Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	)	
	)	
Sandwich Isles Communications, Inc.	)	WC Docket No. 09-133
Petition for Declaratory Ruling	)	

REPLY COMMENTS of the NATIONAL EXCHANGE CARRIER ASSOCIATION, INC.

Sandwich Isles Communications, Inc. ("Sandwich Isles") filed comments with respect to its petition, which sought to justify inclusion of submarine cable and other transport costs in NECA's 2009 annual access tariff.[1] In light of both the petition and comments, NECA believes that it properly excluded these costs based on the facts of this case, and provided sufficient notice to Sandwich Isles of this decision, together with the opportunity to respond to NECA's concerns. NECA files this limited reply only to address to specific points NECA believes will help the Commission to render an opinion in this proceeding.[2]

1 Comments of Sandwich Isles Communication, Inc., WC Docket No. 09-133 (Aug. 31, 2009) ("Sandwich Isles Comments")

2 The Comments filed by NECA in this proceeding continue to accurately reflect NECA's position on this matter. Comments of National Exchange Carrier Association, Inc., WC Docket No. 09-133 (Aug. 31, 2009) ("NECA Comments"). Additional comments in this proceeding were also filed. Comments of Verizon, WC Docket No. 09-133 (Aug. 31, 2009) ("Verizon Comments"); Comments of Alaska Telephone Association, Inc., WC Docket No. 09-133 (Aug. 21, 2009) ("ATA Comments"); Comments of Aaron Stene, WC Docket No. 09-133 (Aug. 19, 2009); and comments of Sandwich Isles' consultant: Comments of GVNW, Inc., WC Docket No. 09-133 (Aug. 31, 2009) ("GVNW Comments"). *See*, Protective Order Declaration of Ben Harper, Sandwich Isles Communication, Inc., WC Docket No. 09-133 (Sept. 2, 2009).

NECA continues to believe that it properly applied the "Used and Useful" doctrine to the facts of this case. NECA agrees with Sandwich Isles that there is a need for the deployment of advanced technologies in rural areas and the provision of such advanced services is a "legitimate factor to be weighed among all the facts and circumstances."[3] NECA also recognizes rural and insular areas of the country face substantial financial and physical considerations compared to other less geographically diverse areas of the country.[4] However, as Sandwich Isles observes, this "does not mean that the NECA pool should reimburse carriers for every conceivable investment in new technology."[5] In the instant matter, NECA believes it responsibly and correctly weighed all the factors and concluded Sandwich Isles' proposal to report the entire cost of its exclusive lease of the new Paniolo transport network to the NECA pool was excessive.[6] Sandwich Isles has not demonstrated that demand would be anything more than minimal in the foreseeable future, particularly in relation to the extraordinary cost associated with the cable lease.[7] These factors combined with the availability of alternative transport options, was the

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3 Sandwich Isles Comments at 20.

4 NECA Comments at 3, 4. These rural and insular areas would, of course, include Hawaii and Alaska as both Sandwich Isles and ATA assert in their respective comments. *See,* ATA Comments at 1-2; Sandwich Isles Comments at 3.

5 Sandwich Isles Comments at 20.

6 *See,* NECA Comments at note 42. NECA did include the current costs of Sandwich Isles' lease of cable from Hawaiian Telcom, in its June, 2009 annual filing. Sandwich Isles has been incurring charges from Hawaiian Telcom to lease cable capacity in order to provide service to Sandwich Isles' customers. However, NECA expects that this lease of capacity from Hawaiian Telcom will terminate sometime in 2009. NECA has allowed the Sandwich Isles' Hawaiian Telcom lease costs to stay in the tariff filing until it can be determined what amount of payments projected for the Paniolo cable lease reasonably satisfy the "Used and Useful" standards.

7 NECA disputes the assertion of Sandwich Isles' consultant that NECA's analysis was based on the current capacity needs of Sandwich Isles and failed to consider the concept of "lumpy investment". *See,* GVNW Comments at 12, 15. NECA used reasonable, if not generous, growth projections compared to similarly sized companies to evaluate Sandwich Isles' capacity needs. *See also*, NECA Comments at note 65, discussing the Department of

basis for NECA concluding Sandwich Isles' proposal failed to meet the "Used and Useful" and prudent investment standards of the Commission.

The decision to exclude the Sandwich Isles' lease costs was clearly not based solely on a price quote received from Pacific LightNet (PLNI) as asserted by Sandwich Isles.[8] NECA's decision considered the extraordinary increase in proposed costs submitted to NECA by Sandwich Isles for the 2009 annual tariff filing with no evidence of material demand growth to offset the substantial cost increases.[9] Discussions with PLNI were simply one part of NECA's analysis of whether Sandwich Isles' lease costs were "Used and Useful" and prudent.[10]

Sandwich Isles also argues that the potential cost of alternatives must be viewed as of the time when the cable construction decision was made, not at the current time when the cable has already been constructed and the lease signed.[11] Sandwich Isles does not provide any legal support for this position. Regardless, given the high cost of the lease, coupled with low foreseeable demand, it is doubtful that utilizing alternative costs available in 2007 prior to

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Hawaiian Home Lands intention to build 500 homes a year. *See also*, Department of Hawaiian Home Lands, General Plan, http://hawaii.gov/dhhl/publications/island-plans/GeneralPlan.pdf/ (February 16, 2002)(last visited on August 25, 2009).

8 Sandwich Isles Comments at 24.

9 The test period effect of the lease costs submitted by Sandwich Isles in 2009 were 300% higher than those submitted in 2008 for the 2008 annual tariff filing. By the end of Sandwich Isles' new lease, the costs would have risen 727% over the amounts initially submitted to NECA in 2008. In addition, these numbers do not take into consideration the unknown cost of maintenance and upgrades of the leased cable for which Sandwich Isles is fully responsible under the terms of its exclusive lease.

10 NECA Comments at 19-23. Hawaiian Telcom's facilities were also part of the evaluation. *See*, Comments of Hawaiian Telcom, Inc., WC Docket No. 09-133, at 2-3 (Aug. 31, 2009) ("Hawaiian Telcom Comments"). NECA believes Sandwich Isles has utilized Hawaiian Telecom facilities in providing service to its HHL customers prior to the Paniolo lease going into service. *See, supra* note 6.

11 Sandwich Isles Comments at 17-18.

entering into the lease would have altered the application of the Used and Useful doctrine in the facts of this case.

NECA provided Sandwich Isles with sufficient notice of its concerns with Sandwich Isles' lease proposal.[12] It is clear from the beginning of discussions on the Paniolo lease issue that NECA communicated in writing its serious concerns regarding the costs associated with the new lease.[13] Although NECA could not provide a definitive response until it learned all the facts,[14] NECA believes it clearly advised Sandwich Isles and its consultants, including a consultant for the bank financing Paniolo's cable construction that NECA had concerns regarding the proposed lease. Sandwich Isles asserts: "[H]ad NECA made clear its specific concerns beyond generic statements that the expense may not be approved later in 2007 or in 2008, Sandwich Isles would have had at least an opportunity to provide full justification or adjust

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12 The GVNW and ATA comments also address the due process claim raised by Sandwich Isles. GVNW Comments at 10-11; ATA Comments at 2. As stated in its comments, NECA does not have a constitutional due process obligation. NECA Comments at note 29. However, NECA's comments, these reply comments, and correspondence between Sandwich Isles and NECA show that NECA dealt fairly with Sandwich Isles and Sandwich Isles was provided with numerous opportunities for its position to be heard.

13 NECA Comments at 9-12. Sandwich Isles refers to two letters from NECA sent in February, 2000 and February 2007 for support of the claim that NECA had approved the project for cost recovery. Sandwich Isles Comments at 6. As NECA explained to Sandwich Isles (see NECA Comments Appendix B at note 1), the 2000 letter was written over seven years before the Paniolo lease was signed. Over that period, the information available to NECA, including the number of served subscribers, changed substantially. The 2007 letter was written after RUS withdrew funding for the cable project and before NECA was informed of the Paniolo Lease in July 2007, therefore, neither letter was relevant to an evaluation of costs based on the new Paniolo Lease.

14 Both Sandwich Isles and its consultant, GVNW, attempt to make much of the fact that letters in 2007 and 2008 from NECA to Sandwich Isles indicated only that it "may" not approve funding. Sandwich Isles Comments at 25; GVNW Comments at 10. With an investment the size of the instant cable construction, a prudent investor would have been expected to obtain a more definitive answer than this.

its business plans";[15] NECA accepted its forecast in 2008 "without complaint";[16] NECA's multiple written communications of its concerns were simply issues of a "mechanical nature only";[17] and, "however the questions (posed by NECA) were answered and the issues resolved, the cost levels would not change."[18] These comments are puzzling because NECA believes its communications to Sandwich Isles and various consultants provided early and sufficient notice that if Sandwich Isles chose to proceed with the new lease arrangement there was no assurance that NECA would find the proposed costs acceptable for pool reporting.[19]

On its own accord and knowing full well there were no assurances of recovering the entire costs through the NECA pool, Sandwich Isles, with a small subscriber base and traffic volumes that "are relatively low,"[20] proceeded with signing an exclusive lease for the entire capacity of the new Paniolo Cable, the largest inter-island undersea cable in the State of Hawaii despite serving less than 0.4% of the land lines in Hawaii.[21] It was imprudent for Sandwich Isles

15 Sandwich Isles Comments at 25.

16 *Id.*

17 *Id.*, at 14.

18 *Id.*, at 25.

19 NECA Comments at 10. In any event, both parties to the pooling agreement are obligated to comply with all applicable FCC rules and orders. Thus, Sandwich Isles had an independent obligation to confirm its actions were consistent with FCC rules, and it is the FCC, not NECA, that will ultimately determine whether Sandwich Isles' proposal satisfies the Commission's standards. *See*, NECA Comments at 6.

20 Sandwich Isles Comments at 4.

21 Sandwich Isles also indicates "that as subscriber counts increase, the resulting traffic volumes will spread the common infrastructure costs over a wider base" and that it "reasonably expect[s] that because the Paniolo network has state-of-the-art technology and substantial capacity, other service providers will use capacity of various network segments." *Id.*, at 4 and 21, respectively. It would seem prudent to obtain significant customer commitments for use of the cable capacity in advance of embarking on an investment of this magnitude. Based on publicly available records, Sandwich Isles should have known prior to signing the lease that HHL customer growth would be low even if it was for "a variety of

to lease the entire cable when a small portion of the Paniolo Cable or a lease from an alternative provider could have been sufficient and more cost effective to serve a reasonable projection of growth in the Sandwich Isles customer base in the Hawaiian Home Lands.[22] Although projections of demand require some future predictions, given the historical predictions of Sandwich Isles' Hawaiian Home Land customers and the relatively low demand that actually transpired, Sandwich demand projections are seriously suspect at this point in time.

Additionally, NECA disputes Sandwich Isles' assertion that NECA has reversed its decision regarding the inclusion of the new cable lease costs, based on the fact it allowed some preliminary cost estimates in the NECA 2008 tariff filing. The cost estimates NECA allowed in 2008 were relatively low and had a minimal impact on the rates included in the tariff filing because the 2008 tariff test period ended in June 2009 and the new Paniolo lease payments were not scheduled to begin until August 2009. Sandwich Isles does not attempt to explain how allowing minimal preliminary cost estimates in a tariff filing can justify including excessive

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reasons outside its control." *See*, NECA Comments at note 65. *See also,* NECA Comments at note 67.

[22] According to an article in the Honolulu Advertiser, as of 2001, Sandwich Isles predicted it would already serve 20,000 subscribers by 2005. *See*, Kevin Dayton, *Savvy developer wins federal money to wire homelands,* Honolulu Advertiser, December 31, 2001, *available at* http://the.honoluluadvertiser.com/article/2001/Dec/31/ln/ln07a.html(last visited on September 9, 2009). Sandwich Isles' comments indicate there are a variety of reasons that "only a portion of the projected approximately 20,000 home sites have been completed and occupied to date." Sandwich Isles Comments at 4. However, Sandwich Isles should have been aware before it signed the lease in 2007 that according to a 2002 General Plan issued by the DHHL, the Department only planned to build 500 homes a year. *See*, NECA Comments at note 65 citing DHHL General Plan and Honolulu Star Bulletin Article.

costs at a later time, since such an argument focuses only on one of the prongs of the "Used and Useful" doctrine, compensation to the investor, and fails to protect customer interests.[23]

NECA also denies the claim that NECA dismissed "[T]he coordinated efforts undertaken in 2007 by Sandwich Isles, the bank and its consultant, and NECA to obtain the assurance needed by the bank to embark on this project."[24] As noted in NECA's comments, prior to the lease signing in July of 2007, NECA advised the bank's consultant that, pending review NECA had not "in any way shape or form, blessed the lease inclusion in NECA pooling and High Cost Loop calculations."[25]

Sandwich Isles has also not provided a sufficiently workable rate design alternative that would resolve this issue. Sandwich Isles suggests that NECA should have considered the implementation of a new "rate band applicable to Hawaii,"[26] instead of rejecting Sandwich Isles' proposed lease costs. NECA did consider this option but concluded that it would be ineffective in resolving the concerns.[27] Even if NECA were to establish a unique rate band for Hawaii, raise the rates Sandwich Isles would charge by 1,000% and assume that Sandwich Isles would not lose demand as a result of such a huge rate increase,[28] the increase in revenue would have covered

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[23] In addition, Sandwich Isles' position fails to recognize the inclusion of a forecast of costs in a tariff filing does not assure recovery of actual costs unless they are in compliance with Commission rules.

[24] Sandwich Isles Comments at 26.

[25] NECA Comments at note 33.

[26] Sandwich Isles Comments at 22.

[27] Should Sandwich Isles believe setting rates based on its cost and demand in Hawaii is a viable option, NECA would support a waiver of Commission rules with regard to the timing of pool exit elections to allow Sandwich Isles to leave the NECA Traffic Sensitive pool and file its own tariff.

[28] This of course is not a realistic demand assumption for a rate change of this magnitude. *See also,* recent customer demand trends in NECA Comments at Appendix A.

only 13% of the initial annualized lease cost and only 7% of the maximum annualized lease cost for the final years of the lease. Thus, even with a rate increase of 1,000%, or a demand increase of 1,000%, the vast majority of the new lease costs would become an obligation of other pool members and their rate payers.[29]

In sum, Sandwich Isles has failed to justify the excessive lease costs under the "Used and Useful" doctrine. NECA continues to stand ready, willing, and able to follow any FCC decision pursuant to this declaratory ruling petition with regard to cost levels that should be included in its interstate access tariff rates and pool.[30] As noted in its comments, NECA is also willing to review additional data and have further discussions with Sandwich Isles regarding what portion of its new cable lease may satisfy the Commission's "Used and Useful" standards.[31]

Respectfully submitted,

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[29] *See*, NECA Comments at 4 and 21(discussing potential impact on broadband "take rates" and impact on the NECA pools). While Sandwich Isles makes reference to "middle mile" costs, *see* Sandwich Isles Comments at 27, the costs of the transport lease from Paniolo used to transport Internet traffic from the Sandwich Isles' HHL service areas to the interconnection point with Internet Service Providers is recovered in Digital Subscriber Line (DSL) rates of NECA pool members.

[30] *See*, NECA Comments at note 77.

[31] *See*, *id*. at note 76.

Certificate of Service

I, Gregory J. Vogt, do hereby certify that I have on this 11th day of September 2009 caused a copy of the foregoing "Reply Comments of National Exchange Carrier Association, Inc." to be served by electronic mail upon the following:

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