NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION
The Voice of Rural Telecommunications
www.ntca.org

September 12, 2008

Ms. Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, S.W., TW-A325
Washington, D.C. 20554

Ex Parte Notice:

***In the Matter of Development of Nationwide Broadband Data,* WC Docket No. 07-38;**

In the Matter of
***Local Number Portability,* WC Docket No. 07-244;**
***Telephone Number Portability,* CC Docket No. 95-116;**
***Numbering Resource Optimization,* CC Docket No. 99-200;**

***In the Matter of NTCA Petition for Expedited Clarification and/or Limited Waiver of the Commission's Part 36 Rules,* CC Docket No. 80-286.**

Dear Ms. Dortch:

On Friday, September 12, 2008, Karlen Reed, Regulatory Counsel with the National Telecommunications Cooperative Association (NTCA), met with Greg Orlando, Legal Advisor to Commissioner Deborah T. Tate. We discussed NTCA's continued request that the Commission keep FCC Form 477 broadband reporting data confidential and refrain from imposing new broadband mapping requirements until the Commission reviews the new census tract data that will be available in March 2009.

NTCA renewed its opposition to shortening the four-business day intermodal number porting interval, and we discussed the merits of a one-year porting interval implementation period for small entities as defined by the Regulatory Flexibility Act. NTCA also highlighted portions of its August 29, 2008 Petition for Clarification and/or Waiver of Part 36 separations rules that would allow all rate-of-return carriers to directly assign USAC audit costs to the interstate jurisdiction. Attached are copies of the handouts disseminated during this discussion.

The discussions were consistent with NTCA's positions in previously filed comments and pleadings in the above-referenced dockets.

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Pursuant to Section 1.1206 of the Commission's rules, a copy of this letter is being filed via ECFS with your office. If you have any questions, please do not hesitate to contact me at (703) 351-2146.

Sincerely,

/s/ Karlen Reed
Karlen Reed
Regulatory Counsel, Legal and Industry

KR: rhb
Enclosures

cc: Greg Orlando

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

In the Matter of	)	
	)	
Jurisdictional Separations and	)	CC Docket No. 80-286
Referral to the Federal-State Joint Board	)	
	)	

NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION
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PETITION FOR EXPEDITED CLARIFICATION AND/OR LIMITED WAIVER OF THE COMMISSION'S PART 36 RULES

The National Telecommunications Cooperative Association (NTCA),[1] pursuant to 47 C.F.R. § 1.3, hereby petitions the Federal Communications Commission ("Commission" or "FCC") for an expedited clarification or limited waiver of the relevant portions the Commission's Part 36 separation rules so that all rate-of-return carriers may directly assign and allocate all costs associated with FCC Office of the Inspector General (OIG) and Universal Service Administrative Company (USAC) audits of the federal Universal Service Fund (USF) program to the interstate jurisdiction. Federal USF audit expenses are solely interstate in nature; consequently, it is appropriate that those expenses be allocated to the interstate jurisdiction.

[1] NTCA is the premier industry association representing rural telecommunications providers, established in 1954 by eight rural telephone companies. All of its members are full service local exchange carriers, and many members provide wireless, cable, Internet, satellite and long distance services to their communities. Each member is a "rural telephone company" as defined in the Communications Act of 1934, as amended (Act).

I. BACKGROUND

The Commission's Office of Inspector General (OIG), and the Universal Service Administrative Company (USAC), which administers the federal USF programs, have been conducting field audits of rate-of-return regulated incumbent local exchange carriers (ILECs) regarding their receipt of funds from the federal USF program. The OIG, in its "October 2007 Semiannual Report to Congress," said it had completed its first round of USAC audits of 459 randomly selected beneficiaries and contributors to the four USF programs: schools and libraries, low-income, rural health care and high-cost. The OIG stated in its "April 2008 Semiannual Report" that its second round of audits would cover 800 USF companies using outside contractor audit firms, and that it had received $21.5 million from USF funds in January 2008 to support the audits. The OIG reviews the USAC audits to detect potentially improper payments, which include overpayments and underpayments. The OIG is conducting these audits also in response to the Improper Payments Information Act (IPIA) of 2002, Public Law 107-300 (IPIA) (31 U.S.C. § 3122).

NTCA represents over 580 rural rate-of-return ILECs, most of which have been, are, or will be subject to the federal audits of their USF funding. These rate-of-return ILECs are required to comply with auditors' requests for information and documentation in a timely manner. From the carriers' standpoint, these audits are costly, both in terms of human resources and monetary expenditures. Several NTCA members have expressed their concerns over the costs of their federal USF audits, often ranging between $30,000 and $50,000. These costs directly affect the rates that rural customers must pay to receive service.

In accordance with Commission rules expenses related to federal USF audits are charged to Account 6720[2] and allocated per 47 C.F.R. §36.392, which reads in part as follows:

Sec. 36.392 General and Administrative--Account 6720.
(a) These expenses are divided into two categories:
(1) Extended Area Services (EAS).
(2) All other.
(b) Extended Area Services (EAS) settlements are directly assigned to the exchange operation.
(c) The expenses in this account are apportioned among the operations on the basis of the separation of the cost of the combined Big Three Expenses.[3]

Jurisdictional separations is "the process by which incumbent LECs apportion regulated costs between the intrastate and interstate jurisdictions."[4] The purpose of separating expenses between interstate and intrastate is to prevent regulated ILECs from recovering the same costs in both jurisdictions.[5]

The National Exchange Carrier Association (NECA) recently informed all cost company pool participants, including many NTCA members, that costs associated with USAC audits, whether consultant fees or company direct costs, should be booked to Account 6720 and allocated under Part 36 rules using the Big Three Expense allocator, with a portion (but not all) of the costs assigned to the interstate jurisdiction.[6]

Allocating a portion of federal USF audit expenses to the intrastate jurisdiction exposes the small rural ILECs to the possibility that their state public service commission may disallow the expense. Consequently, NTCA seeks the Commission's clarification and/or a waiver of the

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[2] 47 C.F.R. § 32.6720(c), providing accounting and financial services (including internal and external auditing), and 47 C.F.R. § 32.6720(d), maintaining relations with government, regulators, other companies and the general public and (d)(2), preparing and presenting information for regulatory purposes.
[3] 47 C.F.R. § 36.392. "*Big Three Expenses* are the combined expense groups comprising: Plant Specific Operations Expense, Accounts 6110, 6120, 6210, 6220, 6230, 6310 and 6410; Plant Nonspecific Operations Expenses, Accounts 6510, 6530 and 6540, and Customer Operations Expenses, Accounts 6610 and 6620." 47 CFR § 69.2(e); 47 C.F.R. § 36.112.
[4] *In the Matter of Jurisdictional Separations and Referral to the Federal-State Joint Board*, CC Docket No. 80-286, Order and Further Notice of Proposed Rulemaking (rel. May 16, 2006) (2006 Separations Order and FNPRM), ¶ 2.
[5] *Ibid.*
[6] NECA letter to Cost Company Pool Participants, dated June 4, 2008. "Absent a ruling by the FCC, there is no provision in Part 36 for directly assigning these costs to interstate."

Commission's Part 36 rules to allow rate-of-return ILECs to directly assign all federal USF audit costs to the interstate jurisdiction.

II. STANDARD OF REVIEW

The Supreme Court, in the 1930 case *Smith v. Illinois*, recognized that "procedures for the separation of intrastate and interstate property and expenses have been necessary for the appropriate recognition of authority between the interstate and intrastate jurisdictions."[7] The Supreme Court added that "[w]hile the difficulty in making an exact apportionment of the property is apparent, and extreme nicety is not required, only reasonable measures being essential, it is quite another matter to ignore altogether the actual uses to which the property is put."[8] The Commission has allocated regulated costs to one jurisdiction exclusively where the cost is used exclusively for either intrastate or interstate communications.[9] The allocation of costs for federal/state jurisdictional separation purposes involves judgment on a myriad of facts using reasonable measures.[10]

The Commission can waive any provision of its rules on its own motion and for good cause shown.[11] A rule can be waived "where the particular facts make strict compliance inconsistent with the public interest."[12] The Commission can "take into account considerations of hardship, equity, or more effective implementation of overall policy on an individual basis."[13] Furthermore, the Commission has said that "waiver is appropriate if special circumstances

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[7] *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133, 148 (1930) (*Smith v. Illinois*).
[8] Id. at 150-151; 2006 Separations Order and FNPRM), ¶ 2, n. 4.
[9] 2006 Separations Order and FNPRM), ¶ 4, fn. 11: "For example, the cost of private line service that is wholly intrastate in nature is assigned directly to the intrastate jurisdiction. *See* 47 C.F.R. § 36.154(a)."
[10] *Id.* at ¶ 18, fn. 44; *MCI v. FCC*, 750 F.2d at 141, *citing Smith v. Illinois*, 282 U.S. at 150; *Colorado Interstate Gas Co. v. FPC*, 324 U.S. 581, 589 (1945).
[11] 47 C.F.R. §1.3.
[12] *In the Matter of Jurisdictional Separations Reform and Referral t the Federal-State Joint Board*, CC Docket No. 80-286, Order (rel. June 26, 2001) (2001 Separations Freeze Order), ¶ 4.

[13] *Ibid*; *WAIT Radio v. FCC*, 418 F.2d 1153, 1157 (D.C. Cir. 1969), *cert. denied* 409 U.S. 1027 (1972).

warrant a deviation from the general rule, and such deviation would better serve the public interest than strict adherence to the general rule."[14]

III. GOOD CAUSE EXISTS TO PERMIT THE COMMISSION TO REMOVE HARDSHIP BY CLARIFYING AND/OR WAIVING ENFORCEMENT OF PART 36 RULES TO PERMIT RATE-OF-RETURN ILECS TO ASSIGN AND ALLOCATE FEDERAL USF AUDIT EXPENSES SOLELY TO THE INTERSTATE JURISDICTION, AND SUCH CLARIFICATION AND/OR WAIVER IS IN THE PUBLIC INTEREST.

NTCA asserts that allocating costs associated with compliance with federal USF audits to both interstate and intrastate jurisdictions would cause undue hardship on rate-of-return carriers, and would be contrary to the public interest, which would be better served by a waiver than by strict adherence to the general rule. For these reasons, good cause exists for granting the requested waiver.

Section 36.392 of the Commission's rules requires all General and Administrative costs, except EAS costs, to be separated based on the Big Three Expenses.[15] The Commission recognized that the General and Administrative costs associated with Extended Areas Services (EAS) are local exchange services that should be directly assigned to the exchange (intrastate) operation. Similarly, 47 C.F.R 36.412(c), relating to apportionment to taxes, provides: "Other operating taxes should be directly assigned to the appropriate jurisdiction where possible."[16] In like manner, since federal USF audits are associated with interstate operations, the Commission should directly assign costs incurred to comply with these audits to the interstate jurisdiction.

A. The Federal Universal Service Fund Is a Federally Administered Fund.

All costs incurred to audit a federal universal service fund should be directly assigned to the interstate jurisdiction. Furthermore, it is inappropriate for any costs incurred in conjunction

[14] *2001 Separations Freeze Order*, ¶ 4.
[15] 47 CFR § 69.2(e).
[16] 47 CFR §36.412.

with an audit of federal USF to be assigned to the intrastate jurisdiction. From both a common sense and a practical standpoint, it is reasonable and prudent that incurred costs be assigned to the cost causer. One of the fundamental principles underlying the Commission's federal-state separations procedures is apportionment of costs among jurisdictions is based on actual use or direct assignment.[17] The costs incurred to comply with USF audits, an undeniably interstate program, are clearly interstate in nature, and should be assigned as such.

B. States May Disallow That Portion Of OIG Audit Expenses Allocated To Intrastate Jurisdiction.

If part of a rate-of-return ILEC's federal USF audit costs is allocated to the state jurisdiction, the state could disallow them for state rate making purposes by declaring the costs as being clearly interstate in nature. The results of such a decision on the state level could deny the rate-of-return carrier appropriate recovery of its costs associated with federal USF audits.

Typically, rate-of-return carriers are smaller entities, and as such have smaller operating budgets than other carriers. All NTCA members are small carriers that are "rural telephone companies" as defined in the Telecommunications Act of 1996 ("Act"). While some offer local exchange service to as few as 44 lines and nearly 50% of NTCA members serve between 1,000 and 5,000 lines. Population density in most member service areas is in the 1 to 5 customers per square mile range. Having a portion of their costs incurred for compliance with federal USF audits disallowed by state authorities would cause rural rate-of-return ILECs a proportionally greater hardship than it would non rate-of-return carriers.

These USF audits are explicitly undertaken in order to identify fraud and waste, and the potential liability for audited carriers is not insignificant. Thus, carriers have no choice but to make the necessary expenditures to fully comply with all requests imposed by auditors. Clearly,

[17] 47 C.F.R. § 36.2(a)(1).

the ability to recover these non-trivial and certainly non-discretionary costs is critical, particularly for the smaller rate-of-return carriers. Should these carriers not be allowed to recover all of the costs spent on USF audits, their ability to serve their customers will be impaired, to the detriment of the public interest.

C. Federal USF Disbursements Are Treated As Interstate, Not Intrastate, Disbursements.

Disbursements from the federal Universal Service Fund are 100% allocated to the interstate (federal) side. To treat costs incurred in complying with federal USF requirements—namely, complying with requests imposed by USF auditors--as anything else would be inconsistent with the nature and origin of these costs and incompatible with accounting and ratemaking practices. Consequently, the Commission should allow rate-of-return ILECs to directly assign federal USF audit costs to the interstate jurisdiction.

IV. CONCLUSION

Good cause and the advancement of the public interest having been shown, NTCA respectfully requests that the Commission clarify and/or waive Section 36.392 of its rules for rate-of-return ILECs, specifically permitting them to directly assign and allocate USF audit costs to the interstate (federal) jurisdiction, as they are a direct result of the OIG and USAC federal USF audits and focus exclusively on the federal interstate jurisdiction.

Respectfully submitted,

NTCA
NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION
The Voice of Rural Telecommunications
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Economist

By: /s/ Daniel Mitchell
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August 29, 2008

CERTIFICATE OF SERVICE

I, Rita H. Bolden, certify that a copy of the foregoing Petition for Expedited Clarification and/or Limited Waiver of Part 36 Rules of the National Telecommunications Cooperative Association in CC Docket No. 80-286 was served on the 29th day of August 2008 by first-class, United States mail, postage prepaid, or via electronic mail to the following persons:

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REMINDER
Final 2007 Cost Studies due July 31, 2008

June 4, 2008

To: Cost Company Pool Participants

Final cost studies due by July 31, 2008
As stated in our March 14, 2008 letter, it is extremely important your **final cost study and required documentation** are received by your NECA region office no later than **July 31st and pooled by August settlement lock**. We continue to work closely with the FCC to assure confidence in our rates and earnings. Key to our success is timely submission of final cost studies. Adjustments are still allowed for errors and omissions to the extent the pool window is open.

In the past few years, we've seen a substantial increase in the number of companies submitting cost studies by the due date and we hope to see that trend continue. However, we will be forwarding to the FCC a list of exchange carriers who are not able to submit cost studies and required documentation by July 31st.

Recovery of USAC audit costs
Some of you have asked whether costs associated with USAC audits can be recovered in the cost study. Costs associated with the audit, whether consultant fees or company direct costs, are booked in Account 6720. These costs are allocated according to Part 36 rules using the Big 3 expense allocator and a portion of the costs are assigned to the interstate jurisdiction. Absent a ruling by the FCC, there is no provision in Part 36 for directly assigning these costs to interstate.

Reciprocal compensation
Costs associated with reciprocal compensation agreements should be reported in Account 6540, Access Expense, and assigned to the state/local jurisdiction. Associated revenues should not be netted with costs; the full amount of the revenues should be recorded in the appropriate 5200 account.

Universal Service Contribution (USC) and Federal Universal Service Charge (FUSC)
Interstate USC expense reported in account 6540 should equal the regulated FUSC revenue reported to settlements. As mentioned in our 2007 cost study letter, this amount must be separately identified in the cost study submission so it can be removed from ICLS calculations. We recently sent out additional information which can be found on NECA.org under member correspondence dated June 3, 2008.

RTB Stock
Companies need to report the pro-rata portion of gain on the stocks paid out at the end of 2007 (4.4¢ per share) if the costs of the initial shares were previously reported in the cost study as a reduction in revenue requirement. The gain realized should be recorded in account 7100, allocated on total plant in service and treated as income, reducing the net interstate revenue requirement. If the gain is recorded in an account other than 7100, the amount must be a separately identifiable reduction to revenue requirement allocated on total plant in service and you must identify the account used. Cost study taxes

calculated using the gross-up method should not separately reflect any change in the taxes associated with this gain. For more details, see our member correspondence dated January 17, 2008.

FIT Rate

Federal Income Tax calculated in the cost study should reflect the company's actual effective tax rate the company is using for IRS tax reporting purposes. Typically, only the largest holding companies, or companies filing on a consolidated basis, will use the maximum tax rate of 35%. If you are using a 35% tax rate, you may be asked to provide documentation supporting that tax rate.

Subchapter S companies should use an effective tax rate based on a composite of shareholders tax rates. NECA will accept cost studies using the statutory corporate rate only if it can be demonstrated that it is a close approximation of the aggregated individual shareholders' rates. Individual shareholder's rates should be based on operating pre-tax income allocated to individual shareholders.

Thank you for your cooperation! If you have questions, please contact your NECA Region Member Service Team.

Sincerely,

Carol A. Brennan

cc: Authorized Consultants