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December 7, 2010

By Electronic Filing

Ms. Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th St., S.W.
Washington, D.C. 20554

Re: Comments of AT&T Corp., *Sandwich Isles, Inc.* Petition for Declaratory Ruling,
WC Docket No. 09-133 (December 6, 2010).

Dear Ms. Dortch:

AT&T is refileing its Comments in the above captioned proceeding. AT&T initially filed these Comments on December 6, 2010. AT&T is refileing these comments to remove proprietary information that was inadvertently included in the original filing. Although AT&T submitted the original filing with ECFS on December 6, 2010, the filing was removed from ECFS before being posted, and thus was not disclosed to the public.

Sincerely,

/s/ Christopher T. Shenk

Attachment

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

In the Matter of)
)
)
Sandwich Isles, Inc. Petition for Declaratory) WC Docket No. 09-133
Ruling)
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COMMENTS OF AT&T CORP.

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December 6, 2010

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In the Matter of)	
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Ruling)	
_____)	

COMMENTS OF AT&T CORP.

Pursuant to the Commission’s *Notice*,¹ AT&T Corp. (“AT&T”) submits these Comments opposing the Petition for Reconsideration submitted by Sandwich Isles Communications, Inc. (“Sandwich Isles”)² and supporting the Application for Review submitted by AT&T³ of the Declaratory Ruling released by the Wireline Competition Bureau (“Bureau”) on September 29, 2010.⁴

INTRODUCTION AND SUMMARY

Sandwich Isles is asking the Commission to require ratepayers to fund an extravagant undersea and terrestrial cable network that ratepayers neither need nor want. Multiple networks already serve those areas with more than enough capacity to serve current and future demand at much lower cost, and ratepayers have thus strongly opposed being forced to pay for the unnecessary expenses associated with the extravagant Paniolo network that Sandwich Isles is

¹ Public Notice, *Comment Sought On AT&T Application for Review And Sandwich Isles Petition for Reconsideration*, WC Docket No. 09-133, DA 10-2151 (rel. Nov. 5, 2010) (“*Notice*”).

² Sandwich Isles Communications, Inc. Petition for Reconsideration, *Sandwich Isles, Inc. Petition for Declaratory Ruling*, WC Docket No. 09-133 (Oct. 28, 2010) (“*Sandwich Isles Petition*”).

³ Application for Review, *Sandwich Isles, Inc. Petition for Declaratory Ruling*, WC Docket No. 09-133 (Oct. 29, 2010) (“*AT&T Application for Review*”).

⁴ Declaratory Ruling, *Sandwich Isles, Inc. Petition for Declaratory Ruling*, WC Docket No. 09-133 (Sep. 29, 2010) (“*Order*”).

leasing at costs that are *eight times* more than the existing alternatives and that Sandwich Isles funded to advance its provisions of Internet, video and other non-regulated services.⁵

When Sandwich Isles first submitted these Paniolo-related expenses to the National Exchange Carrier Association (“NECA”) and sought to recover them from ratepayers by including them in the NECA pool, NECA quite properly rejected them. As NECA properly ruled, because Sandwich Isles failed to demonstrate *any* present or future telephone service need for the Paniolo facilities, the \$15 million annual expenses associated with that cable is neither “used and useful” nor a “prudent investment” for its regulated services. Instead, NECA ruled that Sandwich Isles may continue to recover the \$1.9 million annual expense it was previously paying to lease voice grade capacity on one of the three existing cables that already served the Hawaiian Islands.

The Bureau Order under review in this case overruled NECA, and granted Sandwich Isles a pure windfall by allowing it to include 50 percent of its Paniolo-related expenses in the NECA pool, and thus recover them from ratepayers. The Order recognizes the “current lack of use of the [Paniolo] cable and a lack of substantial record evidence concerning future demand.”⁶ And the Order agrees that “ordinarily” the \$1.9 million that NECA authorized would be “sufficient” and “reflect[] a reasonable application of the threshold ‘used and useful’ considerations.”⁷ Yet on the basis of “other equitable considerations” the Bureau Order saddles ratepayers of Sandwich

⁵ As NECA has pointed out, there are also significant concerns here that the entire Sandwich Isles-Paniolo transaction is an artificial construct and involves inappropriate affiliate transactions. NECA Comments at 1, n.37.

⁶ Order, ¶ 17.

⁷ *Id.* ¶ 18.

Isles' regulated services with millions of dollars in expenses that do not – and will not ever – benefit them in any way.⁸

Unsatisfied with the undeserved windfall it has already obtained from the Bureau, Sandwich Isles seeks to include *100 percent* of its Paniolo-related expenses in the NECA pool. But just as there is no legitimate non-arbitrary basis for passing even half of those expenses on to ratepayers,⁹ there is certainly no valid justification for passing all of those expenses to ratepayers, and Sandwich Isles provides none.

Most fundamentally, Sandwich Isles' Petition is procedurally infirm. “The Commission will consider a petition for reconsideration only when the petitioner shows either a material error in the original order, or raises additional facts, not known or existing at the time of petitioner’s last opportunity to present such matters.”¹⁰ Sandwich Isles' Petition relies mainly on NECA Guidelines that were not previously submitted in this proceeding, but that were fully available to Sandwich Isles and its consultants since at least March 2004.¹¹ The NECA Guidelines are thus not a valid basis for seeking reconsideration under the Commission’s rules. Sandwich Isles also relies on a new Declaration prepared by one of its consultants (the “Harper Declaration”),¹² but this declaration also presents no new facts or circumstances that were not previously available to

⁸ *Id.* ¶ 23.

⁹ See AT&T Application for Review, at 1-16.

¹⁰ *In re: WXNH(AM), Jaffrey, NH, Facility ID No. 129522, File Nos. BNP-20001023ACT and BMP-20080214AHR, Petitions for Reconsideration*, 24 FCC Rcd. 11809, 11811 (2009); 47 C.F.R. § 1.106(b)(2), (c)(1).

¹¹ NECA Nov. 3, 2010 Letter, at 1 (“this document [the NECA Guidelines] has been made available to all NECA members and consultants since at least March 2004” and “[b]oth [Sandwich Isles] and its consultants had access to the document.”).

¹² See Petition, Exhibit A.

Sandwich Isles, and the rest of Sandwich Isles' Petition is just a rehash of arguments that the Bureau properly rejected and that the Bureau need not consider again.¹³

Sandwich Isles' Petition can be also be immediately rejected because it seeks to include 100 percent of Sandwich Isles' Paniolo-related lease expenses in its interstate revenue requirement, and recover those amounts through the NECA pool, even though Sandwich Isles' admits that portions of those facilities, and hence expenses, are used for intrastate services and potentially for non-regulated services (*e.g.*, video and Internet services).

In any event, Sandwich Isles' arguments are meritless. *First*, Sandwich Isles argues that the NECA Guidelines require NECA to allow carriers to recover 100 percent of any spare capacity costs they incur from the NECA pool. The NECA Guidelines require no such thing. The NECA Guidelines merely address how a carrier's "booked" expenses are to be allocated among different regulatory accounts for the purpose of separating interstate expenses from intrastate expenses. The NECA Guidelines do *not* address what costs are used an useful and properly included in a carrier's revenue requirement for recovery in the NECA pool.

Second, Sandwich Isles rehashes its arguments that the Commission implicitly approved of the inclusion of 100 percent of Sandwich Isles' Paniolo-related expenses in the NECA pool when the Commission granted Sandwich Isles' Study Area Waivers (the "SAW" decisions). The Bureau correctly rejected these arguments the first time. The last SAW decision was in 2005 and the Paniolo investments at issue here did not begin until 2007. As the Bureau correctly held, it would be quite unreasonable to read the SAW orders as a substantive decision that any *future*

¹³ See, *e.g.*, *General Motors Corp. and Hughes Electronics Corp., Transferors, and The News Corp. Ltd., Transferee, For Authority to Transfer Control, Order on Reconsideration*, 23 FCC Rcd. 3131, 3135, ¶ 11 (2008) (the Commission will reject petitions for reconsideration that "essentially repeat[] the same arguments"); see also, *e.g.*, *Order on Reconsideration, S&L Teen Hospital Shuttle; Application to Modify and Reinstate the License for Business Radio Service Station WIJ767, Montrose, California*, 17 FCC Rcd. 7899, ¶ 3 (2002).

investments Sandwich Isles chose to make would necessarily be “used and useful” and properly included in the NECA pool. Indeed, *SAW III* expressly *disclaimed* any such future effect of its orders: “the Commission looks at the estimated support on an annualized basis at the time the waiver request is submitted, and does not attempt to estimate the future support amounts.”¹⁴ In all events, it would set a dangerous and arbitrary precedent if the Commission were to hold here that a mere waiver of the study area freeze insulates a carrier from any future challenge to whether that carrier’s costs are “used and useful,” giving all carriers that have received study area waivers a free pass to “gold plate” their networks and pass those unnecessary and imprudent costs on to ratepayers.

Third, Sandwich Isles asserts that the Bureau misapplied the “used and useful” standard, arguing that there was no rational basis for the Bureau to reject the \$15 million lease payments Sandwich Isles sought to include in the NECA pool and limiting Sandwich Isles to including only \$1.9 million in the pool. In fact, the record shows that the \$15 million lease payments are absurdly high and reflect costs of an extravagant network that is neither used nor useful to ratepayers; the \$1.9 million that the Bureau permitted is reasonable because it reflects the amounts Sandwich Isles included in the NECA pool to recover costs for serving its customers prior to the Paniolo arrangement. Sandwich Isles also asserts that there is no basis to reject any amounts related to Sandwich Isles’ lease of terrestrial (as opposed to undersea) facilities from Paniolo on the grounds that NECA never challenged those costs. In fact, as shown below, NECA opposed all of the Paniolo-related lease costs – terrestrial and undersea – and the record confirms that was appropriate given that there was already more than sufficient terrestrial and

¹⁴ *Sandwich Isles Communications, Inc. Petition for Waiver of the Definition of Study Area” Contained in Part 36 Appendix-Glossary and Sections 36.611 and 69.2(hh) of the Commission’s Rules*, 20 FCC Rcd. 8999, ¶ 17 (2005) (“*SAW III*”).

undersea capacity to meet current and future demand by ratepayers. Sandwich Isles further asserts that it reasonably relied on the *SAW I* and *SAW III* decisions when it entered into its arrangement with Paniolo, but as explained above (and further demonstrated below), no reasonable reading of those decisions could have led to the conclusion that Sandwich Isles would be permitted to include all (or indeed any) of the costs related to its arrangement with Paniolo in the NECA pool.

On this record, the Commission should reject Sandwich Isles' Petition for reconsideration and grant AT&T's Application for Review, thus ensuring that ratepayers are not saddled with the expenses for a network that they neither need nor want.

ARGUMENT

"The Commission will consider a petition for reconsideration only when the petitioner shows either a material error in the original order, or raises additional facts, not known or existing at the time of petitioner's last opportunity to present such matters."¹⁵ Sandwich Isles neither acknowledges nor addresses this standard, and for good reason: it precludes a grant of Sandwich Isles' Petition. Sandwich Isles' Petition relies almost entirely on NECA Guidelines not previously submitted in this proceeding and on a new Declaration prepared by one of Sandwich Isles' consultants (the "Harper Declaration").¹⁶ However, Sandwich Isles does not

¹⁵ *In re: WXNH(AM), Jaffrey, NH, Facility ID No. 129522, File Nos. BNP-20001023ACT and BMP-20080214AHR, Petitions for Reconsideration*, 24 FCC Rcd 11809, 11811 (2009); *See* 47 C.F.R. § 1.106(b)(2), (c)(1) ("A petition for reconsideration which relies on facts not previously presented to the Commission or to the designated authority may be granted only" if "(i) The petition relies on facts which relate to events which have occurred or circumstances which have changed since the last opportunity to present such matters; or (ii) The petition relies on facts unknown to petitioner until after his last opportunity to present such matters which could not, through the exercise of ordinary diligence, have been learned prior to such opportunity.").

¹⁶ *See* Petition, Exhibit A.

dispute that it has long had access to the NECA Guidelines¹⁷ and, in fact, the record confirms that Sandwich Isles and its consultants have had access to them since at least March 2004.¹⁸ Likewise, the new facts set forth in the Harper declaration relate to these NECA Guidelines and to Sandwich Isles' own accounts, both of which have clearly long been available to Sandwich Isles. Accordingly, the Commission's rules preclude consideration of arguments based on the NECA Guidelines and the Harper Declaration, which includes virtually all of the arguments in Sandwich Isles' Petition. Sandwich Isles' only remaining arguments rehash arguments it previously made and that were properly rejected, thus violating of the Commission's policy against repeating arguments in petitions for reconsideration.¹⁹

Sandwich Isles' Petition can be immediately rejected for a second independent reason. Sandwich Isles' Petition seeks to include 100 percent of Sandwich Isles' Paniolo-related lease expenses in its interstate revenue requirement, and to include those amounts through the NECA pool. But Sandwich Isles' admits that portions of its Paniolo lease expenses relate to facilities

¹⁷ Sandwich Isles states only that the NECA Guidelines are not "available in public databases." Sandwich Isles Petition, at iii.

¹⁸ Letter from Gregory J. Vogt (NECA) to Marlene H. Dortch (FCC), WC Docket No. 09-133, at 1 (Nov. 3, 2010) ("this document [the NECA Guidelines] has been made available to all NECA members and consultants since at least March 2004" and "[b]oth [Sandwich Isles] and its consultants had access to the document.").

¹⁹ See, e.g., *General Motors Corp. and Hughes Electronics Corp., Transferors, and The News Corp. Ltd., Transferee, For Authority to Transfer Control, Order on Reconsideration*, 23 FCC Rcd 3131, 3135 P 11 (2008) (The "Commission has rejected petitions for reconsideration where the petitioner essentially repeats the same arguments it relied upon in the comments and reply comments it filed and fails to raise new arguments or facts that would warrant reconsideration of [the underlying] order. Accordingly, we decline to revisit the arguments we have already addressed and rejected."); *Order on Reconsideration, S&L Teen Hospital Shuttle; Application to Modify and Reinstate the License for Business Radio Service Station WIJ767, Montrose, California*, 17 FCC Rcd. 7899, ¶ 3 (2002) ("It is settled Commission policy that petitions for reconsideration are not to be used for the mere reargument of points previously advanced and rejected. Reconsideration will not be granted merely for the purpose of again debating matters on which the Commission has already deliberated and decided.").

that Sandwich Isles’ is using to provide non-interstate services (*i.e.*, intrastate services) and potentially non-regulated services (*e.g.*, video and Internet services).²⁰

Even if a grant of Sandwich Isles’ Petition were not barred by the Commission’s rules, it would still have to be rejected because all of the arguments raised by Sandwich Isles are baseless. As explained below, the NECA Guidelines are irrelevant, the Bureau correctly determined that the Study Area Waiver (“SAW”) cases do not require that all of Sandwich Isles’ expenses related to the Paniolo lease be included in the NECA pool, and the Bureau correctly determined that the used and useful standard does not permit Sandwich Isles to include 100 percent of the Paniolo expenses in the NECA pool.

I. THE NECA GUIDELINES ARE IRRELEVANT TO THE ISSUES IN THIS CASE AND IN NO WAY SUPPORT SANDWICH ISLES’ ASSERTIONS THAT IT IS ENTITLED TO ALL OF ITS PANIOLO-RELATED EXPENSES.

Sandwich Isles’ main argument is that “NECA misled the Bureau by failing to advise the Commission that it has spare fiber rules which apply to all rural LECs participating in the NECA pool.”²¹ According to Sandwich Isles, “[a]s it turns out, the existence of spare capacity is so common that NECA has a rule governing it” and that “rule clearly applies to spare Paniolo fiber and application of that rule clearly provides that Sandwich Isles is entitled to recover 100 percent of its spare fiber costs from the NECA Pool.”²²

²⁰ *See, e.g.*, Letter from Dana Frix (Sandwich Isles) to Marlene H. Dortch, WC Docket No. 09-133, at 2 (Aug. 17, 2010) (“there are three undersea cables providing *intrastate* service within Hawaii: the Paniolo Cable, which is leased and operated by SIC; the HTI cable built in 1994; and the cable which is jointly owned and used by tw telecom and Wavecom.”) (emphasis added). It is unclear the extent to which Sandwich Isles today is also providing non-regulated services using the Paniolo facilities, but Sandwich Isles has indicated that, if it is not already, it plans to do so. Sandwich Isles Comments, at 20-21.

²¹ Sandwich Isles Petition, at 1.

²² *Id.* at 1.

Sandwich Isles relies mainly on an “illustrative example” in the NECA Guidelines, which considers a carrier that has deployed 24 fibers, of which 8 are in-use and 16 are spare. This illustrative example explains that “[f]or the most part, spare fiber plant should continue to be assigned to the same cost pools as related ‘in-use’ equipment.”²³ Based on this illustrative example, Sandwich Isles concludes the NECA Guidelines require that the “16 spare fibers are to be recovered from the NECA pool.”²⁴ Sandwich Isles asserts that it uses **[BEGIN CONFIDENTIAL]** **[END CONFIDENTIAL]** out of 48 fibers and that “following the Guidelines . . . the cost of Paniolo spare fibers is required to be allocated to the NECA pool.”²⁵

In fact, the NECA Guidelines relied on by Sandwich Isles do not address the threshold “used and useful standard that governs whether any particular cost may be included in the NECA pool. As Sandwich Isles admits, the NECA Guidelines interpret Commission Rules 36.152 and 36.153 that explain how carriers are supposed to allocate the “Cable and Wireline Facilities” (or “C&WF”) expenses among the various regulatory CF&W sub-accounts. These Commission rules are part of the Commission “Jurisdictional Separations” process in which carriers are required to allocate “booked” “property costs, revenue, expenses, taxes, and reserves as recorded on the books of the company” for the process of separating interstate costs (which can be recovered through interstate tariffs) and intrastate costs (which generally cannot be included interstate tariffs).²⁶ The NECA Guidelines merely explain how spare capacity costs on a carriers’ books are to be allocated among these regulatory accounts.

²³ *Id.* at 2-3 (citing NECA Guidelines at 1).

²⁴ *Id.* at 3.

²⁵ *Id.*

²⁶ 47 C.F.R. § 36.1.

These separations procedures have nothing to do with determining whether any particular expenses are “used and useful” – and therefore may be included in a carrier’s revenue requirement and the NECA pool – and thus there is no merit to Sandwich Isles’ assertions that these NECA Guidelines somehow require 100 percent of a carrier’s “spare capacity” costs to be included in the NECA pool. Rather, as the Commission has explained, the “first step” in the actual *ratemaking* process is the application of the “used and useful” standard to determine the expenses that a carrier may include in its revenue requirement and thus recover from ratepayers.²⁷ NECA is *required* to follow that procedure, regardless of what “book” costs a carrier allocated to the various Part 36 Jurisdictional Separation regulatory accounts.²⁸

The NECA Guidelines are irrelevant for other reasons as well. The NECA Guidelines do not specifically address undersea cable, and thus could not be “controlling” here, as to those issues, even if they were otherwise relevant.²⁹ Further, the NECA Guidelines are just that: *guidelines*. Even if they addressed the threshold question of whether costs should be included in the rate base and even if they specifically addressed undersea fiber, they could not trump the

²⁷ Memorandum Opinion And Order, *Investigation of Access and Divestiture Related Tariffs*, 97 FCC 2d 1082, ¶ 16 (1984) (“The starting point for developing or reviewing a rate filing is establishing an overall revenue requirement. A carrier is entitled to charge rates which recover allowable expenses and a reasonable return on the investment in property *used and useful* for service to the public. This amount is the revenue requirement.”) (emphasis added); *Phase II Final Decision and Order*, 64 FCC 2d 1, ¶ 110 (1977) (“The starting point in calculating [a carrier’s] revenue requirements is a determination of the ‘fair value of its rate base’ and the Commission ‘has always applied the used and useful standard’ to make that determination); Order, ¶ 27 (“the ‘used and useful’ standard is the starting point for developing or reviewing a rate filing”) (emphasis added).

²⁸ Order, ¶ 27 (“NECA . . . must comply with . . . the ‘used and useful’ standards and related ratemaking requirements adopted in prior Commission orders”).

²⁹ Sandwich Isles Petition, at iii-iv.

findings of the Bureau’s analysis based on the governing legal standard and the vast record in this proceeding.³⁰

For these reasons, all of the arguments made by Sandwich Isles that are based on its false assumption that the NECA Guidelines permit it to allocate all of its expenses to the NECA pool, regardless of whether it is used or useful, fail. *First*, according to Sandwich Isles it uses [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] of the 48 fibers under its lease with Paniolo and those [BEGIN CONFIDENTIAL] [END CONFIDENTIAL] account for more than 98 percent of the cost incurred by Paniolo of deploying fiber,³¹ and under the NECA Guidelines it should be allowed to recover those amounts. But this argument is based entirely on its false assumption that the NECA Guidelines permit it to recover 100 percent of its actual expenses. Rather, the issue here is whether those facilities are “used and useful,” and the record confirms that the Paniolo facilities and their corresponding expenses are extravagant and not “used and useful” and thus cannot be included in the NECA pool.³² Similarly, Sandwich Isles’ related assertion that “[i]nstead of following the [NECA] Guidelines, . . . [the Bureau Order] adopted ‘the Paniolo Spare Fiber Rule,’ a standard that applies only to [Sandwich Isles]”³³ is

³⁰ In fact, Sandwich Isles’ interpretation of the NECA Guidelines and Commission rules is contrary to their very purpose. Carriers may recover costs associated with only regulated *interstate* services through federal interstate access tariffs. One of the primary purposes of the Part 36 Rules and the NECA Guidelines is to ensure carriers remove costs associated with non-interstate services before seeking to recover any such costs through rates. According to Sandwich Isles’ reading of these rules and the NECA Guidelines, however, these rules permit carriers to recover 100 percent of their spare capacity through interstate rates, regardless of whether portions of that spare capacity are used for non-interstate services.

³¹ *Id.* at 8.

³² Sandwich Isles’ argument here is also factually inaccurate. It is not true that Sandwich Isles generally has [BEGIN CONFIDENTIAL]

[END CONFIDENTIAL]

³³ Sandwich Isles Petition, at 8.

frivolous. As the Bureau makes clear, the used and useful standard applies to everyone,³⁴ and the Bureau has in the past denied carriers recovery of expenses from ratepayers that were found not to be used and useful.³⁵

Second, Sandwich Isles argues that the Bureau's Order constitutes impermissible retroactive rulemaking because it "creates and imposes upon Sandwich Isles an entirely new and novel requirement that carriers demonstrate anticipated demand for spare fiber based upon specific evidence of demand for regulated services" thus overruling the Commission rules and the NECA Guidelines, that, according to Sandwich Isles, permit it to recover all expenses incurred for spare capacity regardless of whether it is proportional to expected future demand.³⁶

There is no new rule here. The "used and useful" standard has for decades been the standard that "provides the foundation of the Commission decisions evaluating whether

³⁴ Order, ¶ 27 ("NECA – just like carriers that file their own tariffs – must comply not only with the codified accounting, cost allocation, jurisdictional separations, and access charge rules," but the "used and useful" standards and related ratemaking requirements adopted in prior Commission orders, as well.").

³⁵ See, e.g., *Common Carrier Rate Structure Inquiry Investigation*, 88 FCC 2d 1656 (1982) (denying AT&T recovery of a portion of its costs under the used and useful standard). Sandwich Isles also argues that the amount of spare capacity it has is consistent with the spare capacity of large ILECs in the mid-1990s (about 68% according to a 1997 Commission estimate). Sandwich Isles Petition at 4 (quoting *Separations Reform*, Notice of Proposed Rulemaking, 12 FCC Rcd. 22120, ¶ 70 (Oct. 7, 1997) ("*Separations NPRM*"). But nothing in the *Separations NPRM* suggests that these investments were excessive, as the record shows is the case with respect to the Paniolo facilities. Further, as the Bureau has pointed out, nothing in the *Separations NPRM* suggests that the large ILECs were permitted to recover the fully cost of their spare fiber through the NECA pool. Order, n.71. In any event, Sandwich Isles provides no evidence that it is similarly situated to these large ILECs as they existed in 1997. These ILECs were typically the first entrant into the marketplace and were therefore responsible for providing all or almost all of the fiber facilities needed for regulated services. By contrast, Sandwich Isles is a new entrant and there already were multiple providers with substantial amounts of fiber. Thus, unlike the ILECs of the mid-1990s, one would not expect Sandwich Isles to deploy large amounts of additional fiber for the purpose of providing regulated services.

³⁶ Sandwich Isles Petition, at 10-11.

particular investments can be included in a carrier’s revenue requirement.”³⁷ In 1985, the Commission explained that “central to the used and useful concept” is the “principle that ratepayers may not fairly be forced to pay a return except on investment which can be shown to directly benefit them.”³⁸ Where, as here, the bulk of the facilities at issue constitutes spare capacity, such facilities can benefit ratepayers only if those facilities will eventually serve ratepayers. Indeed, the Commission has expressly stated that that facilities are “used and useful” only if they are “necessary to the efficient conduct of a utility’s business, presently or within a *reasonable future period*,”³⁹ and that this inquiry includes, among other things whether the investments in the facilities were “prudent” and whether such “investment will be realized in a *reasonable time period*.”⁴⁰ And, contrary to Sandwich Isles’ assertions, these long-standing requirements are not in any way inconsistent with the NECA Guidelines or Commission Rules 36.152 or 36.153. As explained above, the NECA Guidelines and these Commission rules address how to allocate booked costs among various regulated accounts, not how to determine whether those costs are “used and useful” and can be included in the NECA pool.

Third, Sandwich Isles complains (at 5) that “[a]s a result of the [NECA] Guidelines not being introduced in this case, the Bureau relied upon two cases that well precede the Guidelines, the *PSV Cable* and the *Comsat* cases.”⁴¹ But, as explained above, the NECA Guidelines are irrelevant to whether the Paniolo facilities are used and useful. Thus, the Bureau’s reliance on the *PSV Cable* and *Comsat* cases, which do address that issue, was appropriate.

³⁷ Order, ¶ 12 (citing Phase II Final Decision and Order, *American Tel. and Tel. Co.*, 64 FCC 2d 1, ¶ 111 (1977)).

³⁸ Phase II Final Decision and Order, *American Tel. and Tel. Co.*, 64 FCC 2d 1, ¶ 111 (1977).

³⁹ *Id.* (emphasis added).

⁴⁰ *Id.* (emphasis added)

⁴¹ Sandwich Isles Petition, at 5.

In this regard, there is no merit to Sandwich Isles' backup argument that the *PSV Cable* and the *Comsat* cases support 100 percent inclusion of Sandwich Isles' Paniolo expenses merely because 100 percent of the expenses at issue in those cases was ultimately permitted. The main difference between those cases and the issues here is that in those cases it was undisputed that the investments were "used and useful" at the time the investments were made. It was only much later that circumstances that could not be predicted and that were outside the control of the carriers ended up raising questions as to whether the investments at issue in those cases ultimately turned out to be used and useful. In those limited circumstances, the Commission determined that equitable considerations militated in favor of allowing recovery. Here, by contrast, the Paniolo facilities were deemed non-used and non-useful from day one.

For example, in the *Comsat* decision, there was no dispute that the satellites, once launched successfully, were providing valuable services to ratepayers, and, given the risks inherent in launching these new satellites (which apparently were not otherwise reflected in rates), the Commission concluded that ratepayers could be required to pay for investments that were clearly prudently made when the satellites were launched, even if they later failed – a conclusion to which no party objected.⁴² *Comsat* thus does not support the recovery of the Paniolo lease payments, because here there is no question that Sandwich Isles' investment was at no point in time reasonably believed necessary to benefit ratepayers of regulated services.

⁴² See *In the Matter of Comsat*, 56 F.C.C.2d 1101, ¶¶ 80-91 (1975) (discussing capabilities of various satellites, including, for example, one series that "allowed simultaneous transmission of either four television programs or up to 1200 (later 1500) two-way voice-grade circuits, or some combination of television and voice-grade"); *id.* ¶ 93 ("Trial Staff has no serious quarrel with this approach and recommends that full recovery of failed satellites be allowed"); *id.* ¶ 92 (citing *Washington Gas v. Baker*, 118 F.2d 11 (D.C. Cir. 1950), which holds that in some circumstances it can be reasonable to include "abandoned property" in the rate base where ratepayers have not already paid higher rates, and investors have not earned higher returns, that reflects the risks that such property would become obsolete").

Likewise, the issue in the PSV cases was “Polyethylene shielded video” cables (PSV), which were conductors developed for local video transmission and which had been widely installed by the Bell System; however, as technology changed, many of the PSV cables could not be used for providing video.⁴³ Sandwich Isles correctly notes that “[t]here were two PSV cases,”⁴⁴ and, not surprisingly, Sandwich Isles argues that the second PSV case – the one where the Commission *rejected* large portions of the PSV expenses because they provided no benefit to ratepayers and were thus not used or useful – is not relevant here, and that the Commission should instead focus on the first PSV case, where the Commission permitted 100 percent recovery of the PSV expenses.⁴⁵ But even there (and unlike here) no one disputed that the PSV facilities were reasonable and used and useful at the time they were made: the “composite cables containing PSV pairs remain[ed] in use providing service” and “[t]hus the overall facilities is clearly used and useful property.”⁴⁶

II. THE STUDY AREA WAIVER CASES DO NOT SUPPORT, AND IN FACT REFUTE, SANDWICH ISLES’ ASSERTIONS THAT IT IS ENTITLED TO INCLUDE ALL OF ITS PANIOLO-RELATED EXPENSES IN THE NECA POOL.

Sandwich Isles argues that previous Bureau orders approving waivers that allow Sandwich Isles to participate in the NECA pool also constitute binding, substantive decisions that Sandwich Isles’ costs are “used and useful” and thus fully recoverable through the NECA pooling process. The Bureau correctly rejected these arguments.

⁴³ *Phase I Special Access Tariffs*, 1986 WL 291617 (FCC Jan. 21, 1986); *see also Series 7000 Decision*, 88 F.C.C.2d 1656, ¶ 48 (1982).

⁴⁴ Sandwich Isles Petition, at 5.

⁴⁵ *Id.* at 5-6.

⁴⁶ *Common Carrier Rate Structure Inquiry Tariff Investigation*, 88 FCC 2d 1656, ¶ 49 (Feb. 23, 1982).

Sandwich Isles relies in particular on *SAW III*, in which the Bureau granted a waiver of the study area boundary freeze codified in Rules 36.611 and 69.2(hh) and the Appendix-Glossary of Part 36.⁴⁷ Sandwich Isles emphasizes (at 17) that the Bureau specifically considered that Sandwich Isles had been investing significant capital and that the Bureau took note of USAC's projections of the amount of universal service support Sandwich Isles was receiving at the time (*i.e.*, as of the third quarter of 2005).⁴⁸ Sandwich Isles claims (at 18) that these reference to USAC estimates show that *SAW III* is "replete with accounting analysis and considered, in detail, the costs and benefits of permitting Sandwich Isles to place its costs in the NECA Pool."

But the investments here did not begin until 2007. And, as the Bureau correctly held, it would be quite unreasonable to read the *SAW* orders as a substantive decision that any *future* investments Sandwich Isles chose to make would necessarily be "used and useful" and properly includible in the NECA pool. In fact, in the very passage Sandwich Isles quotes, the Bureau expressly *disclaimed* any such future effect of its orders. In *SAW III*, Hawaiian Telcom opposed the waiver on the grounds that Sandwich Isles' future investments would unreasonably increase the burden on the USF, but the Bureau replied that "the Commission looks at the estimated support on an annualized basis at the time the waiver request is submitted, and does not attempt to estimate the future support amounts. Accordingly, we will not attempt to estimate the amount of universal service support Sandwich Isles may receive in the future."⁴⁹ As the Bureau explained in order under review, the *SAW* orders "did not find that it is in the public interest to

⁴⁷ See *Sandwich Isles Communications, Inc. Petition for Waiver of the Definition of Study Area* "Contained in Part 36 Appendix-Glossary and Sections 36.611 and 69.2(hh) of the Commission's Rules, 20 FCC Rcd. 8999 (2005) ("*SAW III*"). In the *SAW III* order, the Bureau essentially re-established the relief that it had granted in *SAW I* but which the Commission reversed in *SAW II*. See *SAW III* ¶¶ 1-4 (granting new waiver *nunc pro tunc* and explaining history).

⁴⁸ See *SAW III* ¶ 16 & n.53.

⁴⁹ *Id.* ¶ 17.

include all of the cable leasing costs in the NECA revenue pool,” but at most made an “initial determination that Sandwich Isles, a small, new carrier providing service to a previously unserved area, would benefit from participation in the NECA pool as a general matter.”⁵⁰

Indeed, it would set a dangerous and arbitrary precedent if the Commission were to hold here that a mere waiver of the study area freeze insulates a carrier from any future challenge to whether that carrier’s costs are “used and useful.” As the Bureau correctly explained (at ¶ 10), “the analyses for deciding study area waivers and requests to join the NECA pool do not traditionally, and did not in this case, include a determination of what costs should ultimately be allowed in Sandwich Isles’ revenue requirement.” It is simply absurd to claim that merely allowing Sandwich Isles to participate in the NECA pool gives it an unlimited free pass going forward to “gold plate” its network and pass those unnecessary and imprudent costs onto customers of other NECA carriers, and contrary to Sandwich Isles’ contention, any such reading of those orders would give Sandwich Isles special rights that other NECA carriers do not enjoy. Sandwich Isles actually said it best (at 12-13): the SAW decisions answered the question “whether [Sandwich Isles’] *reasonable* costs could be placed in the NECA Pool” – but like all other NECA carriers’ costs, the reasonableness of those costs are properly reconsidered with each tariff filing.

III. THERE IS NO MERIT TO SANDWICH ISLES’ CLAIMS THAT THE BUREAU MISAPPLIED THE “USED AND USEFUL” STANDARD.

Sandwich Isles’ assertions (at 21) that the Bureau’s Order misapplied the “used and useful standard are makeweights. *First*, Sandwich Isles asserts that there is “[n]o rational basis” to “award[] [Sandwich Isles] only \$1.9 million, or 13 percent of the Paniolo annual lease cost of

⁵⁰ See Order ¶ 10; *see also id.* (“the public interest analysis in that context was focused more generally on whether the public interest would be served by extending service to that [unserved] area and its people”).

\$15 million.”⁵¹ In fact, the Bureau awarded Sandwich Isles more than \$7 million. In any event, the record shows that Sandwich Isles’ \$15 million lease with Paniolo is a “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.”⁵² Sandwich Isles itself admits that its lease is based on projections of “serving 20,000 subscribers over the life of the lease,”⁵³ even though Sandwich Isles today serves only a tiny fraction of that number and that Sandwich Isles is highly unlikely to obtain anywhere near 20,000 during the 20 year life of the facilities.⁵⁴ And given that the used and useful standard permits carriers to recover only those costs that are “necessary to the efficient conduct [its] business, presently or within a reasonable future period,”⁵⁵ the Bureau’s denial of the full \$15 million was clearly rational. Further, the Bureau’s decision to limit recovery related to the Paniolo facilities Sandwich Isles actually used to \$1.9 million was likewise rational and fully supported by the record, because that is the amount that Sandwich Isles was previously actually paying for the facilities used to serve its few customers.⁵⁶

⁵¹ Sandwich Isles Petition, at 21.

⁵² NECA Reply Comments, at 5.

⁵³ NECA Comments, at 19

⁵⁴ Order, ¶¶ 22-23; NECA Comments, at 19-20.

⁵⁵ Order, ¶ 12.

⁵⁶ *Id.* ¶ 18; Sandwich Isles White Paper, at 2, 14. Sandwich Isles’ assertion that “NECA does not require carriers to demonstrate that they could have avoided construction costs by leasing,” is incorrect. As the Bureau points out, NECA, as a tariff filer, must comply with the Commission’s used and useful standards when submitting rates. Order, ¶ 27. And the Commission has made clear that factors, such as the availability of lower cost alternatives, are relevant to this assessment. *See, e.g.,* Memorandum Opinion & Order, *AT&T Communications Revisions to Tariff F.C.C. Nos. 1, 2, 11, 13, and 14, Application for Review*, 5 FCC Rcd. 5693 (1990) (examining whether costs produced a “ratepayer benefit” and excluding \$73 million of AT&T’s billing and collection expenses” because they “exceeded what the LECs would have charged [AT&T] for those services”).

Second, Sandwich Isles contends that the Bureau’s Order erred “because it fails to award 100 percent cost recovery for the Paniolo terrestrial construction costs.”⁵⁷ But this argument is based on a false premise. It is not true, as Sandwich Isles asserts, that NECA has not disputed that the terrestrial portion of the Paniolo lease is used and useful. NECA disputed the *entire* amount of Paniolo lease, which includes both the undersea and terrestrial portions of that lease.⁵⁸ Further, the fact that NECA has in the past accepted the expenses associated of Sandwich Isles’ previous terrestrial (non-Paniolo-related) network does not, as Sandwich Isles contends, require NECA to accept the expenses associated with the terrestrial portion of the much more costly Paniolo network. Whether the expenses associated with Sandwich Isles’ previous terrestrial network was used and useful has no bearing at all on whether Sandwich Isles’ inflated Paniolo-related expenses are used and useful.⁵⁹

Third, Sandwich Isles asserts that it reasonably relied on the *SAW I* and *SAW III* decisions when it entered into its arrangement with Paniolo, but as explained above (and further demonstrated blow), no reasonable reading of those decisions could have led to the conclusion

⁵⁷ Sandwich Isles at 22.

⁵⁸ *See, e.g.*, NECA Comment at 2 (NECA “could not support Sandwich Isles’ decision to lease, in its entirety, a cable transportation network” and rejecting the entire costs of that network, including both the terrestrial and submarine portions). It is also not true that the Bureau’s Order does not address “the terrestrial part of the Paniolo network.” Sandwich Isles at 23. The Order twice (§ 5 & n.84) refers to the entire \$15 million lease expense associated with the Paniolo network (which includes both the undersea and terrestrial portion of the network), and the Order expressly explains in footnote 30 that “the expenses subject to dispute” here include “the costs for Sandwich Isles to lease the Paniolo cable network each year,” which includes the cost of leasing the terrestrial portion of the network.

⁵⁹ The Bureau also should not credit Sandwich Isles’ assertion that 55 percent of its Paniolo lease expenses are associated with the terrestrial portion of the Paniolo network. Sandwich Isles at 23. This assertion is based entirely on unsupported summary spreadsheets that cannot be verified and, moreover, the notion that more than half of the Paniolo costs are associated with the terrestrial portion of the network is highly suspect, given Sandwich Isles’ admission that it has 275 miles of submarine cable and only 74 miles of terrestrial cable. Letter from David Cosson (Sandwich Isles) to Marlene H. Dortch (FCC), WC Docket No. 09-133 (Nov. 13, 2009).

that Sandwich Isles would be permitted to include extravagant expenses, such as those related to its arrangement with Paniolo, in the NECA pool.

CONCLUSION

For the foregoing reasons, the Commission should the Commission should grant the relief sought in AT&T's Application for Review and reject Sandwich Isles' Petition for Reconsideration.

Respectfully submitted,

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