

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

In the Matter of)	
)	
High-Cost Universal Service Support)	WC Docket No.05-337
)	
Federal-State Joint Board on Universal Service)	CC Docket No. 96-45
)	
Lifeline and Link Up)	WC Docket No. 03-109
)	
Universal Service Contribution Methodology)	CC Docket No. 06-122
)	
Numbering Resource Optimization)	CC Docket No. 99-200
)	
Implementation of the Local Competition Provisions of the Telecommunications Act of 1996)	CC Docket No. 96-98
)	
Developing a Unified Inter-carrier Compensation Regime)	CC Docket No. 01-92
)	
Inter-carrier Compensation for ISP Bound Traffic)	CC Docket No. 99-68
)	
IP-Enabled Services)	WC Docket No. 04-36

**REPLY COMMENTS
OF THE ARIZONA CORPORATION COMMISSION**

I. Introduction

The Arizona Corporation Commission (“Arizona Commission”) is a constitutionally created agency with authority over the provision of telecommunications services in Arizona. The Arizona Commission submits these Reply Comments in response to the proposals contained in the Federal Communications Commission’s (“FCC”) Further Notice of Proposed Rulemaking (“FNOPR”) released on November 5, 2008. We appreciate the opportunity to comment on the reform proposals set forth in the Attachments to the FCC’s November 5, 2008 Order. We urge the FCC not to adopt the

proposals set forth in the Attachments to the FCC's Order without significant modification.

We commend the FCC for taking action to reform both the Federal Universal Service Fund and Intercarrier Compensation rules. Meaningful reform proposals in these areas should at a minimum encompass the following principles:

- 1) Similar classification and treatment for similar services;
- 2) More reliance upon State expertise and market knowledge in the areas of Intercarrier Compensation and Universal Service Support;
- 3) A clear understanding of the impact of the various reform proposals before they are adopted;
- 4) Fair treatment as between states, carriers and consumers of USF receipts and distributions;
- 5) Reliance upon State discretion as opposed to a one-size-fits-all reform approach; and,
- 6) Preemption only on a case by case basis where warranted.

The Arizona Commission's silence on an issue should not be construed as agreement with any particular proposal. There simply is not enough time to comment on all of the issues raised with respect to the comprehensive reform proposals. Finally, the Arizona Commission's comments are primarily in reference to the Chairman's Proposal contained in Attachment to the FNOPR.

The Arizona Commission's Reply Comments will focus upon the following three broad areas: (1) the appropriate regulatory treatment of IP¹-services; (2) reform of the federal universal service fund; and (3) reform of intercarrier compensation rules. We are particularly concerned with the degree of preemption of State Commission authority in these areas.

II. Regulatory Framework for IP Services

The appropriate regulatory framework for IP-based services is an area of utmost concern and importance to the Arizona Commission. In the *Pulver.com Order*², the FCC found that IP to IP based services³ were information services. In the *Vonage Order*⁴,

¹ Internet Protocol.

² *In the Matter of the Petition for Declaratory Ruling that pulver.com's Free World Dialup is Neither Telecommunications Nor a Telecommunications Service*, WC Docket No. 03-45, Memorandum Opinion and Order (Rel. February 19, 2006).

³ *Pulver.com* at para. 11 ("We conclude that FWD is an information service because FWD offers 'a capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications.' Through its server accessible over the Internet, FWD

which addressed VoIP interconnected to the Public Switched Telephone Network (“PSTN”), the FCC refrained from classifying the service as either an information service or a telecommunications service, but preempted State tariffing and CC&N requirements. Now, with respect to both nomadic and non-nomadic interconnected VoIP, both Attachments A (Chairman Martin’s proposal) and C (the Alternate Proposal) classify services that originate calls on IP networks and terminate them on circuit-switched networks, or conversely that originate calls on circuit-switched networks and terminate them on IP networks (collectively “IP/PSTN” services) as “information services.”⁵

Unfortunately, all this approach is likely to do is result in protracted litigation and harm consumers. Moreover, the Arizona Commission is uncertain why the FCC would want to undertake this extreme action which is so clearly inconsistent with federal and state laws and prior FCC orders. The Arizona Commission believes that it is critical that the FCC reconsider this portion of both Attachment A and C and classify “IP/PSTN” service as a “telecommunications service.”

The Chairman’s Proposed Finding That IP/PSTN Calls Should Be Classified As “Information Services” Is Not Supportable and Is Inconsistent With Past PSTN History.

The ACC cannot support the Chairman’s proposed finding that IP/PSTN calls should be classified as “information services”. The Chairman primarily bases his determination on an assumption that such traffic involves a net protocol conversion between end-users. However, no substantive discussion is provided to support this conclusion. In fact, the Arizona Commission believes that when IP/PSTN calls are compared to other technological changes that have occurred in the PSTN, such a determination is inconsistent with past history and is unsupportable.

This is especially the case with non-nomadic IP-based voice calling such as that which may originate and/or terminate on either: 1) IP networks such as those deployed by many cable companies and increasingly by LEC⁶s as softswitches are deployed as replacements for traditional circuit switches; or, 2) circuit switched networks.

The Arizona Commission views softswitches are just another of technological advancement of the PSTN. Over time, the PSTN has evolved from electromechanical switches to analog stored program control switches to digital switching and now to softswitches. Signaling has made similar advancements such as the transitions from E&M⁷ signaling to in-band signaling such as MF⁸ and then to out-of-band signaling

makes available to its members information that enables them to determine whether other members are available to talk; information on how to contact other members; and an optional voicemail capability that enables members to leave messages for unavailable members who have chosen this feature.”).

⁴ *In the Matter of Vonage Holdings Corporation*, Memorandum Opinion and Order, 19 FCC Rcd 22404 (Rel. November 12, 2004).

⁵ Appendix A at para. 209; Appendix C at para. 204. Appendix C (the Alternate Approach) appears to be the Chairman’s proposal (Appendix A) with some modifications as set forth in ex parte filings contained therein.

⁶ Local Exchange Carriers; may be either Incumbent or Competitive in this context.

⁷ A type of loop signaling for analog telephone circuits that utilizes separate wires or leads to signaling between network equipment.

such as SS7⁹. In addition, similar advancements have occurred in the transmission paths utilized to interconnect the switching nodes of the PSTN (for example, analog trunking to digital trunking to IP-based trunking)¹⁰. Protocol conversions¹¹ and the concept of gateways¹² have been inherent to this evolution of the communications network that is commonly referred to as the PSTN.

When a voice call is analyzed from an end-to-end perspective, the introduction of IP into the PSTN is just another technological advancement and simply not a basis for a regulatory reclassification of what is clearly a local exchange service from a Title II telecommunications service to an “information service”. By way of example, consider the following common examples of the types of interconnection and associated protocol conversion that could occur for a voice call.

1. Originating end-user over copper cable connected to a digital subscriber loop device connected to by a TDM DS-1 facility to a digital switch connected by SONET fiber facilities to a digital tandem connected by digital microwave to digital switch connected by fiber-to-the-home through a terminal adapter to the terminating end-user with all switches using SS7 signaling where the signaling and routing databases are located out-of-state.¹³
2. Originating end-user over copper cable connected to a digital subscriber loop device connected to by a TDM DS-1 facility to a digital switch connected by SONET fiber facilities to a digital tandem connected by digital microwave to a gateway to a softswitch connected by coax-to-the-home through a terminal adapter to the terminating end-user with all switches using SS7 signaling where the signaling databases are located out-of-state or IP-based routing.

From an end-to-end analysis perspective, just as the voice telecommunications service components in example 1 are governed by Title II so should the IP component in example 2 be Title II. Both examples make use of differing protocols throughout the call path and have signaling components that may involve out-of-state elements. It is obvious there is no basis for the voice service in example 2 to be classified as an “information

⁸ Multi-frequency signaling utilizes a pair of frequencies for communications between network switches.

⁹ Signalling System 7 employs a dedicated data circuit to carry packetized messages about each call connected between and among switches of the network. Earlier variations had a lower reference number; such as SS6 for example.

¹⁰ This overly simplifies the changes in transmission medium and protocols that may be utilized for the routing of a call depending upon the facilities interconnecting points within the network; for example, but not limited to, TDM, analog/digital microwave, fiber-based SONET, Ethernet, ATM, IP, etc.

¹¹ Generally, a protocol defines the rules governing the format and timing of messages that are exchanged between two devices. Thus protocol conversion permits devices with different protocols to communicate with each other.

¹² Generally an entrance or exit into a communications network. Gateways typically can perform protocol conversion between dissimilar networks and the routing (or switching) IP calls. Though the term gateway is more frequently used in reference to data networks, a line switch module in a digital circuit switch could also be considered as a gateway from an analog network into a digital network.

¹³ Intrastate local calls today may involve out of state elements but that has not been reason for such calls to be moved to the interstate jurisdiction. Similarly, it should not be a cause to classify VoIP calls differently.

service” and in example 1 as a Title II telecommunications service. A call in both of these examples begins as an analog voice call and terminates as an analog voice call from the perspective of the end users.

As the Arizona Commission stated in a January 11, 2006 filing with the FCC:

Analog, digital and soft switches coexist in the network and transparently deliver voice calls from one caller to another. Similarly the trunk facilities between switches have been some combination of analog, digital or even IP-based as technological change has occurred. As the network has evolved, many different combinations of these technologies and protocol conversions would have been utilized as calls were originated and terminated. Migration to an IP-based network is just one more step in the evolution of the network. Just as the regulatory classification of voice telecommunications did not change with these earlier forms of protocol conversion, use of IP protocol for voice service should not, of itself, necessitate a change in the form of regulation of the service.¹⁴

The critical question appears to be at what level does the protocol conversion take place. The Act and earlier Commission rulings suggest that the protocol conversion must take place so as to be apparent at the end user level; and would not encompass protocol conversions at the transmission level that have existed in the PSTN for years. Protocol conversions not apparent at the end user level have never before transformed a voice service from a “telecommunications service” into an “information service”.

The Arizona Commission recognizes there may be additional features above and beyond basic telephony service offered to end-users by a carrier that utilizes softswitches and an IP network. In those situations, the Arizona Commission believes the additional features could be viewed as vertical services and an independent determination made as to the proper regulatory treatment of them. This would be consistent with how the Commission and the states have viewed custom calling and Advanced Intelligent Network features for example.

The Chairman’s Proposed Finding that IP/PSTN calls are “information services” conflicts with earlier FCC orders which utilized the “integrated service” approach to classify a service as an “information” or “telecommunications” service.

In November, 2005, the Arizona Commission filed a petition for clarification and reconsideration in Docket No. 02-33, with respect to the proper regulatory classification of DSL service when combined with VoIP.¹⁵ We noted that where underlying DSL or internet access service is used to provide VoIP, then under the logic used by the FCC in

¹⁴ Arizona Corporation Commission Response to Oppositions/Comments of Verizon, AT&T, BellSouth and Qwest in Docket No. CC Docket No. 02-33 et al..

¹⁵ See Arizona Commission Petition for Clarification and/or Reconsideration, filed on November 16, 2005 in *In the Matter of: Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, et al.

its decisions leading up to *Brand X*¹⁶ and ultimately the logic underlying the Supreme Court's decision in *Brand X*, the "integrated" service should be classified as a "telecommunications service" not an "information service." This is because from the end user's perspective, the service is a telecommunications service, not an information service.

In *Brand X* (which cited extensively to the FCC's reasoning contained in its prior Orders and Reports), the critical point was the integrated character of the offering which the Court felt reasonably led the FCC to conclude that cable modem service was not a "stand-alone," transparent offering of telecommunications. *Brand X* at p. 2704.

At page 14 of the *Wireline Broadband Internet Access Service Order*, the FCC stated:

Applying the definitions of 'information service', 'telecommunications,' and 'telecommunications service,' we conclude that wireline broadband Internet access service provided over a provider's own facilities is appropriately classified as an information service because its providers offer a single, integrated service (i.e., Internet access) to end users.

In its Decision affirming the FCC, the Supreme Court at p. 2704 (citing para. of the FCC's Cable Modem Declaratory Order) looked only at the high speed wire's use in connection with Internet access and the information processing capabilities that it provides:

Seen from the consumer's point of view, the Commission concluded, cable modem service is not a telecommunications offering because the consumer uses the high-speed wire always in connection with the information-processing capabilities provided by Internet access, and because the transmission is a necessary component of Internet access: "As provided to the end user telecommunications it is part and parcel of cable modem service and is integral to its other capabilities."

As illustrated in the passage cited above, the service and functions the end-user obtained were also critical to both the Court and FCC in determining the ultimate classification of the combined, integrated service. In the Cable Modem Declaratory Ruling, the FCC stated at para. 38: "[c]onsistent with the analysis in the Universal Service Report, we conclude that the classification of cable modem service turns on the nature of the functions that the end-user is offered."

With internet access service, the consumer is receiving functions that the meet the definition of an "information service".

¹⁶ *National Cable & Telecommunications Association v. Brand X Internet Services*, 125 S.Ct. 2688 (June 27, 2005)("Brand X").

That is, like cable modem service (which is usually provided over the provider's own facilities), wireline broadband Internet access service combines computer processing, information provision, and computer interactivity with data transport, enabling end users to run a variety of applications (e.g., e-mail, web pages and newsgroups). These applications encompass the capability for 'generating, acquiring, storing, transforming, processing, retrieving, utilizing, or making available information via telecommunications,' and taken together constitute an information service as defined by the Act.¹⁷

With VoIP, the consumer no longer only uses the high-speed wire in connection with the information processing capabilities provided by Internet access. VoIP offers the end-user a transparent transmission path without any change in the form or content of the information. Further, the content or form of information conveyed is of the user's own choosing. The transparent ability to transmit information was a critical factor in distinguishing between "telecommunications services" and "information services" in the Supreme Court's discussion at p. 2710 of its *Brand X* decision (citing the Stevens Report at 11539, para 79):

The service that Internet access providers offer to members of the public is Internet access, (cite omitted), not a transparent ability (from the end user's perspective) to transmit information.

Under this line of cases, since VoIP is the functional equivalent of telecommunications service, the combined service (DSL plus VoIP) should be classified as a telecommunications service. "...[T]he statutory definition of 'telecommunications service' does not 'rest on the particular types of facilities used,..." *Brand X* at page 2703.

This is also supported by the FCC discussion at para. 19 of the Wireline Broadband Internet Access Services NPRM, wherein the FCC discussed at para. 19 the distinction between "telecommunications" and a "telecommunications service" which also supports classification of DSL combined with VoIP as a 'telecommunications service.'

Under this definition, an entity provides telecommunications only when it both provides a transparent transmission path and it does not change the form or content of the information. If this offering is made directly to the public for a fee, it is deemed a 'telecommunications service.' On the other hand, '[w]hen an entity offers subscribers the 'capability for generating, acquiring, storing, transforming, processing, retrieving, utilizing or making available information via telecommunications, it does not provide telecommunications, it is using telecommunications.

¹⁷ *Wireline Broadband Internet Access Service Order* at para. 14.

In summary, to the extent VoIP is combined with DSL, the combined offering should be classified as a telecommunications service. VoIP (IP/PSTN) should be classified as a telecommunications service.

The Chairman's Proposed findings that IP/PSTN calls are "information services" would work a tremendous disservice to consumers.

Classification of VoIP (IP/PSTN) calls as an "information service" would also work a tremendous disservice to consumers. By inappropriately classifying VoIP (IP/PSTN) calls as an "information service", the FCC will virtually eliminate all state oversight over the service.

There is really no difference from the consumer's perspective, between fixed and nomadic VoIP and traditional telephone service. Moreover, while the Commission uses its *Pulver.com Order* to support the classification of VoIP as an information service, there is really no connection or similarity between the two services. The FCC also cites to its *Vonage Order* to support its classification of nomadic and fixed VoIP as an "information service". But, the FCC did not classify Vonage's services as either a "telecommunications" service or "information" service in that Order. In addition, Vonage's services were nomadic in nature and the Court specifically noted that state preemption was only appropriate until classification of intrastate and interstate calls became possible. With fixed or non-nomadic VoIP, classification of intrastate and interstate calls is technologically possible, just as it is with traditional telephone service. And, since the FCC's IP 911 orders now require customers to provide their current service address for proper routing of 911 calls, with appropriate OSS enhancements, jurisdictional determination of calls could more easily be determined.

Because the telecommunications network is evolving to an IP based network at a rapid pace, if the Chairman's current finding stands, it will mean that State commissions will likely no longer regulate telecommunications services in the future. This would result in a very poor outcome for consumers. Further, the availability of State oversight would also depend upon the type of service the end-user utilizes under the Chairman's proposal. State consumer protection measures would be available to telephone customers utilizing traditional circuit-switched networks but not to consumers obtaining service through an IP based network. The outcome for consumers should not vary based upon the type of network that is used to provision service.

It is Congress' and the State Legislatures responsibility to determine the role State commissions are to play with respect to the provision of telecommunications services. Both Congress and the Arizona Constitution and Legislature have given the Arizona Commission responsibility over the provision of telecommunications within Arizona. Further, if a service falls under Title II, it should be subject to Title II protections. If a service does not fall under Title II, it should not be subject to Title II protections. There is no legal basis for the FCC to redefine the Act in such a manner which abrogates the important role afforded to States under the Communications Act. Effective regulation cannot be accomplished in this manner. The FCC's concern that State commissions will

impose economic regulation inconsistent with federal policy objectives can and should be addressed on a case-by-case basis.

The Chairman’s Proposal to classify IP/PSTN calls as “information services” is not competitively neutral.

Finally, the Chairman’s proposal to classify VoIP (IP/PSTN) calls as information services is not competitively neutral. It would result in the imposition of Title II requirements on some telecommunications services and providers but not others. It would also result in favoring one technology over another, which is also inappropriate.

For the above stated reasons, the Arizona Commission opposes the Chairman’s proposed finding that VoIP (IP/PSTN) calls should be classified as “information services” and instead recommends that the Commission instead find that IP-based voice services (in particular non-nomadic services) are a Title II telecommunications service subject to Commission jurisdiction for interstate calls and to State jurisdiction for intrastate calls.

III. Federal Universal Service Fund Reform

The Chairman’s proposed universal service fund reform proposals do not go far enough. While some of the Chairman’s proposals are commendable, others need further modification. If the Commission decides to adopt the Chairman’s universal service fund reform proposals, it should first make some significant modification to them.

The Chairman’s Broadband USF provisions are in need of modification.

Broadband Transmission should be the service subject to USF support (not Internet Access Service) and it should be classified as a “telecommunications” service in order to be eligible for Federal universal service fund receipts.

It is not clear that the FCC has the authority to include broadband service, when classified as an “information service,” within the definition of universal service or subject to subsidy from the Federal universal service fund. For instance, Section 254(c) of the Act provides that “Universal service is an evolving level of **telecommunications services** that the Commission shall establish periodically under this section, taking into account advances in telecommunications and information technologies and services.” (Emphasis added). That section of the Act goes on to provide:

The Joint Board in recommending, and the Commission in establishing, the definition of the services that are supported by Federal universal service support mechanisms shall consider the extent to which **such telecommunications services-**

- (A) are essential to education, public health, or public safety;
- (B) have, through the operation of market choices by customers, been subscribed to by a substantial majority of residential customers;

- (C) are being deployed in public telecommunications networks by telecommunications carriers; and
- (D) are consistent with the public interest, convenience and necessity.

Because the FCC has classified broadband as an “information service” in certain cases, the Act does not appear to envision its inclusion within the definition of services subject to subsidy from the fund. The Arizona Commission has consistently filed comments with the FCC since this issue arose advocating that broadband be classified as a “telecommunications service” since it very clearly falls within the definition of a telecommunications service. Moreover, classification of broadband as a “telecommunications service” would resolve many other issues that will continue to plague the FCC for years to come, until the appropriate classification is made. Carriers should not be able to pick and choose how a particular service will be classified under the Act. If the FCC chooses not to reconsider this issue, a carrier that chooses to classify broadband as an information service may not be entitled to Federal universal service fund receipts as the 1996 Act now stands.

Moreover, it is really the transmission service that should be subject to support. Once the transmission service becomes available, internet access services are available from multiple sources. Finally, the FCC should reconsider the required speed of the underlying transmission service in order for the service to be eligible for support.¹⁸ Currently the Chairman has proposed three tiers of broadband service. Basic Broadband Tier 1 refers to service with download speeds equal to or greater than 768 kbps but less than 1.5 mbps, and upload speeds greater than 200 kbps. The term Broadband Tier 2 refers to service with download speeds equal to or greater than 1.5 mbps and less than 3 mbps, and upload speeds greater than 200 kbps. Broadband Tier 3 refers to service with download speeds equal to or greater than 3 mbps, and upload speeds greater than 200 kbps.¹⁹ The FCC might consider the following to bring the United States closer to the speeds of broadband access that residents of other countries currently have available: Tier 1: download speeds less than or equal to 3 mbps and upload speeds less than or equal to 760 kbps; Tier 2: download speeds less than or equal to 10 mbps and upload speeds less than or equal 1.5 mbps; Tier 3: download speeds less than or equal to 20 mbps and upload speeds less than or equal to 3.0 mbps.

States should have a more predominant role in the broadband auction process since ETC status may be impacted.

In order to operate most effectively and achieve maximum benefit, the FCC’s reform measures should allocate oversight responsibility to the States when it makes sense. Right now, the reform measures do not do that.

With respect to the Chairman’s proposed reverse auctions for study areas unserved by broadband, the Chairman proposes to conduct a reverse auction for the right to receive high-cost support in an Unserved Study Area. Milestones will be established

¹⁸ Attachment A at para. 32.

¹⁹ Attachment A at para. 45.

for all ETCs receiving high-cost support and failure to achieve any milestone will result in loss of eligibility for support (and, where the FCC has jurisdiction over the designation of ETC status, loss of ETC status) for the service areas.

Consistent rules for all ETCs would appear to make the most sense, however, the support provided needs to be sufficient in order for ETCs to comply with any build-out requirements. Under the Chairman's proposal, a study area could conceivably end up with multiple networks, a situation that would not be in the public interest. An ETC could also under the Chairman's guidelines lose its high cost support. Since States have responsibility under the 1996 Act for designating most ETCs within their respective jurisdictions, States should make any determinations regarding carrier receipt of high cost support. Therefore, it would seem to be a better approach to allow the State the opportunity to carry out the actual auction process subject to the FCC guidelines. Under the Chairman's proposal, all ETCs must offer broadband Internet access service to all customers in their supported service areas as a condition of receiving universal service high-cost support.²⁰ Clearly, under the Chairman's proposal, ETC status is impacted, and thus States should therefore have the opportunity to carry out such auctions subject to FCC guidelines.

States should also have the ability to waive the milestones benchmarks for good cause shown, and set an alternative schedule. State commissions should have the ability to perform audits as well as the Inspector General. In this regard, State commissions should also have full access to all accounting systems, records, reports and source documents of the service providers and their employees, contractors, and other agents, in addition to all other internal and external audit reports that are involved, in whole or in part, in the administration of this program.

Finally, the States can perform other important roles to keep the size of the Federal fund in check as discussed below.

A permanent cap on universal service support is not an effective reform measure.

The Chairman proposes to place a permanent cap on the amount of universal service support that is distributed to carriers.²¹ In order to limit the growth of high-cost support, the Chairman proposes to cap the overall high-cost fund at the total amount of high-cost support disbursed by the Universal Service Administrative Company (USAC) for December 2008 on an annualized basis, net of any prior or past period adjustments.²² The Chairman also proposes to freeze each incumbent LEC ETC's individual, annual high-cost support at the amount of support, on a lump sum basis, that the ETC received in December 2008 annualized, net of any prior or past period adjustments, on a study area or service area basis.²³

²⁰ Attachment A at para. 22.

²¹ Attachment A at para. 16.

²² *Id.*

²³ *Id.*

It seems somewhat inconsistent for the Chairman to impose broad-based infrastructure requirements on ETCs, but then turn-around and cap the high-cost fund at current levels. It may be that such levels of funding are insufficient for some carriers to meet the build-out requirements established in Attachment A. Section 254(A) of the Act, requires that there be “specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.” It is not at all clear that this objective or requirement will be met under the Chairman’s proposal.

Moreover, a permanent cap raises other concerns. While the Chairman raises a legitimate concern regarding the size of the federal universal service fund and the need to contain its growth in the future, a permanent cap may not be the best way to accomplish this objective. A cap will essentially freeze in place current levels of support under the current rules using the current system. This is hardly “reform” in the true sense of the word. Moreover, a cap is indiscriminate in its operation. It will benefit certain states and providers over others. For instance, some states may have been more aggressive in designating competitive ETCs than other states. The more aggressive states will receive greater USF receipts in the future. State USF receipts should be based upon need and should be fair as between the various states and carriers.

The Arizona Commission believed the cap to be an interim step until true reform could be achieved. An indiscriminate cap is not an effective reform measure. Growth of the fund should be constrained in ways which still allow for sufficient support. A cap may not do this.

State involvement in ensuring need and accountability for funds received is a better reform proposal than an indiscriminate cap.

Rather than a cap on the overall high-cost fund and a cap on each incumbent LEC ETC’s individual annual high-cost support, on a lump sum basis, that the ETC received in December 2008 annualized, the FCC should consider increased State involvement on funds designated for particular carriers to ensure that there is a need for the funds and that the carrier is held accountable for its expenditures. This type of measure would be better than an indiscriminate cap which will only operate to freeze existing levels of support without regard to need and further will result in some carriers not receiving sufficient support as required under the 1996 Act. Alternatively, the FCC could allocate funds on a per state basis based upon the number of high costs access lines in each state. The State commission could determine need for those funds which would ensure that only carriers in need of the funds would receive them.

In addition, States could play a role in ensuring that the requirement in the Federal Act to ensure comparability between local rates in rural areas and urban areas. Section 254(b)(3) provides in this regard:

“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.

The Chairman's proposal does not provide any role for State commissions in this regard.

The numbers-based contribution methodology proposed by the Chairman is not limited to interstate services or providers.

The numbers-based contribution methodology proposed by the Chairman has no relationship to the provision of interstate services contained in Section 254(d) of the Act. That Section states in part:

Every telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, to the specific, predictable and sufficient mechanisms established by the Commission to preserve and advance universal service.

The existing contribution methodology seems sufficient and more closely tracks the statutory requirement that the federal fund target interstate services. Another concern with such a drastic change in the contribution methodology is that there was nothing in Attachment A to indicate what the impact of such a change would be. Before the FCC proceeds with this drastic change, it should obtain information on what impact this new contribution methodology would have.

There was also no discussion by the Chairman in his Attachment A as to the impact of a numbers based contribution methodology upon State universal service funds. Does the use of a numbers based contribution methodology make it more likely that any State funds will burden the federal universal service support mechanism, something the Act prohibits. Thus, will this action have the inadvertent effect of discouraging State funding mechanisms, a result that would not be in the public interest.

The subsidies provided, whether by way of the Federal Universal Service Fund or the Subscriber Line Charge ("SLC") should be discretionary. Their application should be studied and ways to make their impact more competitively neutral should be examined.

In addition, there are issues with respect to exclusion of numbers and the Chairman's proposal being inconsistent with network resource optimization in some respects, which need to be reviewed in the comprehensive reform proposal that is ultimately adopted.

IV. Intercarrier Compensation Reform

The Arizona Commission agrees that the existing system of intercarrier compensation is in dire need of reform. However, the Arizona Commission has concerns with the intercarrier compensation reform proposals of Chairman Martin because they appear to be premised in large part upon preemption of State commission authority over intrastate access and reciprocal compensation rates.

The intercarrier compensation reform proposal of Chairman Martin is premised upon a reading of Section 251(b)(5) and 252(d) of the Act that is once again the subject of appeal.

Chairman Martin has premised his comprehensive intercarrier compensation reform proposal upon a reading of the Act that would require the payment of reciprocal compensation for all forms of traffic in the future. This new interpretation by the FCC of Sections 251(b)(5) and 252(d) of the Act is already the subject of appeal. Before proceeding with comprehensive reform based upon its reading of the Act offered up in response to the Core Mandamus Petition relating to ISP-Bound traffic, the FCC might want to wait and see if it's most recent interpretation is upheld.

Attachment A's proposal is a one-size-fits-all approach which would impose a uniform rate on all traffic regardless of the costs involved.

The proposal contained in Attachment A to the FNOPR for intercarrier compensation reform consists of a ten-year transition plan, with separate stages, designed to reduce rates over a period of time. At the end of the transition period, all telecommunications traffic would be treated as if it fell within the reciprocal compensation provisions of section 251(b)(5) of the Act and States would set the default reciprocal compensation rates pursuant to a new methodology established by the FCC.

More specifically, in the first stage, intrastate access rates would be reduced to interstate levels. During stage 2, carriers would reduce their rates to an interim uniform termination rate, set by the state. During stage 3, the rates carriers charge at the end of stage 2 will be gradually reduced to the rates that will apply at the end of the transition period.

One year after the effective date of the FCC's Order, all LECs would be required to reduce their terminating intrastate switched access rates by 50 percent of the difference between their intrastate switched access rates and their interstate switched access rates.

Within 2 years from the effective date of the FCC's order, states must adopt a state-wide interim, uniform reciprocal compensation rate applicable to all carriers. Three years from the effective date of the FCC's order, the FCC requires that all LECs reduce their terminating rates by 50 percent of the difference between their current terminating rate and the interim, uniform reciprocal compensation rate established by the state. Four

years from the effective date of the FCC's order, all LECs must reduce their terminating rates by the remaining 50 percent of the difference between their current terminating rate and the interim, uniform reciprocal compensation rate established by the state so that their terminating rates equal the state-set interim uniform reciprocal compensation rate. This rate will then become the starting point for stage three-a six-year gradual downward transition to the final uniform reciprocal compensation rate.

The Arizona Commission does not support the adoption of a one-size-fits-all approach with respect to the establishment of reciprocal compensation rates. The rates established by the state commission should reflect the costs of providing the service for the particular carriers involved. At a minimum, there should be a distinction between rural carriers and larger urban providers.

Further, the Arizona Commission is concerned because there has been no determination made as to the impact upon this sweeping proposal upon affected carriers and the likely impact upon the universal service fund and local service rates.

Attachment A's comprehensive reform proposal inappropriately preempts State authority over intrastate access rates.

The FCC does not have authority over intrastate access rates. Nor does the FCC have authority over the establishment of rates for reciprocal compensation.

Section 152 of the Act reserves State authority over intrastate rates and services:

Nothing in this Act shall be construed to apply or to give the Commission jurisdiction with respect to (1) charges, classifications, practices, services, facilities, or regulations for or in connection with intrastate communications service by wire or radio of any carrier.

By rolling intrastate access charges into Section 251(b) of the Act, the Chairman purports to suddenly obtain authority to establish rates for this intrastate service. However, this is not a plausible reading of Section 251(b)(5), Section 251(g) or Section 252(d) of the Act.

At one time, the FCC had before it several different intercarrier compensation reform proposals. While the Arizona Commission had concerns with each of those individual plans standing alone as did many other parties; each of those plans had some provisions that were worthy of consideration. The Chairman's proposal does not give any consideration to individual provisions in those plans which may be in the public interest.

Attachment A's comprehensive reform proposal for intercarrier compensation does not give the States sufficient discretion to set rates based upon costs and to preserve affordable local service rates

As NARUC noted in its Comments at page 11, Attachment A's approach:

“illegally constrains State retail rate design options and restricts States' ability to set intrastate rates based solely upon State-determined reasonable costs of service. It also requires a prior and significant adjustment of the FCC's separations rules. But legal infirmities aside, the policy problems associated with expanding Section 251(b)(5) reciprocal compensation to encompass State intrastate access charges are obvious. Any approach that effectively eliminates intrastate access charges, on its face, undermines State universal service policies and will cause a cascading series of implementation problems for many States.

The FCC should reexamine several of the earlier proposals and select provisions which allow State commissions considerable discretion in revamping intrastate intercarrier compensation rates. A one-size-all-approach while attractive because of its simplicity, will not work.

V. Conclusion

The Arizona Commission appreciates the opportunity to offer comments on the Chairman's comprehensive reform proposals. We reserve the right to supplement these comments and offer further perspectives on these important issues as they continue to be discussed and examined.

RESPECTFULLY submitted this 22nd day of December, 2008.

/s/ Maureen A. Scott

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