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

In the Matter of	)
	)
Connect America Fund	) WC Docket No. 10-90
	)
A National Broadband Plan for Our Future	) GN Docket No. 09-51
	)
High-Cost Universal Service Support	) WC Docket No. 05-337

TO: The Commission

REPLY COMMENTS OF BLOOSTON RURAL CARRIERS

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Dated: August 11, 2010

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Summary

The Blooston Rural Carriers urge the Commission to exercise care to ensure that its proposed modifications to high-cost support programs are effective in promoting future broadband deployment and in preserving the previous progress of rural local exchange carriers ("RLECs") in deploying broadband. Specifically, the Commission should retain the incentives, features and instrumentalities of Rate of Return ("RoR") regulation that have been so successful in producing RLEC broadband deployment, and should not force RLECs to convert to either price caps or untested forms of incentive regulation that will slow or reverse the progress of RLECs in providing their rural customers with broadband facilities and services reasonably comparable to those available in urban areas.

To date, price caps and other potential forms of incentive regulation have demonstrated little or no capability to encourage or effectuate broadband or other significant infrastructure investment in rural areas. Rather, two decades of success by small ROR RLECs with limited financial resources in deploying quality voice services and more recently quality broadband services in their rural service areas (while neighboring rural service areas of much larger and financially more powerful price cap carriers have outmoded facilities and indifferent service) constitute persuasive evidence of the greater effectiveness of RoR regulation, at least regarding small carriers in rural service areas. RoR regulation not only is the superior mechanism for RLECs with respect to the primary standard of effectiveness in stimulating investment and service quality, but also is efficient and supportive of innovation.

Finally, the lawfulness of a forced migration of RLECs from RoR regulation to some unidentified form of incentive regulation is unclear, while the productivity improvement rationales underlying incentive systems are not applicable to entities as small as most RLECs.

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The law firm of Blooston, Mordkofsky, Dickens, Duffy & Prendergast, LLP ("Blooston"), on behalf of its rural local exchange carrier ("RLEC") clients listed in Attachment A (the "Blooston Rural Carriers"), respectfully submits the following reply comments with respect to the Commission's *Notice of Inquiry and Notice of Proposed Rulemaking*, FCC 10-58, released April 21, 2010 ("*NOI/NPRM*") in the captioned proceedings.

The focus of these reply comments is upon the issue raised in the *NPRM* portion of the *NOI/NPRM* as to whether rate-of-return ("RoR") carriers should be required to convert to "some form of incentive regulation" as one of the possible ways to cut "legacy" high-cost support.

I. Key: Effectiveness in Promoting Broadband Deployment

The Blooston Rural Carriers recognize that existing Universal Service Fund ("USF") support mechanisms need to evolve into broadband high-cost support mechanisms as the transformation of the current multiple use telecommunications and information services network into the National Broadband Network proceeds forward. However, the paramount goal of the

Commission should be to employ high-cost support mechanisms (whether existing, modified or new) that are effective for increasing broadband deployment so that more and more rural residents will have access to broadband facilities, speeds and services reasonably comparable to those available in urban areas. In designating and implementing broadband support mechanisms, the Commission should identify and retain those incentives, features and instrumentalities that have been successful in producing past and present broadband deployment, and should be particularly careful not to take steps that slow or reverse the progress that has already been made in providing broadband facilities and services in particular high-cost rural and insular areas.

II. The Record: Small RLECs under RoR vs. Large Carriers under Incentive Regulation

As indicated in the initial comments of the Blooston Rural Carriers, small RLECs with limited financial resources and minimal access to capital markets have done a far better job of deploying broadband to their rural customers than the much larger and financially powerful Regional Bell Operating Companies ("RBOCs") and mid-sized price cap carriers. RoR RLECs not only have but a small fraction of the access lines, revenues, assets, economies of scale and employees of the publicly traded price cap carriers, but also serve predominately remote, rugged, sparsely populated, or otherwise economically unattractive rural areas that the price cap carriers have long declined to serve (or that they divested as soon as federal and state regulators would permit). Yet, despite these major disadvantages, RoR RLECs have deployed some form of "broadband" [generally, hybrid fiber-copper digital subscriber line ("DSL") services] to approximately 90 percent of their rural customers, while price cap carriers lag far behind in rural broadband deployment. As the Commission itself has recognized, about half of the nation's households deemed "unserved" for broadband purposes are located in RBOC rural exchanges and another 15 percent are located in the rural exchanges of mid-sized price cap carriers.[1]

RoR regulation [including associated National Exchange Carrier Association ("NECA") pooling and federal high-cost support based upon actual costs] constitutes a critical and key factor explaining the difference between the RLEC rural record and the price cap carrier rural record. RoR regulation allows small RLECs to focus upon infrastructure deployment in their rural service areas, and enables them to overcome their size and resource disadvantages by furnishing reasonable assurance to their small circles of lenders and investors that they will be able to repay the 10-to-30-year loans needed to finance their infrastructure investments.

In stark contrast, "[i]ncentive regulation awards profit taking, it does not reward serving high-cost rural areas."[2] Price caps and other forms of incentive regulation encourage carriers to invest only in projects expected to be highly profitable (that is, they discourage substantial infrastructure investment in most rural areas) and to limit operating expenses to the minimum levels needed to retain customers (even if this results in degradation of service quality).

Hence, for almost twenty years, we have had the anomaly of small RLECs subject to RoR regulation furnishing their rural customers first with quality voice networks and services, and now with multi-use broadband networks and services, while the operations of much larger and better financed price cap carriers in nearby rural areas have too often been characterized by outmoded facilities and indifferent service.

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[1] Federal Communications Commission, *Connecting America: The National Broadband Plan* (March 16, 2010), p. 141 ("*NBP*").

[2] *Comments of CoBank, ACB*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 9.

III. Why Move RLECS from Effective to Ineffective Mechanism?

The Blooston Rural Carriers remain puzzled as to why regulators would want to force RLECs to move from a RoR regulatory mechanism with a long and proven record of success in encouraging and enabling small and highly diverse carriers to make the investments necessary to provide quality and affordable voice and broadband services to a broad variety of rural service areas. They are even further puzzled as to why such regulators would want to require RLECs to move to either (1) a price cap system that has had a very poor record of stimulating rural infrastructure investment by much larger and financially more powerful entities; or (2) some other yet-to-be-identified form of incentive regulation that has no record upon which it can be evaluated at this time.

First, there is the basic question of effectiveness. Why require RLECs to abandon a mechanism that has long permitted them successfully to deploy quality voice and broadband networks and services? And why require RLECs to move to a system that has been singularly unsuccessful in inducing much larger and better financed carriers to upgrade or deploy broadband in their rural exchanges, and that is likely to be an even more unsuitable mechanism for small companies?

Second, there is the question of the lawfulness of requiring RLECs to move from RoR to incentive regulation. In the past, the Commission has permitted RLECs to shift to incentive regulation on a voluntary basis, but has never mandated such changes. The Commission has repeatedly indicated that its experience over the years in attempting to develop incentive regulation for smaller companies has revealed that the wide variations among RLEC operating conditions make it impossible to devise a plan suitable for mandatory imposition on all RLECs.[3]

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[3] *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers,* Report and Order and Second Further Notice of Proposed

The Blooston Rural Carriers are not aware of any conditions that have changed to an extent that would warrant a reversal of the Commission's prior rulings. On the contrary, RLEC networks, service areas and operating conditions continue to be very diverse; and RoR regulation continues to be the most effective mechanism for enabling RLECs to obtain the financing necessary for broadband deployment.

Third, if the Commission is considering a form of incentive regulation other than price caps, it has not yet identified the features and characteristics of such alternative or given interested parties a reasonable opportunity to analyze and comment upon the particular strengths and weaknesses thereof. The Blooston Rural Carriers are particularly concerned that the RoR-incentive regulation question is part of the *NPRM* portion of the *NOI/NPRM*, and that an untested alternative form of incentive regulation might be devised, adopted and implemented by the Commission after the current pleading cycle is completed without a sufficient opportunity by RLECs and other interested parties to evaluate it. Rather, any alternative form of incentive regulation should be put out for comment, and should not be adopted or implemented until a full record is compiled with respect to its specific features.

Finally, to the extent that the Commission is concerned about the variations in broadband deployment in RoR rural service areas vis-à-vis broadband deployment in price cap rural service areas, the more effective approach may be to re-evaluate the incentives and impacts of price cap regulation upon large carrier investment in rural infrastructure. In their initial comments in this proceeding, the Blooston Rural Carriers proposed that the Commission address lagging broadband deployment in rural areas served by price cap carriers: (1) by increasing aggregate

Rulemaking, 19 FCC Rcd 4122, FCC 04-31 (rel. February 26, 2004), at par. 86; *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Second Report and Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256; Fifteenth Report and Order in CC Docket No. 96-45, and Report and Order in CC Docket Nos. 98-77 and 98-166, 16 FCC Rcd 19,613, FCC 01-304 (rel. November 8, 2001), at par. 227.

federal high-cost support via expansion of the Universal Service Fund contribution base; and (2) by establishing a separate capital expenditure support mechanism designed to create more effective incentives for rural infrastructure investment by price cap carriers.

IV. Responses to Criticisms of RoR Regulation

Commenting parties seeking to impose a much less effective form of regulation upon RLECs have asserted that RoR was implemented in the 1960s when there was only a single provider of voice service in most markets, that it was not designed to promote efficiency or innovation, that it frustrates competition, and that it is "not unreasonable" to expect RoR RLECs to achieve productivity gains similar to those of the price cap carriers.[4]

A. RoR Is Not an Outmoded Relic of the 1960s

The operative question is not when RoR regulation was first implemented,[5] but whether it works effectively today. Whereas larger carriers serving primarily urban and suburban areas may have found price caps to be more effective in meeting their pricing flexibility, profitability, dividend and stock price needs, RLECs have continued to find RoR to be the most effective mechanism for obtaining the loans and other financing that are essential for the upgrade, operation and maintenance of their rural networks. At the beginning of the second decade of the 21st Century, RoR regulation continues to play a decisive role in enabling small RLECS to bring broadband as well as quality voice services to the 37 percent of the U.S. land mass they serve –

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[4] Federal Communications Commission, *Connecting America: The National Broadband Plan* (March 16, 2010), p. 147; *Comments of Time Warner Cable Inc.*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 8; Comments of T-Mobile USA, Inc., WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 7; *Comments of Sprint Nextel Corporation*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 12; *Comments of CTIA – The Wireless Association*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at pp. 16-17; and *Comments of Verizon and Verizon Wireless*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at pp. 18-19.

[5] *Comments of Verizon and Verizon Wireless*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 19 ('relic of bygone era").

an area containing the nation's most remote, rugged, sparsely populated and difficult-to-serve rural areas.

B. RoR Is Not Inefficient

The canard that RoR regulation is "inefficient" has been repeated so often that few of its present purveyors bother to offer any evidence. The commenting parties herein have once again reasserted the myth without submitting any evidence to support it. [6]

The truth of the matter is that the costs of RoR RLECs are high because of the areas they serve and the regulatory conditions under which they operate, and not because of any unsubstantiated "inefficiencies." RLECs serve remote, rugged, and sparsely populated rural areas that are very expensive to serve under any circumstances in both relative and absolute terms. Moreover, these high costs are exacerbated by the substantial additional costs imposed by Carrier of Last Resort ("COLR") obligations to serve the most remote, expensive and unprofitable customers within these high-cost areas. In addition to the substantial investments and recurring expenses necessary to serve remote and unprofitable customers, COLRs are subject to a host of additional and expensive regulatory obligations, including service quality standards, requirements to maintain "warm lines" or "soft dialtone" in households that have terminated service, and federal and state oversight of rates, costs, accounting methods, record keeping and customer relationships. Hence, the high costs of RLEC service areas are not the result of "inefficient" RoR regulation; rather, they are the result of the geography, topography, demographics, economics and COLR requirements of the rural service areas.

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[6] *Comments of Time Warner Cable Inc.*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 8; *Comments of T-Mobile USA, Inc.*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 7; *Comments of CTIA – The Wireless Association*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at pp. 16-17; and *Comments of Verizon and Verizon Wireless*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 18.

Second, because they are small companies with limited cash flows and other financial resources that serve very expensive areas, RoR RLECs must be very prudent and efficient with respect to their investments and cash management. The "urban legend" that RLECs build unnecessary and gold-plated facilities to maximize their high-cost support and returns on investment is laughably fictitious for RLEC managers who must deal with boards of directors, loan applications and reviews, business plans and two-year lags in federal high-cost support. In the real world, RoR RLECs must justify their investment projects and business plans by filing detailed loan applications with the Rural Utilities Service ("RUS"), the Rural Telephone Financial Cooperative ("RTFC"), CoBank or (in a few cases) a local bank (as well as justifying their proposals, estimates and reasoning to their boards of directors and investors) before they can get approval and funding for infrastructure upgrades and operating budgets. These extensive loan and budget review procedures ensure that RLEC investment projects and day-to-day operations are prudent and efficient.

For example, contrary to some unfounded rumors, RLECs are not able to obtain the lender or investor approvals, and do not have the funding resources, to deploy fiber-to-the-home ("FTTH") facilities extravagantly to maximize their high-cost support beginning two years hence. Rather, RLECs are continuing to use fiber very carefully and conservatively to extend their DSL services to rural customers located further and further from their central offices and to increase the speeds and capacities of their existing DSL services in response to the needs and demands of their rural customers. Where undertaken, FTTH builds are limited predominately to green field and similar applications (*e.g.*, some exchange rebuilds) where fiber is less expensive to deploy than copper lines.[7]

[7] It is the information and belief of the Blooston Rural Carriers that RUS encourages or requires its RLEC borrowers to deploy fiber optic facilities (including FTTH facilities) under certain circumstances.

Finally, whereas any group of 1,100 entities is likely to have a couple members that push the limits, the wide and substantial variety of RLEC oversight mechanisms [including Commission tariff reviews, state commission audits and rate cases, NECA and Universal Service Administrative Company ("USAC") audits, and RUS compliance reviews] has demonstrated time and time again that virtually all RLECs are law-abiding entities that use federal-regulated and state-regulated resources in a reasonable, prudent and efficient manner.

C. RoR Does Not Discourage Innovation

The commenting parties alleging that RoR regulation "discourages innovation"[8] fail to submit any evidence to substantiate their claim. In fact, during the twenty years since price cap regulation was implemented, small RoR RLECs have far surpassed their larger price cap counterparts in bringing innovative facilities and services to their rural customers and exchange areas. During the 1990s, RoR RLECs led the way in deploying digital switches in their rural exchanges, burying lines to limit weather damage and outages, and offering custom calling options. As the Internet grew and developed, RoR RLECs have been pioneers in the use of fiber optic trunks to extend the availability of DSL services far beyond their initial ranges, and to offer a variety of higher-speed fiber-DSL services such as symmetrical digital subscriber line ("SDSL"), high data rate digital subscriber line ("HDSL") and/or very high speed digital subscriber line ("VDSL") to more and more of their rural customers. The RoR RLEC record of bringing predominately DSL-based broadband services to approximately 90 of their rural customers is unlikely to have been accomplished under incentive regulation, as demonstrated by

[8] *Comments of Time Warner Cable Inc.*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 8; Comments of T-Mobile USA, Inc., WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 7; *Comments of CTIA – The Wireless Association*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at pp. 16-17; and *Comments of Verizon and Verizon Wireless*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 18.

the absence of extensive broadband deployment in the rural exchanges of existing price cap carriers.

D. RoR Does Not Frustrate Competition

CTIA offers no evidence for its assertion that RoR regulation frustrates competition.[9] The rural service areas of RoR RLECS are generally remote, rugged and/or sparsely populated areas whose geography, topography, demographics and economics have discouraged competitive entry to a far greater extent than RoR regulation. RBOCs and other larger carriers have declined to serve these rural areas, while cable television and wireless operators (including most CTIA members) rarely venture beyond a few of the larger population centers and certain heavily-trafficked highway corridors.

E. RLECs Cannot Achieve Productivity Gains Comparable to Large Carriers

Sprint Nextel's claim that it is "not unreasonable" to expect current RoR RLECs to achieve productivity gains similar to those achieved by price cap carriers during the past two decades[10] wholly disregards the critical factors of size and economies of scale. The typical RoR RLEC is a very small company with a staff of less than 100 (and often less than 10) full-time employees and a customer base of less than 10,000 (and often less than 5,000) access lines. It is impossible for such small entities to generate economies of scale and productivity gains comparable to those of RBOCs and other larger carriers that have thousands or tens of thousands of employees and millions of customers.

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[9] *Comments of CTIA – The Wireless Association*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 17.

[10] *Comments of Sprint Nextel Corporation*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 12.

The asserted experience of Windstream Communications, Inc. ("Windstream") in converting voluntarily to price cap regulation[11] is not remotely relevant or applicable to the typical RoR RLEC. Windstream is a publicly-traded company (included in the Standard & Poor 500 index) that has 9,500 employees, that serves 3.4 million access lines in 23 states, and that generates $4 billion in annual revenues.[12] Whether or not Windstream can increase the productivity of its large staff, realize other economies of scale and/or reduce the amount of high-cost support it receives, the huge disparities in its size and scale render its experience wholly useless for predicting the impact upon RoR RLECs of a forced conversion to incentive regulation.

V. Conclusion

To date, price caps and other potential forms of incentive regulation have shown no capability to foster broadband or other infrastructure investment in rural areas. Rather, the two decades of success by small ROR RLECs with limited financial resources in deploying first quality voice services and recently broadband services in their rural service areas (while much larger and financially more powerful price cap carriers have invested minimally in their rural service areas) demonstrate beyond peradventure the greater effectiveness of RoR regulation as an investment incentive (at least with respect to small carriers) in rural service areas. RoR regulation not only is the superior mechanism for RLECs regarding the critical criterion of effectiveness, but also is efficient and supportive of innovation.

Consequently, in designing and implementing its broadband high-cost support mechanisms, the Commission should focus upon retaining the RoR incentives, features and

[11] *Comments of Windstream Communications, Inc.*, WC Docket Nos. 10-90, 05-337; GN Docket No. 09-51 (July 12, 2010), at p. 33.
[12] www.windstream.com/about/overview.aspx (viewed 8/11/2010).

instrumentalities that have been so successful in producing RLEC broadband deployment. It should not force RLECs to convert to hitherto ineffective price cap regulation or to a hitherto untested alternative form of incentive regulation. Likewise, the Commission should not require any other major changes that are likely to produce intended or unintended consequences that slow or reverse the excellence progress that is being made by RLECs in deploying broadband facilities and services in their rural service areas.

Respectfully submitted,
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ATTACHMENT A

BLOOSTON RURAL CARRIERS

3 Rivers Communications
Amery Telcom, Inc.
Amherst Telephone Company
Bayland Telephone, LLC
BEK Communications
Bergen Telephone Company
Bernard Telephone Co.
Bloomer Telephone Company
Bruce Telephone Company
Buggs Island Telephone Cooperative
Butler-Bremer Communications
Christensen Communications Co.
Clear Lake Telephone Company, LLC
Coon Valley Farmers Telephone Company
Dakota Central Telecommunications Cooperative
Delhi Telephone Company
Dumont Telephone Company
Emery Telcom
Farmers Independent Telephone Company
Farmers Mutual Telephone
Glenwood Telephone Membership Corporation
Harrisonville Telephone Company
Hector Communications Corporation
Hillsboro Telephone Company, Inc.
Hinton Telephone Company of Hinton, Oklahoma, Inc.
La Motte Telephone Company
Manawa Telephone Company
Midvale Telephone Exchange, Inc.
Minford Telephone Company
Monitor Cooperative Telephone Company
New Ulm Telecom, Inc.
Northeast Telephone Company, LLC
Oneida County Rural Telephone Company
Pineland Telephone Cooperative, Inc.
Pioneer Telephone Cooperative
Sharon Telephone Company of Wisconsin
Somerset Telephone Company, Inc.
South Slope Cooperative Telephone Co., Inc.
Spring Grove Communications
Tri-County Communications Coop., Inc.
Union Telephone Company
United Telephone Association, Inc.
Upper Peninsula Telephone Company
Walnut Telephone Company, Inc