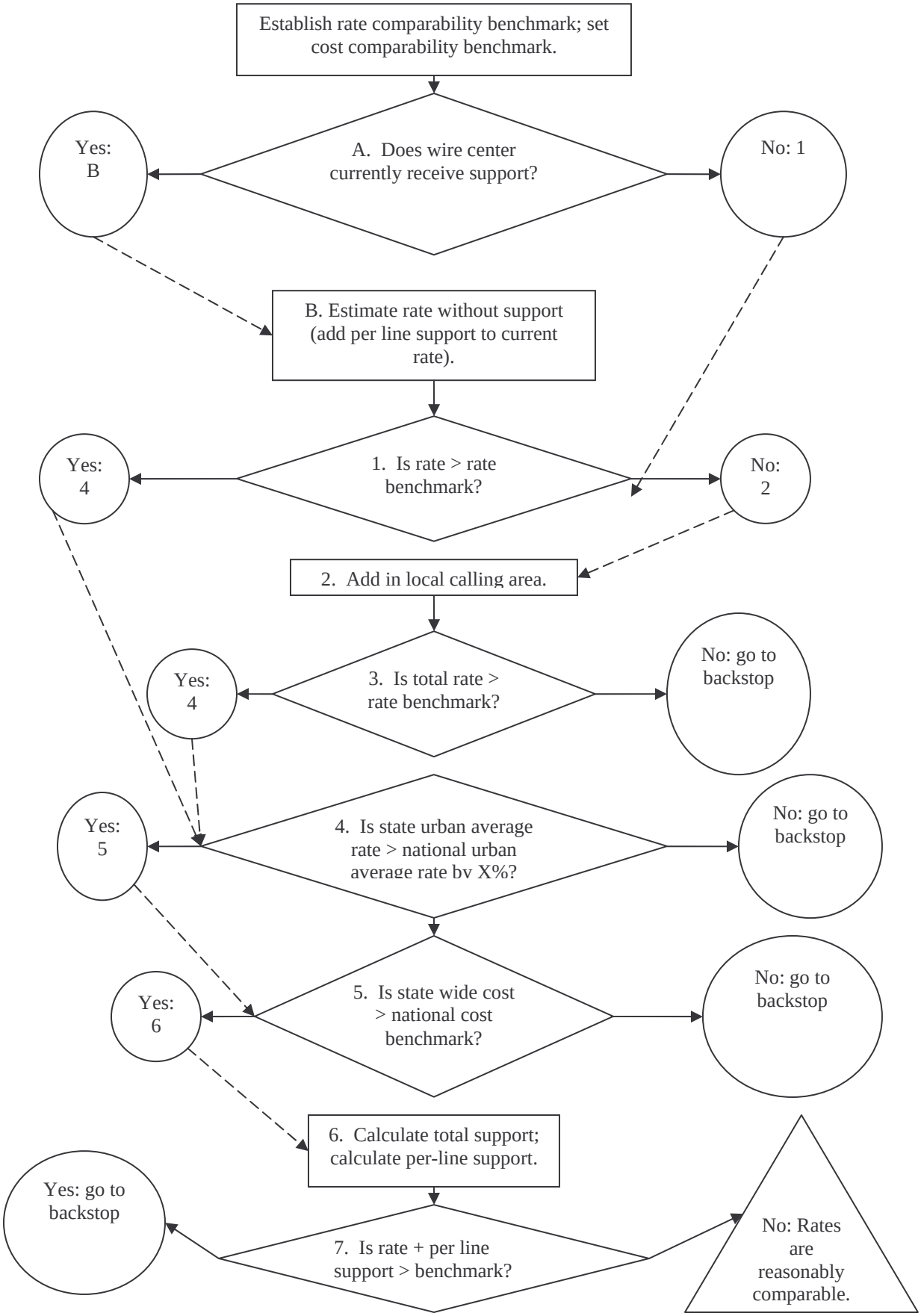
[189] The proposal also factors in consideration of support already received, local calling areas, and state ratemaking decisions.

priority for the Commission. Throughout the process, however, states will have recourse to a state-specific (or carrier-specific) supplemental process, where they will have the opportunity to request additional support.[190] This too builds on the Commission's current mechanism.[191]

The following flowchart depicts the process:

[190] The earlier in the process recourse is made to the backstop mechanism, however, the more substantial will be the burden to justify federal support.

[191] See Section J., below.


Establish rate comparability benchmark; set cost comparability benchmark.
A. Does wire center currently receive support?
Yes: B
No: 1
B. Estimate rate without support (add per line support to current rate).
1. Is rate > rate benchmark?
Yes: 4
No: 2
2. Add in local calling area.
3. Is total rate > rate benchmark?
Yes: 4
No: go to backstop
4. Is state urban average rate > national urban average rate by X%?
Yes: 5
No: go to backstop
5. Is state wide cost > national cost benchmark?
Yes: 6
No: go to backstop
6. Calculate total support; calculate per-line support.
7. Is rate + per line support > benchmark?
Yes: go to backstop
No: Rates are reasonably comparable.

Note that the current universe of non-rural companies is addressed here. In NASUCA's comments on the rural high-cost mechanism, it was proposed that study areas of rural companies that are affiliated with non-rural companies within the same state should be treated as non-rural and combined with the non-rural company study areas.[192] NASUCA has not attempted to build this combination into the analysis here.

Based on the data, NASUCA's proposal begins by examining rates on a wire center basis. This is the minimum feasible area. It might be possible to cluster wire centers that share key characteristics.[193]

In terms of priority on the first run-through, the wire centers that need to be addressed first are those whose rates are not reasonably comparable now and do not currently receive any support. Next are those that have rates that are not reasonably comparable but do currently receive support.[194] Both of these would be with a view to adding or increasing support in order to make those rates reasonably comparable. After that, the wire centers that receive support but whose rates would be reasonably comparable even without that support can be examined, with a view to eliminating the support. Other wire centers could be relegated to the backstop mechanism, for their states to plead their case for support. After that, the review would be accomplished on an

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[192] CC Docket 96-45, NASUCA Reply Comments on Rules Relating to Rural High-Cost Universal Service Support (December 14, 2004) at 15.

[193] See *In the Matter of Unbundled Access to Network Elements*, WC Docket No. 04-313, NASUCA Comments (October 4, 2004) at 17-20.

[194] If the support currently received is imputed in these wire centers, their rates would, in fact, be even less reasonably comparable.

annual cycle.[195]

A. DETERMINING REASONABLY COMPARABLE RATES AND COSTS.

Determining benchmarks for reasonably comparable rates will be done by the Commission, with the considerations described in Section VII., above. The task will need to be done at the inception of the process and then again periodically, possibly annually.

In Step Six, below, support levels are calculated by a comparison of statewide costs to national average urban costs. The Commission will also have to determine a benchmark for urban costs.

As discussed above, the Commission could adjust these benchmarks in order to meet the goal of § 254 that universal service be "advanced." This could be done by 1) narrowing the gap between rural rates and urban rates; 2) expanding the definition of rural territory where rates are supports; and/or 3) increasing the level of costs that are supported.

B. INITIAL REVIEW: IDENTIFYING RURAL RATES THAT ARE NOT CURRENTLY SUPPORTED BUT ARE NOT REASONABLY COMPARABLE.

The most urgent priority is to bring support to rural areas that currently have rates that are not reasonably comparable to urban rates but currently receive no support. These can be identified from the data in Appendix F. These wire centers will take first priority in the determination of levels of support in Step Six.

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[195] During the first iteration, it would be possible to establish a (large) group of wire centers that are not eligible for support that would not have to be reviewed in subsequent years, absent changes in the rates. These wire centers would also be covered by the required state certifications, and states would always have recourse to the backstop mechanism to plead the need for support.

C. INITIAL REVIEW: ASSESSING THE LEVEL OF SUPPORTED RATES IF SUPPORT WERE REMOVED.

As discussed in many sub-contexts above, the current high-cost support mechanisms (HCM, IAS and ICL) have little relationship to rates, and cannot be shown to cause rural rates to be reasonably comparable. Thus an early challenge in resolving non-rural high-cost support issues is to determine -- as best as possible -- the impact of the current level of support on rates. This would initially be done as part of a transition, in order to determine subsets of wire centers for prioritization in the initial round of the process. It would also need to be done on an ongoing basis.

NASUCA proposes that this be done by applying (or, rather, "imputing") support on a per-line basis in non-rural carriers' rural wire centers. In the initial iteration, the Commission should start with wire centers that contain no more than 20% urban territory.[196]

The first piece of current support is HCM. For some wire centers, HCM is significant; for others it is not. HCM support is reported on a per-line per-wire center basis in USAC Appendix HC15. This is where the process of "imputing" current high-cost support to rural rates can begin.

IAS, on the other hand, is available in wire centers and to companies that do not receive HCM support. It is allocated by the ILEC's unbundled network element zones (again, without direct connection to cost of service), but the wire centers in each zone can be identified. This support is reported on a per-line per zone basis in USAC Appendix

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[196] Whether or not the Commission progresses to "less rural" definitions of rural, to the extent that there is IAS or ICL that goes to wire centers that do not meet this definition, it would likely be phased out.

HC13. Looking at the data in Section IV., however, there are a few states where IAS contributes significantly to overall funding.[197]

ICL is the only form of high-cost support received by those few states and non-rural companies that receive it.[198] For some of the companies, ICL is significant. ICL funding is reported on a per-line basis in USAC Appendix HC10.

Appendix F2 lists, by state, the rural wire centers (again, defined as 0% to 20% urban using Census Bureau criteria) that currently receive HCM, IAS or ICL funding, their rates, their per-line support, and the impact of imputing the federal support to the rates.[199] Appendix F1 explains the data contained in Appendix F1.

Specific examples might be helpful. In Mississippi, the DNCNMSMA wire center has $95.17 per month in HCM support targeted to it, and receives $4.72 in IAS. Combined with the $20.55 rate plus SLC, this implies that the rate would be $120.44 without support, above most likely benchmarks. On the other hand, the BSLSMSMA wire center in Mississippi receives $0.10 in HCM support. Imputed to the $22.27 rate plus SLC, this would be a $22.37 rate, likely under any reasonable comparability benchmark.[200] (This does not, of course, include the impact of local calling areas.)

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[197] The most substantial impact appears to be in Alabama, Kentucky, Nebraska, West Virginia and Wyoming.

[198] See footnote 49. As discussed above, Puerto Rico is excluded from this analysis.

[199] As with the non-rural carrier rate dataset, given the volume of the data and the time allotted to prepare this review, there are a few gaps in the data. Here again, NASUCA intends to present the Commission with the complete dataset when it is complete. At this point, there are questions about the rates charged in 35 of the almost 600 rural wire centers that receive support that are included in Appendix F.

[200] As discussed in Step Five, since actual support will be based on cost, if a wire center has high rates but low costs it will not receive support under the combined model. Any support for such wire centers will be the responsibility of the states, given that those rates are not based on costs.

Notably, however, in 1999 Mississippi received $4 million in high cost support. In 2005, that number had increased to $35 million. It is difficult to see how the support, **much less the increase in support**, had any actual effect on the rates.

Overall, after the substantial tasks of gathering the rate data, determining support on a wire center basis, and combining the two, there has been little opportunity to systematically assess the results of this imputation. One thing is clear, however: **There is no connection between the level of support received by a rural wire center and the rate charged in that wire center**. This is true of HCM support looked at separately, and of IAS/ICL separately[201]; it is also true of combined total support (HCM plus IAS/ICL). The *Qwest I* court would have approved of the Commission's support mechanism if such a connection had been shown, and the Qwest II court agreed, but found that the Commission had not made empirical findings in that regard.[202] Unfortunately, the evidence shows that the Commission could not make such empirical findings.

On the other hand, there are 1660 rural wire centers that receive less than $2.00 per month in support. It is hard to see how losing this support would result in rates in those wire centers that were no longer reasonably comparable.[203]

D. STEP ONE: COMPARING RURAL RATES TO THE NATIONAL URBAN AVERAGE RATE

On the initial run-through, priority for this step would be taken as follows:

1) Wire centers that have rates above the benchmark but currently receive no support.

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[201] Not surprising, because neither IAS nor ICL were designed to have an impact on rates.

[202] *Qwest II*, 398 F.3d at 1237, referring to *Qwest I*, 258 F.3d at 1202.

[203] The state mechanism described below would be available for those states.

2) Wire centers that currently receive support but still have rates above the benchmark.

3) Wire centers where imputing support yields rates above the benchmark.

4) Wire centers where imputing support yields rates below the benchmark.

The remaining wire centers (that get no current support and have rates below the benchmark) will be addressed last. This step will also be undertaken on a periodic basis.

The first need in ensuring support sufficient to create rural rates reasonably comparable to urban rates is to compare a specific rural rate to the urban rate benchmark. A wire center where the rural rate was greater than the urban benchmark would "pass on" to Step Four of the process. Wire centers that have rates lower than the benchmark could pass on to Step Two for consideration of the local calling area.[204]

As previously discussed, the Tenth Circuit required the Commission's support mechanism for non-rural carriers to both preserve *and advance* universal service, as the statute directs.[205] As noted above, NASUCA's second proposal could advance universal service in two ways: First, by lowering the range of reasonable comparability -- that is, lowering the benchmark -- on an annual basis. For example, if the benchmark were set at 6% above the urban maximum, the 6% would be used in the first year. In the second, the benchmark could be lowered to 5% above the maximum, and so on.

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[204] Alternatively, in this step of the process, a state could resort directly to the backstop state support mechanism described in Section XII.H., below, if the local calling area analysis were not attractive.

[205] *Qwest II*, 398 F.3d at 1236.

Under NASUCA's proposal, universal service could also be advanced by gradually expanding the definition of "rural." To begin with, only wire centers that are 0% urban would have their rates considered for eligibility for high-cost support. In subsequent years, "rural" areas could include those with up to 20% urban territory.[206]

It should be noted that these moves to advance universal service should be sufficient to ameliorate any risk that the initial benchmarks might be deemed to be arbitrary. This is especially true because the end result will be to have rural rates that are within the range of urban rates, as they are now overall.

E. STEPS TWO AND THREE: CONSIDER LOCAL CALLING AREAS

Up to this point, the process has focused only on local service rates. It did not consider the true cost of service in rural areas that is reasonably comparable to the cost urban service, that is, the cost of having a reasonably comparable local calling area. As discussed in Section VIII., above, the costs of establishing a reasonably comparable local calling area will vary tremendously, depending on how the local calling area is defined. Whether it is described numerically -- in terms of other access lines reachable with a local call -- or functionally -- in terms of neighboring exchanges, county seats and nearby metropolitan areas reachable with a local call -- it is clear, however, that establishing a comparable local calling area typically increases the cost of local service.

NASUCA proposes that wire centers that "pass" Step One, i.e., that have basic local rates that are reasonably comparable to the weighted urban average, should also

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[206] This would add another almost 4000 wire centers to the eligibility list. It is not clear if a subsequent move to include wire centers with up to 40% urban territory would go beyond the range of "rural" wire centers that should be supported.

have their local calling areas reviewed. As discussed in Section VIII. above, however, consideration of local calling areas could add 35% to the customer's payment for "local" service. Step Two would add the local calling area factor; Step Three would compare the combined rate to the benchmark. A wire center where the combined rate exceeded the benchmark would move to Step Four.

Rural wire centers where rates remain reasonably comparable even after adding consideration of the cost of local calling areas do not appear to need support to keep their rates at those levels. Under NASUCA's proposal, however, a state may request consideration for additional support.[207]

F. STEP FOUR: CONSIDER THE STATE URBAN AVERAGE RATE

There may be states that have high rural rates but also have relatively high urban rates, as a result of state-specific regulatory decisions. Such urban rates may not be based on the costs of urban service, which appears to be uniformly low nationwide.

In such an instance, the state has made the decision to narrow the gap between urban and rural rates. Citizens of other states should not be required to support those rural rates and further narrow the gap.

Rates in each wire center that passes to this step should be compared to the statewide urban average rate.[208] Only wire centers that exceed the statewide average by an amount to be determined by the Commission should progress to Step Five.[209]

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[207] See Section J.

[208] Wire centers that had local calling areas considered should retain the local calling area adder when being compared to the national benchmark should have the adder included at this step as well.

[209] Those that do not may still be eligible for support under the backstop mechanism.

G. STEP FIVE: COMPARING STATEWIDE AVERAGE COST TO THE NATIONAL AVERAGE URBAN COST

Rural wire centers that reach this step will have rates that are not reasonably comparable to urban rates. At this point, NASUCA's second alternative proposal temporarily moves away from consideration of rates. The actual amount of support received by a specific wire center would be calculated based on a comparison of statewide average forward-looking costs to a national urban cost benchmark, like what is done in the current non-rural high-cost mechanism.[210]

To the extent that this step eliminates IAS or ICL currently received by a wire center, it would be because those mechanisms were not focused on rural areas. This step should not eliminate any current HCM support, unless it was awarded in a state that had no rates above the benchmark even with imputation and the use of a local calling area adder.

The use of costs for determining support levels, including the use of national and statewide averages, has of course been found reasonable by the Commission.[211] It has also tacitly been accepted by the industry.[212] And the Tenth Circuit approved the use of the cost model.[213] The *Qwest II* court stated,

> [W]e would be inclined to affirm the FCC's cost-based funding mechanism if it indeed resulted in reasonably comparable rates. However, we expected the Commission to return to us with

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[210] The current mechanism, of course, compares the statewide average cost to the national overall average cost, not the national urban average cost.

[211] *Ninth Report and Order*, ¶ 32.

[212] See *Qwest I*, 258 F.3d at 1197, n.2 (noting that no party had appealed this aspect of the *Ninth Report and Order*).

[213] Id. at 1206.

> empirical findings supporting this conclusion. Once again, we find no evidence in the record before us to support the FCC's pairing of rates to costs in this context.[214]

Further, as previously noted, the use of forward-looking costs under the Act has been upheld by the Supreme Court.[215]

The FCC's rationale for using costs rather than rates to determine the amount of support -- as expressed in the *Seventh Report and Order* -- still holds true:

> This approach does not consider rates directly. Instead, it uses costs as an indicator of a state's ability to maintain reasonable comparability of rates within the state and relative to other states. We conclude that the underlying assumption in the Joint Board's recommendation -- that a relationship exists between high costs and high rates -- is a sound one, because rates are generally based on costs. We adopt this approach, in part, because states possess broad discretion in developing local rate designs. State rate designs may reflect a broad array of policy choices that affect actual rates for local service, intrastate access, enhanced services, and other intrastate services. A state facing costs substantially in excess of the national average, however, may be unable through any reasonable combination of local rate design policy choices to achieve rates reasonably comparable to those that prevail nationally. Through an examination of the underlying costs, instead of the resulting rates, we can evaluate the cost levels that must be supported in each state in order to develop reasonably comparable rates. Because responsibility for such support is shared at the federal and state levels, determining the federal portion based on costs rather than rates allows the federal jurisdiction to help accomplish the goal of rate comparability without having to evaluate states' policy choices affecting those rates.[216]

Fundamentally, if a state has established high rates in its rural areas despite low costs in those areas, it should be the state's responsibility -- and only the state's responsibility --

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[214] *Qwest II*, 398 F.3d at 1237.

[215] *Verizon Communications v. FCC*, 535 U.S. 467 (2002).

[216] *Seventh Report and Order*, ¶ 32 (footnotes omitted).

to provide support. On the other hand, if a state deaveraged its current averaged rates, this might increase the likelihood of eligibility for support, but would not impact the amount of support.

Costs are determined according to the Commission's HCM. NASUCA must note that as previously discussed, the HCM itself is badly in need of updating and upgrading. Making improvements to the model should be a priority of the Commission regardless of the context in which the model is used. As also previously noted, the model should focus on national urban costs rather than national urban, suburban and rural costs combined as is done now.

As indicated in Section XIII.D., review of wire centers would be prioritized. Likewise in this step, the same priority would be observed. Thus wire centers that have rates above the benchmark but currently receive no support would be accumulated for each state and looked at first; wire centers that currently receive support but still have rates above the benchmark would be looked at by state next, and so on, until wire centers that get no current support and have rates below the benchmark can be addressed last.

Having had support calculated based on costs, the carrier will move on to Step Six. If a wire center does not qualify for support based on costs -- as many in the nation currently do not -- its state may nonetheless apply for support under the backstop mechanism.

H. STEPS SIX AND SEVEN: COMPARE CURRENT RATE MINUS PER-LINE SUPPORT TO THE BENCHMARK RATE

The Tenth Circuit required the Commission to demonstrate that its support mechanism based on costs would actually produce reasonably comparable rates.[217] In this step, NASUCA's proposal does just that.

The total amount of support based on costs for each wire center would be divided by the number of lines in that wire center.[218] That per-line support would be "deducted" from the basic service rate for each wire center to determine what the rate would be if the support were applied.

If the resulting rate is below the reasonable comparability benchmark, then the process is essentially over.[219] The federal fund will have provided enough support to allow rates that were not reasonably comparable to become reasonably comparable. It would be up to each state to ensure that the support is actually used to lower rates in the high-cost wire centers; a certification that this has resulted should be part of the annual state certification required by the Commission.[220] Alternatively, the Commission could simply directly require that this high-cost support -- specifically designed to produce reasonably comparable rural rates -- is actually and immediately used for that purpose.

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[217] *Qwest I*, 258 F.3d at 1202.

[218] Here the distinction would need to be made between residential and business access lines. Support focused on residential rates would be divided by the number of residential lines; support focused on business rates would be divided by the number of business lines. NASUCA's focus here is on residential rates.

[219] If the rate still remains above the reasonable comparability benchmark, then the state will have to resort to the backstop mechanism for additional support.

[220] See *Order on Remand*, ¶ 89.

I. IS A PHASE-IN (OR PHASE-OUT) NEEDED?

As with the first proposed alternative, NASUCA is unable to predict at this point the precise effect the second alternative will have on the high-cost funding received by the various states.[221] What is certain, however, is that support levels will change; some carriers in some states will be entitled to more funding than the current mechanism provides, and other carriers will be entitled to less funding than they currently receive. This is especially true with regard to carriers that receive IAS and ICL, which have nothing to do with rates and very little to do with the carriers' costs.

In order to prevent disruption for any carrier or its consumers -- and in the interests of gradualism as discussed in Section X -- NASUCA proposes that if current support levels per carrier per state vary from support levels based on the process set forth here by more than 20% (either higher or lower), a three-year transition to the new rate be allowed.

J. THE BACKSTOP MECHANISM FOR STATES

In the *Order on Remand*, the Commission adopted a mechanism to allow states to apply for "additional targeted federal support."[222] The existence of such a mechanism is a fundamental part of NASUCA's second alternative proposal, capable of being invoked by a state at any point in the process.

This backstop mechanism for the states will continue to be "based on a showing that federal and state action together are not sufficient to achieve reasonable

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[221] See Section IV, above for the current high-cost funding situation.

[222] *Order on Remand*, ¶¶ 93-96.

comparability of basic service rates in rural, high-cost areas served by non-rural carriers within the state to urban rates nationwide."[223] Further, it would be required that

> any request for further federal action fully explain the basis of the request, including a demonstration that the state's rural rates are not reasonably comparable to urban rates nationwide and that the state has taken all reasonably possible steps to achieve reasonable comparability through state action and existing federal support.[224]

Further, the burden should still "fall on the state to demonstrate the reasons underlying the failure to achieve reasonable comparability, because only the state is in a position to identify the existence and sources of problems that may be unique to that state."[225]

XV. NASUCA'S MECHANISMS SHOULD PRODUCE REASONABLY COMPARABLE RATES, SHOULD "PRESERVE" AND "ADVANCE" UNIVERSAL SERVICE, AND SHOULD YIELD A "SUFFICIENT" NON-RURAL HIGH-COST FUND.

The purpose of NASUCA's proposals is to meet the statute. NASUCA's first alternative proposal does so by establishing a rational national benchmark against which rural costs can be compared, in order to determine that rural rates are at realistic risk of not being reasonably comparable. By simplifying the process, and by recognizing the increasing use of the network for unsupported services, NASUCA's first alternative both preserves and advances universal service. And by supporting rural costs where the rates are at risk for becoming not reasonably comparable, the proposal should yield a fund that

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[223] Id., ¶ 93. The Commission also suggested that it could "modify calling scopes or improve quality of service where state commissions have limited jurisdiction." Id. It is not clear that the Commission would have jurisdiction to do either; granting additional federal support is unquestionably within the Commission's jurisdiction.

[224] Id.

[225] Id., ¶ 96.

is sufficient to meet its purposes.

NASUCA's second alternative proposal meets the statute in different ways. It is intended to achieve reasonably comparable rates in rural areas by examining those rates, and providing support directly to areas where the rates are not reasonably comparable and costs are high.[226] Thus NASUCA's proposal will not allow a "significant variance between rural and urban rates [to] continue unabated."[227] In addition, NASUCA's second mechanism will phase out current support that is not necessary to produce reasonably comparable rates, i.e., where if the support were removed the rates would still be reasonably comparable. Thus NASUCA's proposal meets the objectives of 47 U.S.C. § 254(b)(3). As discussed in Section VIII., above, "reasonable comparability" is the key goal for the high-cost universal service support mechanism.

NASUCA's second proposal will also "advance" universal service, as the statute requires.[228] This is done by gradually narrowing the range of reasonable comparability, such that as time goes by, support will be given to rural rates that are less divergent from the urban average than at the beginning.[229] It would also be done by broadening the definition of rural areas eligible for support.

Finally, NASUCA's second alternative proposal will also be "sufficient," as required by 47 U.S.C. § 254(e). *Qwest II* reversed the Commission's prior definition of

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[226] The backstop mechanism is available all throughout NASUCA's process, but especially at the end where, if cost-based support does not prove sufficient to produce reasonably comparable rates, a state may apply to the Commission for additional support that will achieve that end.

[227] *Qwest II*, 398 F.3d at 1236.

[228] See id. at 1235-1236.

[229] The *Qwest II* court noted that "preserve" and "advance" must be applied to the same aspects of universal service, rather than preserving one aspect (i.e., rates) while advancing another (i.e., technology). Id. at 1236. NASUCA's high-cost proposal applies both to rates. As discussed in Section XVI. next, however, NASUCA also has proposals for advancing universal service in other directions.

sufficiency first, because it failed to consider all of the § 254(b) principles[230]; second, because even under the Commission's inadequately-considered focus on reasonable comparability, the Commission was unable to show that its support mechanism produced the desired results[231]; and third, as just discussed, because the Commission did not assert that its mechanism advanced universal service.[232] Considering all the principles, both of NASUCA's proposed mechanisms will demonstrably result in reasonably comparable rates, and that universal service goal will be advanced through the process. Under these terms, the mechanisms will be sufficient for the purposes of the statute.[233]

XVI. OTHER MEANS OF "ADVANCING" UNIVERSAL SERVICE

Some have indicated that the goal of universal service has largely been met, principally because of the reported level of telephone subscribership. Yet as noted by NASUCA in a number of contexts, there are significant questions about the accuracy of the Commission's assessment of subscribership levels, based on recent reports that show significant decreases in subscribership.[234] One thing that the Commission can do to both preserve and advance universal service would be to expeditiously engage in a focused investigation into the accuracy of the subscribership reports. Clearly, it is impossible to

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[230] Id. at 1234.

[231] Id. at 1237.

[232] Id. at 1235-1236.

[233] NASUCA's review of areas currently receiving support in order to determine whether that support is needed to produce reasonably comparable rates will also ensure that the support is no more than sufficient. The *Qwest II* court did not object to the Commission's determination that support should be at levels only as large as necessary. Id. at 1234. Likewise, the dependence on state mechanisms discussed in Section XI. will help to ensure that the federal fund is no larger than necessary.

[234] See, e.g., CC Docket No. 96-45, NASUCA Comments on Joint Board High-Cost Proposals (September 30, 2005) at 2.

know whether universal service programs are working unless we know their impact on consumers.

The subscribership reports show declines in service at all income levels. Yet there apparently is a somewhat greater decline in subscribership among low-income consumers. The FCC has recently taken steps to increase the effectiveness of the Lifeline and Link-up programs that assist low-income consumers, through the joint Commission/NARUC/NASUCA task force.[235] Continuing these efforts will both preserve and advance universal service.

In another direction, however, there is one key opportunity to advance universal service, by bringing the rural networks of non-rural carriers into the 21st century. Under its statutory authority, the Commission can adopt a program to incent the deployment of broadband service in such rural areas. NASUCA proposes such a program, as follows:

A. The Network Investment Incentive Plan

NASUCA proposes that the Commission adopt a Network Investment Incentive Plan ("NIIP"). The plan provides for a glide-path that reduces support to carriers that fail to provide access to advance services. Thus, the plan meets the Tenth Circuit's concern that the Commission is responding to only one of the Act's universal service standards, comparable rates, and not to the other standards, such as comparable access to advanced services.[236] Moreover, the plan is responding to a growing body of evidence that confirms that non-rural carriers are not investing in the rural portions of their study areas.

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[235] See http://www.lifeline.gov/.

[236] *Qwest II*, 398 F.3d at 1236.

Even telecommunications executives recognize that the non-rural carriers do not have an incentive to invest in rural areas. For example, one executive recently intimated "that many telcos have chosen to milk the wireline network instead of investing in it."[237]

The NIIP proposes to reduce support to carriers that does not provide broadband service in rural wire centers. In the first year, the plan reduces per-line support to 90 percent of support that would otherwise be received on every line that does not meet the broadband quality of service requirement. That requirement is the ability to provide high-speed service (200 kbps in at least one direction). After the first year, support would be reduced according to the following schedule:

- 2nd year: 2 percent reduction to 88 percent funding;
- 3rd year: 3 percent reduction to 85 percent funding;
- 4th year: 4 percent reduction to 81 percent funding;
- Then continue the pattern for each succeeding year.

Having the plan accelerate the incentive over a period of years, provides for a small incentive in the first year and increasing higher incentive in the out years. This glide-path allows the carriers the opportunity to meet the requirement without causing excessive problems in planning, purchasing and engineering the new facilities. At the same time, carriers that refuse to provide adequate service will receive less support. In addition, the plan does not dictate the type of technology used to provide the service. Each carrier is free to choose fiber to the home, fiber to the node, ADSL over copper or any other technology that is capable of providing the required service quality level.

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[237] "Verizon Official Tells States More Reforms Needed to Spur Investment," TRDaily (February 14, 2006) at 2.

B. Recent evidence of Non-Rural Carrier failure to invest in the rural sections of their Study Areas

Evidence from a recent case in Maine, a Vermont state report and an academic study on broadband and universal service support that conclusion that non-rural carriers are allowing their rural wire centers to fall behind in provision of advanced services compared to either non-rural carriers' urban wire centers or the rural carriers' service territories.

First, in Maine, the President of Verizon-Maine has testified that a little over 65 percent of Verizon Maine's lines can provide ADSL service.[238] This statement acknowledges that over 34 percent of Verizon Maine's working lines cannot provide ADSL service. A significant contributing factor that reduces the availability of ADSL service in the Verizon Maine service territory is the existence of older Digital Loop Carriers ("DLCs") in the outside plant.[239] The older DLCs do not have the ability to split the communications arriving from the end-user between low frequency voice messages and high frequency data communications. Instead, these older digital loop carriers merely pass through the low frequency messages and block the high frequency data communications.[240] On the other hand, the Maine independent telephone companies,

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[238] *Investigation into Line Sharing Pursuant to State Law*, Maine Public Utilities Commission Docket No. 2004-809 ("Maine Line Sharing Docket"), Declaration of Edward Dinan (February 9, 2005), ¶ 11.

[239] Maine Line Sharing Docket, Direct Testimony of Robert Loube on behalf of the Office of Public Advocate (February 9, 2005) at 6-10.

[240] For a discussion of the different types of digital loop carriers see *In the Matter of Ameritech, transferor and SBC, Inc. Transferee*, CC Docket No. 98-141, Second Memorandum Opinion and Order (rel. September 8, 2000).

rural carriers serving mostly rural sections of Maine, can provide ADSL service to between 85 to 100 percent of their customers.[241]

Second, the Vermont Telecommunications Plan is a comprehensive report on the state of communications in Vermont combined with a set of policies, strategies and action plans. The report provides detailed maps of incumbent telecommunication carriers' service territories (Figure 2.2) and DSL coverage as of May 2004 (Figure 3.1).[242] A comparison of the maps clearly indicates that rural carriers are providing DSL service, while there are large portions of rural Vermont served by Verizon that do not have DSL service.

Finally, Professor David Gabel's paper, "Broadband and Universal Service," investigates the relationship between federal support for telecommunications and the provision of DSL capable lines.[243] Specifically he tests to determine if federal support raises the likelihood that a working line is capable of DSL service. His test separates the impact of federal support from the impact of other important economic, demographic and regulatory variables.[244] These variables include population density, consumer wealth, the size of the market, whether the line is in a Metropolitan Statistical area, whether the state has price-cap regulation, and the ratio of UNE loop price to the embedded cost of the loop. The paper analyzes two data bases, one that includes 2,000 wire centers across the

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[241] Maine Line Sharing Docket, Rebuttal Testimony of Robert Loube on behalf of the Office of Public Advocate (March 18, 2005) at 27-28.

[242] Vermont Telecommunications Plan, September 2004, Department of Public Service, www.state.vt.us/psd

[243] "Broadband and Universal Service," Dr. David J. Gabel, Queens College and Internet and Telecommunications Convergence Consortium, Massachusetts Institute of Technology (July 18, 2005), accessible at http://gullfoss2.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6518012421.

[244] Id., page 3-4.

Verizon East footprint, and the other is restricted to the Vermont including small companies in Vermont.

Dr. Gabel's results show that a DSL capable line is more likely to be found in urban areas. Second for non-rural carriers, he found that federal support is not statistically related to the provision of DSL capable lines. Thus, the paper concludes that "together these parameter estimates suggest that the Commission is failing to achieve the Congressional goal that access to advance telecommunications and information services in 'in rural, insular and high cost areas… should…[be] reasonably comparable to those services provide in urban areas…'"[245]

In his second statistical analysis, Dr. Gabel examined whether the existence of a cable competitor and whether the carrier participates in the NECA pools affects the deployment of DSL capable lines. These variables are in addition to the other variables listed above. This analysis was restricted to Vermont. Again, he finds that density is directly related to the provision of DSL lines and that the receipt of universal service HCM support has no impact on DSL deployment. In addition, he finds that the existence of a competitor also has no impact on the provision of DSL lines in rural areas.

However, he finds that carrier's membership in the National Exchange Carrier Association ("NECA") pools is directly related to the provision of DSL capable lines.[246] He notes that the members in the NECA pool are recipients of other types of universal service funding such as high cost loop, local switching support and interstate common line support. Thus, his study supports a conclusion that current universal service funding

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[245] Id., page 17 and 47 U.S.C. §254(b)(3).

[246] Id., page 22.

does affect the decisions of rural carriers to invest in advanced services but such funding does not affect the decision making of non-rural carriers.[247] Therefore, there is a need to change the incentives associated with providing universal service to non-rural carriers in order to address the problem of the lack of investment in high-speed and broadband facilities in the rural portions of non-rural carriers' study areas. This can be done as the NIIP provides, by providing a disincentive for failure to invest.

XVII. CONCLUSION

The Commission must arrive at a support mechanism for non-rural carriers that meets the requirements of § 254, or face rejection again in the courts. NASUCA has provided the Commission with sufficient data and legal and policy arguments to allow it to address the concerns of the Tenth Circuit. NASUCA has also presented the Commission with two alternative proposals for a legally-compliant non-rural high-cost mechanism. Both of the proposals -- in different ways -- meet the needs of the statute and would therefore result in a fund that is sufficient, as required by § 254(e).

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[247] Id.

Respectfully submitted,

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