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

In the Matter of	)	
	)	
Jurisdictional Separations and Referral to the Federal-State Joint Board	)	CC Docket No. 80-286
	)	DA 09-623
Petition Filed by National Telecommunications Cooperative Association for Clarification and/or Limited Waiver of the Commission's Part 36 Jurisdictional Separations Rules	)	
	)	

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

NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION
REPLY COMMENTS

Respectfully submitted,

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May 5, 2009

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NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION
REPLY COMMENTS

The National Telecommunications Cooperative Association (NTCA)[1] responds to the initial comments filed April 20, 2009, regarding the Federal Communications Commission's (Commission's or FCC's) March 19, 2009 Public Notice seeking comment on NTCA's August 29, 2008, petition for clarification and/or limited waiver of the Commission's Part 36 Jurisdictional Separation rules (Petition).[2] Every commenter save one agrees that rate-of-return (ROR) carriers should be allowed to directly assign and allocate to the interstate jurisdiction all costs associated with FCC Office of the Inspector General (OIG) and Universal Service

[1] NTCA is the premier industry association representing rural telecommunications providers. Established in 1954 by eight rural telephone companies, today NTCA represents over 585 rural rate-of-return regulated incumbent local exchange carriers (ILECs). 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). NTCA members are dedicated to providing competitive modern telecommunications services and ensuring the economic future of their rural communities.

[2] *Comment Sought on a Petition Filed by National Telecommunications Cooperative Association for Clarification and/or Limited Waiver of the Commission's Part 36 Jurisdictional Separations Rules*, CC Docket No. 80-286, DA 09-623, Public Notice (rel. Mar. 19, 2009). NTCA silence on any positions or proposals raised by other commenters in this proceeding connotes neither agreement nor disagreement by NTCA with those positions or proposals.

Administrative Company (USAC) audits of the federal Universal Service Fund (USF) program.[3] Only Verizon disputes the request, and the foundation for that challenge is without merit. Consequently, the Commission should grant NTCA's Petition.

I. MOST COMMENTERS AGREE WITH NTCA THAT RATE OF RETURN ILECS NEED TO RECOVER FEDERAL USF AUDIT EXPENSES FROM THE INTERSTATE JURISDICTION THROUGH THE SEPARATIONS PROCESS.

Many small rural ROR ILECs, including NTCA members, are feeling the pain of bearing the increasing audit-related expenses caused by USAC and OIG audits of the high-cost and low-income portions of the USF. More than 50% of NTCA's ROR members serve between 1,000 – 5,000 access lines, and the average population density per square mile in most NTCA member service areas is between 1 – 5 customers per square mile.[4] All NTCA members are regulated local exchange carriers and many offer video, wireless, satellite and/or long distance services to their rural customers.

Many NTCA rural members have reported a significant jump in their USAC / OIG audit expenses due to the federal government's enhanced and expanding efforts to detect and deter waste and fraud in the federal USF program. NTCA's informal member survey reveals that per audit expenses have run between $30,000 and $50,000 apiece.[5] The Missouri Small Telephone Companies (Missouri Companies) confirmed in their comments the level of audit expense,

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[3] Alexicon Telecommunications Consulting (Alexicon) Comments, pp. 2-3; GVNW Comments, p. 2; Missouri Small Telephone Companies (Missouri) Group Comments, p. 1; Telcom Consulting Associates, Inc. (TCA) Comments, p. 1.

[4] 2008 NTCA Broadband/Internet Availability Survey Report, p. 5, available at: http://www.ntca.org/images/stories/Documents/Advocacy/SurveyReports/2008ntcabroadbandsurveyreport.pdf.

[5] National Telecommunications Cooperative Association, *Petition for Expedited Clarification and/or Limited Waiver of the Commission's Part 36 Rules*, CC Docket No. 80-286, Filed August 29, 2008 (NTCA Petition), p. 2.

noting that one of the companies incurred $47,800 in audit expenses for the most recent audit.[6] The Missouri Companies assert accurately that small rural telcos spend significant employee time and company resources to comply with the federal/interstate USF audits, yet 35% of the audit expense is potentially unrecoverable as that portion would fall to the intrastate jurisdiction under the FCC's accounting rules.[7] The Missouri Companies confirmed that some of them have incurred USAC audit costs in the $30,000 to $50,000 range, so roughly $17,500 per audit is at risk due to allocation to the intrastate jurisdiction.[8] "These costs are substantial for small rural carriers such as the [Missouri] companies, and such costs should be accounted for correctly," according to the Missouri Companies.[9]

The ROR ILECs do not challenge the need for audits and have attempted to comply with the numerous demands for documentation and information production within an extremely short time frame. The mounting financial burden of these federal audit expenses, however, should be fairly allocated to the federal interstate jurisdiction for jurisdiction separations purposes, and not separated according to the Big Three expenses under Account No. 6720 and allocated per 47 C.F.R. § 36.392, as is currently done.

Commenters who help ROR carriers prepare and respond to USAC and OIG audits of USF funds agree with NTCA that the current allocation method of OIG audit expenses for USF programs must change. Alexicon, a consultant for small rate-of-return ILECs serving rural, insular and Native American tribal lands, noted that ROR ILECS have been experiencing

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[6] Missouri Companies Comments, p. 2.

[7] *Ibid*.

[8] *Ibid.*

[9] *Ibid*.

"substantial increased FCC OIG audit-related expenses."[10] GVNW, another management consultant that represents small rural ROR ILECs, also supports NTCA's Petition. GVNW cites Commission precedent which allows clarifying the role of direct assignment, which was done by the Common Carrier Bureau's August 21, 1991 Letter of Interpretation (DA 91-1059) and in the April 11, 1986 Average Schedule Order (cost studies that are wholly interstate are compensable from interstate ratepayers).[11] TCA, another ROR ILEC consultant, notes that "for small rural LECs, these audit costs are substantial…Because these audit-related costs are a direct result of a federal action(,) that responsibility should not fall to the state jurisdiction, but should remain entirely with the cost causer—the federal jurisdiction."[12] These consultants, who have participated in the actual OIG audits by assisting their ROR clients, are well-acquainted with the detailed level of documentation and investigation that USAC and the OIG auditors seek. These consultants are also on the front-line for hearing the ROR's concerns about not being able to recover the costs of these federal expenses.

II. VERIZON'S OBJECTIONS TO THE PETITION ARE MERITLESS.

The only commenter who questioned the merits of NTCA's petition was Verizon, a vertically integrated telecommunications company with operating revenues of $97.3 billion and operating income of $16.9 billion in 2008. Verizon has approximately 36 million wireline access lines and more than 8 million broadband connections, and, through Verizon Wireless, more than

[10] Alexicon Comments, p. 2.

[11] GVNW Consulting Comments, p. 3.

[12] TCA Comments, p. 2.

72 million wireless subscribers nationwide.[13] Verizon's perspective as the largest telecommunications provider in the United States is understandably different from that of the small rural ROR ILEC; indeed, they are on opposite ends of the scale on this issue. As a price-cap carrier and alternative regulation carrier with major market power, Verizon can seek recovery through exogenous cost recovery mechanisms for costs and has the ability to spread out costs over millions of customers. Recovering $17,500 per audit through separations has virtually no bearing on Verizon's bottom line. For small rural ROR companies, however, these audit expenses are significant, especially when small rural ROR companies are striving to use available funding to extend and enhance broadband throughout their service territories. For these reasons, the FCC should grant this Petition.

A. Federal USF Audit Expenses Belong To the Interstate Jurisdiction.

Verizon's primary objection to the Petition concerns whether the federal USF audit expenses should be allocated solely to the federal jurisdiction. Verizon contends that federal USF subsidies are used to support both interstate and intrastate services and claims that apportionment of federal USF audit expenses is therefore appropriate.[14] Verizon notes that the USF is a collaborative federal-state program, with the state PUCs designating who receives USF support and the FCC gathering and distributing that support.[15]

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[13] Verizon Communications, Inc., United States Securities and Exchange Commission Form 10-K Filing, Fiscal Year Ended December 31, 2008, http://investor.Verizon.com/SEC/sec_frame.aspx?FilingID=6435582.

[14] Verizon Comments, pp. 2-3.

[15] *Id.*, pp. 3-4.

Verizon is quite cognizant of the USF program as it received $165.7 million in USF support in 2008 from the low-income portion and $221.5 million in the high-cost portion.[16] Verizon's USF services/audit cost analogy, however, ignores the fundamental source of the expense, which is the federally-mandated (not state-mandated) audits. As Alexicon indicates, Part 36.2(a)(1) specifically states, "Separations are intended to apportion costs among categories or jurisdictions by actual use or by direct assignment."[17] The federal OIG audits are causing the expense, so the audit expenses should be allocated and assigned to the interstate jurisdiction. TCA also refutes Verizon's position, contending that federal USF (FUSF) audits "are directly related to ensuring waste or fraud does not occur by recipients of the FUSF, not state universal service funds," with state public utility commissions responsible for auditing state high-cost funds.[18] "One of the foremost underlying principles of the federal-state separations procedures," TCA rightly asserts, "is the apportionment of costs among the jurisdictions based on actual use or direct assignment."[19] Fairness, equity and proper cost recovery mandate direct assignment of federal USF audit costs to the interstate jurisdiction.

B. Enhanced Federal Enforcement Through OIG Audits Greatly Increased Small Rural Companies' Audit Expenses.

Next Verizon contends that no need exists to change the historical treatment of USAC audit expenses.[20] Verizon admits that the USAC audit activity has increased recently, but surely

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[16] Universal Service Administration Corporation website: low-income, www.usac.org/li/telecom/step07/disbursement-tool.aspx; high-cost, www.usac.org/hc/tools/disbursements/default.aspx.

[17] Alexicon Comments, p. 3.

[18] TCA Comments, p. 1.

[19] *Ibid.*

[20] Verizon Comments, p. 4.

the need for change has arisen due to the increased expense of the audits. Indeed, 14 Congressmen recognized this growing expensive burden on rural ILECs in their April 9, 2009 letters to Chairman Serrano and Ranking Member Emerson of the House Financial Services and General Government Appropriations Subcommittee. (Copies of these letters are attached to these reply comments.) The Congressmen expressed their deep concerns about "the striking cost of an audit initiative … which appears to be deriving little public benefit."[21] They also note that USAC itself has outlined the extreme costs placed in the USF program by the OIG audits. "More than $192 million will have been spent on this wide-ranging audit initiative by the end of FY 2009."[22] These Congressmen have characterized the OIG audit process as creating "extreme financial costs" because it implements a "costly attestation style audit process."[23] Clearly the costs of federal OIG USF audits have increased greatly, and small ROR carriers are those most affected.

C. Intrastate Recovery of Federal Audit Expenses Would Increase the Regulatory Burden on Small Rural ROR Companies.

Requiring rate-of return carriers to recover Federal USF audit expenses from both the interstate and intrastate jurisdictions requires small rural ROR ILECs, who are already under increased economic strains, to incur additional time and expense seeking intrastate recovery through rate cases or earnings reviews. TCA observes that intrastate cost recovery mechanisms, including rate cases, not only "usually impose a significant regulatory burden" but intrastate

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[21] Letter from 13 Congressmen to The Honorable Jose E. Serrano and The Honorable Jo Ann Emerson, April 9, 2009 , p. 1 (13 Congressmen Letter); Letter from Congresswoman Stephanie Herseth Sandlin to The Honorable Jose E. Serrano and The Honorable Jo Ann Emerson, April 9, 2009, p. 1 (Rep. Sandlin Letter). (Both letters are attached to these reply comments.)

[22] *Ibid.*

[23] 13 Congressmen Letter, p.1; Rep. Sandlin Letter, p. 2.

jurisdiction recovery cannot automatically be assured.[24] Disallowance by the state public utility commissions would force rural ILECs to absorb these costs, thus reducing revenues and potentially delaying broadband investment and upgrades. TCA also accurately asserts that most recovery mechanisms are prospective, so there would be unrealistic chances for recovery of paid expenses.[25]

Verizon chooses to ignore the cost of seeking state recovery which imposes its own unreasonable burden on small ROR carriers. Alexicon asserts that it is highly unlikely that any state regulatory agency will allow pass-through of OIG/USAC audit-related interstate costs to their intrastate ratepayers, leaving ILECs with unrecovered costs.[26] NTCA agrees. The state procedures for rate cases are heavily time-consuming and expensive in their own right. Small rural rate-of-return carriers are faced with the daunting prospect of either initiating a rate case or else bearing the increasing burden caused by not being able to recover federal audit expenses.

D. OIG Audit Expenses Are Beyond the Control of ROR Carriers.

Another misconception contained in Verizon's approach is that ROR carriers' compliance with USF programs "is solely within their control," so the federal audit costs should not be shifted to interstate access rates.[27] Anyone who has closely examined the OIG/USAC document request letters can tell that the production of required information is an enormous burden and the ROR companies have no control over the questions asked. TCA explains that audit costs include fees for attorneys and outside consultants who are used to meet deadlines and

[24] TCA Comments, p. 2.

[25] *Id.*, pp. 2-3.

[26] Alexicon Comments, p. 2.

[27] Verizon Comments, p. 4-5.

document/info production requests. "These audit costs are substantial and largely uncontrollable," asserts TCA.[28] NTCA agrees. The burden of responding to these federal questions should fall squarely on the interstate jurisdiction, so the shift is completely and correctly justified. As Alexicon correctly contends, waiver of the Part 36 separations rule is appropriate because strict compliance is inconsistent with the public interest.[29]

E. Allowing Interstate Allocation of Federal Audit Expenses Reduces Regulatory Uncertainty and Promotes Efficiency.

Another unsupported portrayal is Verizon's view that allowing ROR ILECs to directly allocate and assign the federal audit USF expense to the interstate jurisdiction "would provide a disincentive for these carriers to operate efficiently and would not result in better compliance with USF program rules."[30] Precisely the opposite is true – allowing ROR companies to recover the costs through interstate access rates is far more efficient from an economic standpoint because the expenses are caused by the federal audits. The Missouri Companies astutely note that regulatory lag and uncertainty will be precluded if audit costs are allocated to the interstate jurisdiction.[31] Recovering those expenses fully will permit small rural ROR ILECs to better build out and maintain their networks, bring broadband to rural communities, and meet the growing demands of full-service telecommunications providers in the remote rural areas where Verizon and others have chosen not to provide service. Full recovery from the interstate jurisdiction is needed and merited, so the Commission should grant the Petition.

[28] TCA Comments, p. 2.

[29] Alexicon Comments, p. 4.

[30] Verizon Comments, p. 5.

[31] Missouri Companies Comments, p. 3.

F. The Overall Policy Decision Regarding Continuation of the Separations Process Should Not Impact Consideration of NTCA's Petition.

Finally, Verizon's diatribe against the concept of separations requirements in Part 36 rules is a distraction from the key issues presented in the Petition. Verizon is fully aware that the separations freeze expires June 30, 2009, and that the Commission has sought comment on whether to extend the freeze.[32] Several commenters in that pending docket (CC Docket No. 80-286) have urged the Commission to eliminate separations, while others (including NTCA and a host of others) have asked the Commission to extend the separations freeze at least one year after the Commission completes its USF and intercarrier compensation reform efforts.[33] The issue of whether to discontinue the separations process will not be resolved any time soon. Given that the Commission has not indicated when it will decide whether and how to revise the separations rules, it becomes increasingly important that the Commission relieve the small ROR carriers who are suffering from the burden of unrecovered audit expenses now, rather than later. ROR regulation is very meaningful today and the separations rules are still completely relevant. The recovery requested in this petition is not "piecemeal modification" but a necessary change to help small rural ROR companies.

[32] *Jurisdictional Separations and Referral to the Federal-State Joint Board*, CC Docket No. 80-286, Notice of Proposed Rulemaking, 74 Fed Reg. 15236 (2009) (NPRM).

[33] Joint Comments of NECA, NTCA, OPASTCO, ERTA and WTA, *In the Matter of Jurisdictional Separations and Referral to the Federal State Joint Board*, CC Docket No. 80-286, filed April 17, 2009, p. 1.

III. CONCLUSION.

For these reasons, the Commission should grant NTCA's Petition and allow all rate-of-return carriers to directly assign and allocate all costs associated with OIG and USAC audits of the federal USF program to the interstate jurisdiction through the Part 36 separations rules.

Respectfully submitted,

NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION

By: /s/ Daniel Mitchell
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By: /s/ Karlen Reed
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May 5, 2009

CERTIFICATE OF SERVICE

I, Adrienne L. Rolls, certify that a copy of the foregoing Reply Comments of the National Telecommunications Cooperative Association in CC Docket No. 80-286, FCC 09-24, was served on this 5th day of May 2009 by first-class, United States mail, postage prepaid, or via electronic mail to the following persons:

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Congress of the United States
Washington, DC 20515

April 9, 2009

The Honorable José E. Serrano
Chairman
House Appropriations Subcommittee on Financial Services
B-300 Rayburn HOB
Washington, D.C. 20515

The Honorable Jo Ann Emerson
Ranking Member
House Appropriations Subcommittee on Financial Services
1016 Longworth HOB
Washington, D.C. 20515

Dear Mr. Chairman and Ranking Member:

We write to express our deep concern regarding the striking cost of an audit initiative of the Universal Service Fund (USF) that is underway at the direction of the Federal Communications Commission (FCC) Office of Inspector General (OIG), and which appears to be deriving little public benefit. Clearly audits play a fundamental role in the oversight of policies and programs such as this; yet, only to the degree that they reasonably build upon program compliance to achieve underlying policy goals. Unfortunately, such does not appear to be the case with regard to the costly attestation audit approach the OIG is employing in this instance.

In a vividly detailed February 12, 2009, analysis of the OIG audit process, the Universal Service Administrative Company (USAC), which is charged by Congress and the FCC to administer and protect the integrity of the USF, outlines the extreme costs the OIG audit initiative has placed squarely upon the USF, and by extension every American telecommunications consumer. The USAC report methodically notes how over the course of approximately three years, tens of millions of USF dollars have been diverted from universal service program objectives to conduct 1,100 separate audits. Yet even more telling is that all these dollars later, the OIG audit reports have identified no instances of fraud or gross non-compliance with the program's parameters.

Specifically, the USAC analysis outlines how, at the direction of the OIG, as well as congressional appropriators, more than $192 million will have been spent on this wide-ranging audit initiative by the end of FY 2009. Nearly $165 million of this has come straight out of the USF -- $118 million to pay private auditors contracted at the direction of the OIG and $46.9 million that was provided directly to the OIG at the direction of congressional appropriators. Approximately $13 million of the $192 million total cost was borne directly by audited companies that were forced to employ accountants and lawyers to respond to the exhaustive details the attestation audits mandated.

In addition to the extreme financial costs of this audit process, USAC's analysis also outlines how the OIG is unique among federal entities in its interpretation that compliance with the Improper Payments Information Act of 2002 mandates employing the costly attestation style audit process rather than using other widely accepted processes and procedures. The USAC Report also elaborated on how the OIG approach to statistically extrapolating and then reporting anticipated program erroneous payments is wholly inconsistent with actual final audit results, thus leaving policymakers and the public alike with a faulty perception of program operations and compliance.

Today, more than ever, as federal policymakers, we have an overriding obligation to ensure that programs under our jurisdiction are managed appropriately and efficiently. We have that same responsibility with regard to the tools that are used to conduct the oversight of such programs. In light of the stark findings outlined in the USAC overview, we strongly urge that, as you develop your FY 2010 funding recommendations for the FCC, serious thought be given to directing the OIG to consider more reasonable and cost effective oversight approaches for the USF.

Sincerely,

Congressman Sam Graves

Congressman Frank Lucas

Congressman Mike Ross

Congressman Henry Brown

Shelley Moore Capito
Congresswoman Shelley Moore Capito

Mike McIntyre
Congressman Mike McIntyre

Congresswoman Cynthia Lummis

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Congressman Jerry Moran

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CC:
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COMMITTEE ON NATURAL RESOURCES
SUBCOMMITTEE ON NATIONAL PARKS, FORESTS, AND PUBLIC LANDS

SELECT COMMITTEE ON ENERGY INDEPENDENCE AND GLOBAL WARMING

Congress of the United States
House of Representatives

April 9, 2009

The Honorable Jose Serrano
Chairman, Financial Services and General Government Appropriations Subcommittee
Room B-300 Rayburn House Office Building
Washington, DC 20515

The Honorable Jo Ann Emerson
Ranking Member, Financial Services and General Government Appropriations Subcommittee
Room 1016 Longworth House Office Building
Washington, DC 20515

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Today, more than ever, as federal policymakers, we have an overriding obligation to ensure that programs under our jurisdiction are managed appropriately and efficiently. We have that same responsibility with regard to the tools that are used to conduct the oversight of such programs. In light of the stark findings outlined in the USAC overview, we strongly urge that, as you develop your FY 2010 funding recommendations for the FCC, serious thought be given to directing the OIG to consider more reasonable and cost effective oversight approaches for the USF.

Sincerely,

Stephanie Herseth Sandlin

Stephanie Herseth Sandlin
Member of Congress