Before the
Federal Communications Commission
Washington, DC 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
	)	
Establishing Just and Reasonable Rates for	)	WC Docket No. 07-135
Local Exchange Carriers	)	
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Developing an Unified Intercarrier	)	CC Docket No. 01-92
Compensation Regime	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
Lifeline and Link-Up	)	
	)	WC Docket No. 03-109

Comments of the Rural Broadband Alliance

April 18, 2011

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Comments of the Rural Broadband Alliance

SUMMARY OF COMMENTS

The Rural Broadband Alliance (the "Alliance" or "RBA") proposes in these Comments the adoption of the Transitional Stability Plan ("TSP") to ensure that rural communities and businesses continue to have access to universal service, as that concept evolves. The TSP will provide a responsible alternative for many rural carriers in need of action to restore stability in their operations and certainty of an opportunity to recover their established investments and operating expenses.

Although the Alliance proposes modifications to the Commission's "near-term" proposals, its TSP is consistent with and responsive to the fundamental principles and goals of this proceeding while answering carriers' concerns of stability and sustainability in a manner that ensures the continued provision of universal service and the deployment of advance networks in rural areas. To accomplish these goals, the TSP proposes the following plan:

1. Electing rate-of-return carriers will freeze their interstate revenue requirement, consisting of the most recent cost study elements and future capital investment arising from participation in RUS financing or the ARRA Broadband stimulus program.

2. The electing carrier's frozen interstate revenue requirement is subject to an annual reduction (based either on an adjustment to reflect additional accumulated depreciation over time or a factor), as well as an annual increase to reflect additional expenses needed to maintain universal service or to provide an evolving expansive definition of universal service. These upward adjustments, subject to prior FCC approval, ensure that the rural carrier has a meaningful opportunity to recover costs, and that it is not subjected to unfunded mandates. To the extent that the electing carrier demonstrates a requirement for additional funding, any additional funding will be distributed from the Connect America Fund ("CAF").

3. The electing company's annual USF funding will be the residual of its adjusted frozen interstate revenue requirement reduced by the company's settled access charge revenues and subscriber line revenues. This residually-derived USF payment may be exercised either within or outside of the NECA pools.

4. To address the concerns of some rural carriers with regard to excessive cost recovery reliance on access charges, the plan provides the option for the electing carrier to move to access charge price caps with recovery from the CAF of the otherwise resulting lost access revenue needed for cost recovery.

The TSP addresses each of the Commission's announced tenets. It requires that additional funding be available only to authorized proposals to maintain or expand universal service offerings, thereby answering the Commission's concerns that the Universal Service Fund be modernized and refocused on broadband availability. To further rationalize universal service funding, and to assist in modernizing the Intercarrier

Compensation mechanism, the plan proposes an option to move forward with a reduction in access charges as a method of minimizing implicit support.

Supporting fiscal responsibility, the TSP proposes a freeze on access to the existing fund, and requires that additional funding be tied to demonstrated expansion or maintenance of universal service. Accountability is similarly served through the TSP's requirement that access to the CAF be justified. Accountability is also furthered by the TSP's proposal that the Commission establish clear goals and performance metrics to provide universal service carriers with clear expectations regarding the availability of funding necessary to provide universal service.

Finally, the TSP option offers meaningful incentives to rural companies to maximize the efficient operation of their businesses within the frozen revenue requirement. Recognizing the current reality of scarce program resources, the TSP ties additional funding requests to the Commission's objective of targeting funding to where it is needed to foster the provision of broadband and maintenance of universal service.

The Alliance shares the Commission's goal of establishing a firm foundation for 21^{st} century communications needs. It offers the TSP as a practical pathway to achievement of this goal.

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Comments of the Rural Broadband Alliance

The Rural Broadband Alliance (the "Alliance" or "RBA") respectfully responds to the Commission's invitation to comment on its far-reaching plan to reform carrier compensation mechanisms.[1] The Alliance shares the Commission's goal of establishing a firm foundation for 21st century communications needs. To ensure that rural communities and businesses continue and expand their access to universal service offerings, the Alliance herein offers an alternative to the Commission's reform proposals which RBA believes will better meet both statutory

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1 *See generally, Connect America Fund*, WC Dkt. No. 10-90; *A National Broadband Plan for Our Future*, Gen. Dkt. No. 09-51; *Establishing Just and Reasonable Rates for Local Exchange Carriers,* WC Dkt. No. 07-135; *High-Cost Universal Service Support*, WC Dkt. No. 05-337; *Developing an Unified Intercarrier Compensation Regime*, CC Docket 01-92; *Federal-State Board on Universal Service*; CC Dkt. No. 96-45; *Lifeline and Link-Up*; WC Dkt. No. 03-109, Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, __ FCC Rcd. __, FCC 11-13 (rel. Feb. 9, 2011) ("NPRM").

universal service policies and the Commission's guiding principles, and best accommodate the requirements and aspirations of Rural America.

I. Prologue: Rural Telephone Companies Are The Engines That Drive Rural Economic Development And Opportunity In Rural America

A. The Commission's Universal Service Mechanisms For Rural Rate-of-Return ("RoR") Carriers Is A Success Story.

Until very recently, living in rural America meant a distant, at times isolated, life. Lower population densities and longer distances between communities meant that rural Americans simply endured the challenges that accompanied their chosen lifestyle. These challenges included diminished access to healthcare, decreased educational coursework capabilities, and severely limited economic development possibilities. No longer. Today, many rural Americans, particularly those served by small telephone companies, have jetted into the 21st century, embracing opportunities previously unavailable to them and surmounting the obstacles posed by distance and low population densities.

Rural telephone companies have been the engines of rural America's emergence into this new era of opportunity. The hundreds of rural telephone companies that today serve communities from Alaska to Florida are in existence largely because the former Bell Operating Companies (the majority of whom have now been consolidated into the AT&T and Verizon communications giants) chose not to extend service to these areas, reflecting their analysis that profitable service in low-density areas was marginal, if not impossible.

Rural telephone companies today employ thousands across the country, often constituting one of the larger employers in their communities. They also play a vital role in the economic health and development of rural America by providing the communications networks that support local small businesses and entrepreneurs, connect telecommuters to their workplaces, join buyers and sellers in virtual marketplaces, and otherwise encourage and facilitate commerce. The development of this infrastructure, aided by the operation of the current Universal Service Fund, is largely responsible for the banishment of rural isolation. The role of rural telephone companies in the social and economic advances for rural America should be recognized and supported. To do otherwise could propel rural America swiftly back into the prior century where distance and low population densities were frequently insurmountable obstacles to success.

The telecommunications industry and the communications markets have undeniably changed in the past decade, and the Commission's review of compensation mechanisms, including universal service funding and intercarrier compensation arrangements, is both appropriate and necessary. Operationally, telephone companies are attempting to meet the challenges of changing technologies and changing markets. No longer do telephone companies engineer systems dedicated to voice service. Rather, companies must establish networks capable of supporting broadband services, as well as supporting the services required by other telecommunications service providers, such as wireless and middle mile carriers. Today's telephone networks must also be engineered to participate in the delivery of other services to carriers and end users alike, including, importantly, emergency services.

As the Commission made clear in its NPRM, "[u]biquitous broadband infrastructure has become crucial to our nation's economic development . . . . Businesses need broadband to start and grow; adults need broadband to find jobs; children need broadband to learn . . . . As important as these benefits are in America's cities . . . the distance-conquering benefits of broadband can be even more important in America's more remote small towns, rural and insular areas, and Tribal lands."[2]

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[2] NPRM at para. 3 (footnotes omitted).

The current Universal Service Fund has been successful. Its function was to ensure that services and pricing available to customers in rural America were comparable to the services and pricing offered to customers in urban and suburban areas. Notably, as a result of the USF, rural telephone companies have been able to deploy networks that connect rural hospitals, remote schools, emergency service coordinators and providers, and the myriad other basic linkages that enhance the daily lives of rural Americans. Indeed, long before the initiation of this NPRM, many rural telephone companies relied on the Universal Service Fund to upgrade their networks from "plain old telephone service" to broadband.

B. Speed Matters.

Some have argued against the 21st century upgrades that allowed for services beyond voice, calling them "gold-plating." The fact is, however, that these high performance network deployments were forward looking and customer focused. Customer demand for high performance networks began in the early 2000's and, for many fortunate rural residents, their telephone company answered that demand. To call such customer-focused delivery "gold-plating" is at best, merely insulting, and at worst, misguided and insensitive to the needs of rural customers.

Speed matters, and it matters every bit as much in rural America as in our urban centers. Although the proposals set forth by the RBA provide for the initial interim determination that universal service provided by telecommunications carriers should include broadband capability of 4 Mbps down and 1 Mbps up, it is vital that the definition of broadband universal service evolve quickly to match the pace required to meet the requirements of economic development and consumer expectations in rural America.

Comcast recently announced its intent to deploy a service that delivers 105 Mbps to more than 40 million homes in cities across America. According to Comcast, a 6GB movie transmitted at 6 Mbps would download in 2 hours and 15 minutes, while at 105 Mbps that movie would transmit in 8 minutes.[3] To put this in perspective, a 6144 MB sized movie at speeds between 1.5 Mbps and 3 Mbps would take 4 hours and 33 minutes to download; and the same movie would take 33 minutes if transferred at speeds between 10 Mbps and 25 Mbps.[4]

The differences in these speeds can mean the difference between life and death for patients in rural hospitals relying on the transmission of radiology films, diagnostic videos or other health-care related information. For businesses that rely on heavy data transfer, these speeds reflect the difference between real time customer service or product delivery. As a result, for business and residents in rural communities, these speeds are not discretionary – they are required.

As technology evolves, the application of the principles embedded in the Communications Act of 1934, as amended (the "Act") remain a constant:

> Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have <u>access to telecommunications and information services</u>, including interexchange services <u>and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas</u> and that are available <u>at rates that are reasonably comparable to rates charged for similar services in urban areas</u>. [5]

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3 USA Today, April 14, 2011, page B1.

4 *See,* http://www.broadbandmap.gov/classroom/speed.

5 47 USC § 254(b)(3) (emphasis added).

To consign rural communities to "low-speed" not only would be contrary to the explicit Universal Service principles set forth in the Act, but would also deprive those communities of the lifeblood and vitality they require for economic development and job creation.

Few other private industries bear as much public responsibility as the rural telephone industry. These companies are charged with fulfilling the universal service aspirations of the Act throughout a large portion of rural America. The nation's rural RoR carriers are committed to bringing rapidly evolving telecommunications services and infrastructure to all of the residents of the communities they serve. The rural telephone industry has met these requirements in the past, and remains ready to meet these challenges today. The provision of advanced telecommunications networks within small and rural communities is a cornerstone of future economic development and jobs recovery in those areas. Without these networks, connections will falter and jobs failures will follow.

It is vital to rural America that the Commission expediently resolves the long-pending issues raised in this proceeding, and it is essential to rural economic development, job creation, and job preservation that the Commission gets it right. The Commission, therefore, has a two-front broadband battleground. First, to ensure that the unserved and underserved are served; and, second, but equally as important, to ensure that those communities that are currently well-served under today's standards can continue to evolve to and have available comparable service levels provided in urban areas. The Commission must succeed in both of these fronts and recognize the vital role that USF has played and can continue to play in the economic vitality of the rural areas communities served by the rural RoR carriers. These communities deserve nothing less.

II. Introduction and Synopsis of Comments

The Alliance is a growing coalition of more than two hundred rural incumbent local exchange carriers formed to advance sensible, evidence-based policies for the deployment and adoption of broadband services for all of the nation's citizens, including consumers and businesses residing in rural, insular and high cost-to-serve areas of the nation. With these Comments, the Alliance continues the dialogue it initiated more than six months ago[6] to highlight the growing lack of predictability and stability of the cost recovery mechanisms upon which the provision of universal service relies. To neutralize the growing financial uncertainty among rural providers and the financial markets that is impacting both infrastructure investment and job creation, and may lead to rural community job loss, and to achieve the NPRM's policy goals, RBA proposes an elective Transitional Stability Plan ("TSP"), as detailed herein.

The TSP will achieve the Commission's underlying objectives without causing disruption to existing investment recovery, and without perpetuating (or exacerbating) the problem that occurs as increased investment is made under a capped fund: as companies invest more in the aggregate, the funding requirement increases, but because of the overall limitation on funding, there is a growing gap of unrecovered costs which will threaten the economic viability of rural providers. As more fully developed in Section III of these Comments, the TSP proposes that an electing carrier could freeze its interstate revenue requirement as of a date certain. This

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6 *See*, *e.g.*, Letter from Stephen G. Kraskin on behalf of the Rural Broadband Alliance to Marlene H. Dortch, Secretary, FCC, WC Dkt. No. 10-90, GN Dkt. No. 09-51 and WC Dkt. No. 05-337 (filed Oct. 13, 2010); Letter from Stephen G. Kraskin on behalf of the Rural Broadband Alliance to Marlene H. Dortch, Secretary, FCC, WC Dkt. No. 10-90, GN Dkt. No. 09-51 and WC Dkt. No. 05-337 (filed Dec. 15, 2010); and Letter from Stephen G. Kraskin on behalf of the Rural Broadband Alliance to Marlene H. Dortch, Secretary, FCC, WC Dkt. No. 10-90, GN Dkt. No. 09-51, WC Dkt. No. 07-135, WC Dkt. No. 05-337, CC Dkt. No. 01-92, CC Docket No. 96-45 and WC Dkt. No. 03-109 (filed Feb. 28 2011).

annual interstate revenue requirement (decreased as described herein) would be recovered from three sources: the sum of (i) settled access charge revenues and (ii) subscriber line revenues, and (iii) the Universal Service Fund ("USF"). Any defined additional universal service requirements, or increases in recovery necessary to maintain universal service would, in each case subject to prior Commission approval, are recovered from the Commission's newly proposed Connect America Fund ("CAF"). Simultaneously with achieving a sustainable and predictable system of cost recovery for rural local exchange carriers, this two-step plan is also consistent with the Commission's guiding principles:

1. The TSP fosters the goal of *modernizing USF and Intercarrier Compensation ("ICC")* to refocus on affordable broadband;

2. The TSP allows the realization of *fiscal responsibility* by providing for both reductions in the existing funding mechanism for rural rate-of-return carriers and constraint on the proposed CAF;

3. The TSP mandates *accountability* by ensuring that existing investment and expenses remain subject to the Commission's current audit processes and providing for additional funding subject to an accountability/review process to be established by the FCC; and

4. The TSP provides an option for *transition to market-driven and incentive-based policies* while ensuring the ubiquitous availability of universal service.[7]

Not only does the TSP advance the Commission's express principles, but adoption of the TSP would also be beneficial and appropriate because the plan (i) is consistent with existing law and policy, (ii) provides an appropriate "glide path" to more permanent reforms,[8] (iii) incorporates a

[7] *See, e.g., NPRM* at para. 10. Regarding the limitations to a universal reliance on market-based policies, the Commission recognizes that "in some geographic areas there may be no private sector business case for offering broadband services." NPRM at n. 16.

[8] The Commission has expressed its intent to avoid any disruptive "flash cuts" in its policies. *See, e.g.,* NPRM at paras. 12 and 17.

fair and reasonable framework for the recovery of investment made in good faith, and (iv) may be implemented quickly and efficiently.

III. The Objectives and Elements of the TSP for Carriers Subject to Rate of Return ("RoR") Regulation

As noted above, the basic components of the elective TSP are (1) the continued recovery of existing or "legacy" interstate investment and associated expenses through the traditional elements of access charges, subscriber line revenue and the USF; and (2) the recovery of new universal service investment and associated expenses through the new CAF by participating carriers. The Alliance believes that these two components, implemented as described in these Comments, will provide both a reasonable transition to, and a sound foundation for, access to 21st century universal service by all Americans.

A. Need for Reform

As the Commission notes, current interstate recovery mechanisms comprise a mixture of various USF components, access charges, and intercarrier compensation arrangements, as well as "bill & keep" arrangements.[9] This historic hodgepodge of compensation mechanisms evolved over time, each element a product of its own set of technological, market, statutory and policy requirements and limitations. With technology both evolving and being shaped by the market, and blurring once-sharp policy distinctions, the basic foundations of the current cost recovery system are under significant pressure.

The Alliance agrees that ensuring the continued fulfillment of statutory and public interest mandates requires reform of the existing cost recovery mechanisms. Universal service cost recovery concepts long precede the codification of universal service in the Telecommunications Act of 1996. The underlying policy of universal cost service recovery has

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[9] NPRM at para. 7.

always incorporated a "fair share" concept that recognized that all who benefit from the ability to reach and be reached by residents and businesses located in a high cost-to-serve area of rural America should share in paying for the costs of the networks they utilize. Today's cost recovery mechanisms are based on 1984 policy considerations that defined this value generally in terms of long distance usage.

As a result, the current cost recovery mechanisms were essentially based on assessments of long distance usage over the network that interconnects rural areas to the rest of the nation. The evolution of technology and broadband has resulted in more usage of the network, but a diminished relative utilization for traditional long distance voice services. Accordingly, with the continuing relative decline in long distance service, it is necessary to reform the cost recovery mechanisms. Moreover, the Alliance believes that this reformation must occur promptly and therefore advocates the adoption of systemic modifications that can be implemented without significant additional delay.

RBA members and their fellow rural incumbent telephone RoR companies today provide universal service and maintain the infrastructure necessary for its continued provision in a world of shrinking access minutes and increasing pressure on pooled resources because the High-Cost Fund ("HCF"), a major component of the USF,[10] is capped. As companies invest more in the aggregate, the funding requirement increases, but at the cap, the gap of unrecovered costs will develop and grow. With declining access revenues and the eventuality of less-than-full cost recovery from a capped HCF, the current system of cost recovery simply will not sustain, let alone allow for improvement or expansion of, universal service at reasonable rates.

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[10] The High-Cost Loop Support element of the existing HCF available to rural incumbent RoR carriers has been "capped since the 1990s" (NPRM at para. 21).

B. Objectives of RBA's Transitional Stability Plan

The Alliance seeks meaningful reforms to cost recovery mechanisms that will return stability to the current operations of rural rate-of-return carriers, and provide those carriers with a rational basis for future investment. Rural incumbent carriers, like all businesses, require predictability of recovery of their investment. The Alliance believes that its Transitional Stability Plan offers a framework that promotes confidence in the opportunity to recover investment in rural America. Encouraging investment clearly benefits rural consumers and businesses alike through the direct creation and maintenance of jobs, as well as improvement of economic conditions generally. And, because "the benefits of broadband grow when all areas of the country are connected,"[11] rural broadband investment promotes the welfare of the nation as a whole.

In concert with this overarching objective, and consistent with statutory and Commission objectives, the Alliance proposes the TSP as the vehicle that will:

1. Restore stability to the rural communications investment arena by ensuring recovery of established operational costs and capital investments of rate-of-return carriers.

2. Ensure that sustainable and predictable cost recovery mechanisms are available to a rural rate-of-return carrier to provide that carrier with a reasonable opportunity to recover additional expenses incurred to provide an evolving level of universal service. Rate-of-return carriers should not be required to incur additional investments and expenses to provide universal service unless sustainable, predictable support is available.

3. Alleviate the financial instability and uncertainty in a manner consistent with the overall objectives of the NPRM.

4. Ensure that support is reasonably refocused and transitioned to support the deployment and maintenance of universal broadband service in the high cost to

[11] NPRM at para. 3.

serve rural areas of the nation that are unserved or underserved, and in those high cost areas where universal service could not be maintained in the absence of support.

5. Transition switched access charges to lower rate levels, and reduce the exposure of rural companies to reliance on declining switched access charge minutes as a primary source for the recovery of costs by rate-of-return carriers, and recover the access revenues lost thereby from the USF.

6. Provide rural incumbent rate-of-return carriers with meaningful incentive regulation alternatives.

The elements of the TSP are set forth below; proposed implementation details, entitled "Operational Specifics of the Transitional Stability Plan Option," are attached.

C. RBA Proposal for the Transitional Stability Plan

To meet the objectives enumerated above, the Alliance proposes the following optional incentive plan to encourage prudent investment while maintaining RoR as both a safety valve and as a fair and much-needed transition from today's mechanisms established within a regulatory system focused on the transmission of voice services. Similar to options provided today to rural rate-of-return carriers (cost, average schedules, and price-caps), this plan provides an option for electing carriers to address the need for financial stability in the provision of universal service.

The elements of this optional plan are as follows:

1. Freeze of current interstate revenue requirement

The centerpiece of the Alliance's proposal is the restoration of stability for RoR carriers. Carriers have undertaken investment in reliance upon existing rules, but recovery of this investment and associated expenses has become uncertain as the mechanisms themselves, and the policy basis for the support associated with the mechanisms, has become weakened over time. Specifically, the continued reliance of recovery mechanisms on assessments related to the provision of long distance services is not sustainable given the reality of the relative decline in the utilization of traditional long distance service. At the same time, the existing cost recovery mechanisms fail to address explicitly the burgeoning utilization of universal service networks to transmit data and support the delivery of numerous applications enabled by broadband technology.

This proposed interstate revenue requirement freeze does not guarantee an unending revenue flow but rather provides RoR carriers with the cost recovery revenues that are consistent with the established annualized levels of capital and operational expenses undertaken to provide and sustain universal service. These expenses have been incurred in reliance on existing rules and regulations, and subject to continued regulatory scrutiny. There is no reason that a cloud of uncertainty should continue to hamper the recovery of these expenses or impede infrastructure investment in rural America.

Adoption of the proposed interstate revenue requirement freeze, and the resulting restoration of stability and predictability to the recovery of the established costs necessary to provide universal service is not, however, sufficient by itself. If the frozen and declining[12] level of interstate revenue recovery is insufficient to recover the costs of providing universal service, the RoR regulatory mechanism should remain available to provide the opportunity for cost recovery and a fair return. Maintenance of the proven mechanism of a RoR safety valve is consistent both with the statutory requirement to ensure that universal service support should be "explicit and sufficient" and with the Commission's concern that support should be targeted and recipients accountable.

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[12] The TSP proposes that the frozen interstate revenue requirement be adjusted downward annually to reflect the depreciation of capital investment. *See*, Attachment "Operational Specifics of the Transitional Stability Plan Option," Section II.A. 2.

The basic implementation steps for this aspect of the TSP are:

i. Electing rate-of-return carriers freeze their interstate revenue requirement as of a date certain (subject to adjustment as provided in subparagraphs iii and iv below) for a period of 10 years.

ii. All investments and expenses included in an electing carrier's most recent cost of service study are deemed used and useful and are not subject to further disallowance. An electing carrier's future capital investment commitments arising from the electing carrier's participation in RUS financing or the ARRA Broadband Stimulus program are also deemed used and useful and included in adjustments to the frozen interstate revenue requirement as they are incurred.

iii. The electing carrier's frozen interstate revenue requirement is subject to an annual reduction based either on an adjustment to reflect additional accumulated depreciation over time or a factor (similar to the productivity factor concept used with price-caps).

iv. The electing carrier's frozen interstate revenue requirement is subject to an annual increase to reflect additional expenses needed to maintain universal service or to provide an evolving expansive definition of universal service. These adjustments ensure that the rural carrier has a meaningful opportunity to recover costs, and that it is not subjected to unfunded mandates. Carriers should not have the obligation to incur additional expense without the provision of a cost recovery mechanism that will predictably provide the needed funding.

  a. To the extent that the electing carrier demonstrates a requirement for additional funding, any additional funding will be distributed from the CAF.

  b. Demonstration of justification for upward adjustment includes a showing that additional investment meets the "used and useful" standard;[13] proposed investment is deemed just and reasonable upon 15 days' notice absent Commission notification of review, which review process is complete within five months.[14]

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[13] The Commission has long relied upon the "used and useful" doctrine to consider whether specific investments are to be included in a carrier's revenue requirement. Generally, property is considered "used and useful" if it is "necessary to the efficient conduct of a utility's business, presently or within a reasonable future period." *Americal Tel. and Tel. Co.,* Phase II Final Decision and Order, 64 FCC 2d 1 at para. 111 (1977). *See also* NPRM at para. 454.

[14] The five-month review period is consistent with the established review period of Section 204 of the Communications Act of 1934, as amended (the "Act"), 47 U.S.C. § 204(a)(1). It is critical that the review process be known and finite to avoid delay or diminution of the provision of universal service.

v. The electing company's annual USF funding will be the residual of its adjusted frozen interstate revenue requirement reduced by the company's settled access charge revenues and subscriber line revenues.

vi. Because the plan provides for a residually derived USF payment, the option can be exercised either within or outside of the NECA pools.

vii. In order to address carrier concerns with shrinking access minutes, the plan provides the option for the electing carrier to move to access charge price caps with recovery from the CAF of the otherwise resulting lost access revenue needed for cost recovery.

2. Establishment of an Interim Universal Broadband Service Requirement

The fundamental policy consideration for the inclusion of broadband as a component of universal service is the adoption of a baseline service requirement. The Alliance supports the adoption of the proposed "4 Mbps down/1 Mbps up" broadband speed as an interim universal service standard[15] subject to annual review and adjustment to maintain reasonably comparable rates and services in rural areas with those available in urban areas.

While this initial benchmark may be both realistic and consistent with existing statutory requirements, we respectfully note that the data transmission speeds that are essential to education and public health, and the transmission capabilities that customers expect are growing quickly.[16] The establishment of an initial standard provides clarity and stability, and provides an appropriate basis for the further review of the evolving definition of universal service. Importantly, its adoption provides the necessary legal and policy foundation for both the NPRM

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[15] *See* NPRM at para. 109.

[16] The Act provides express authority to extend universal service support to broadband: "Universal service is an evolving level of telecommunications services that the Commission shall establish periodically under this section, taking into account advances in telecommunications and information technologies and services." 47 U.S.C. § 254(c). The 4/1 standard "represents a speed comparable to what the typical broadband subscriber receives today" (The National Broadband Plan at 135).

policy goals (the establishment of the CAF, targeted investment, etc.), and the immediate actions to institute stability for rural exchange carrier operations, as advocated by the Alliance.

3. Maintain A Universal Service "Safety Valve"

To ensure the continued provision of universal service, as it is currently defined and as it evolves, carriers must have reasonable assurance of a meaningful opportunity to recover the costs incurred. Accordingly, electing carriers should be afforded access to the CAF for defined universal service funding requirements beyond the frozen revenue requirement. Under the TSP, an electing carrier would provide cost support pursuant to established procedures to justify its request for an increase in interstate cost recovery. To avoid uncertainty and instability, the Commission would process adjustment requests within 5 months, consistent with the underlying policy of Section 204 of the Act.[17] Approved operational and capital expenses would be recovered from the CAF.

Alternatively, the utilization of models, as proposed in the NPRM, "to establish benchmarks for reimbursable operating and capital costs for rate-of-return companies" could be utilized in conjunction with this aspect of the TSP.[18] In lieu of a demonstration of company-specific costs, the established benchmark could be utilized to provide surrogate support for the need for an increase in funding to provide interstate cost recovery. The Commission and all parties should recognize, however, that a rural RoR carrier must retain the opportunity to obtain support based on its actual costs. No model could ever sufficiently predict in every instance and circumstance the costs of providing universal service under any and all circumstances. Accordingly, there should always be a safety valve process based on actual costs,

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17 47 U.S.C. § 204(a)(1).

18 NPRM at para. 201.

as described above, available to address any instance where the model and resulting benchmarks are not adequate to ensure the provision of universal service.

4. Reform Intercarrier Compensation

i. Transition Access Charges to Lower Levels with Lost Revenues Recovered from the USF

In recognition of evolutions in network usage and the necessity for intercarrier compensation reform to eliminate "indirect funding of broadband-capable networks today through our legacy high-cost programs, which is occurring without transparency or accountability for the use of funds to extend broadband service,"[19] the Alliance supports a measured and identified reduction to access charges, assuming that the affected recovery of interstate revenue requirement is appropriately allocated to the USF.

Following from its proposal as outlined above to freeze the interstate revenue requirement and recover fully from subscriber line charges, access charges and the USF, the Alliance therefore proposes that the access charge reduction be supplanted on a dollar-for-dollar basis by USF/CAF funding to avoid local rate shock and the alternative adverse financial ramifications resulting from the absence of a reasonable opportunity for the rural carrier to recover its costs.[20]

ii. Rural Carrier Price Cap Incentive

The TSP additionally proposes that a rate-of-return carrier may alternatively make an election to utilize price-caps in a manner similar to the option provided to mid-size carriers,

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[19] NPRM at para. 53.

[20] The NPRM specifically seeks comment on proposals to accommodate for universal service support lost as a result of access charge reform: "[w]e recognize that ICC revenues today remain an implicit subsidy for certain carriers, and we seek comment on how to structure the recovery mechanism to provide certainty and predictability during the transition." NPRM at para. 43.

utilizing the same rates as the mid-size carriers utilize. The rates would ultimately transition further in accordance with a transition established by the FCC that recognizes the need for revenue recovery from the CAF established to replace the lost access revenues.[21]

iii. Intrastate Access Charges

The TSP does not suggest any specific framework regarding the reform of intrastate access charges, but encourages the transition of intrastate access rates to parity with interstate rates in order to avoid arbitrage issues. With respect to any such authorized intrastate access charge transition, the cost recovery shortfall resulting from mirroring interstate access rates should be recovered from a cost recovery restructure mechanism provided from the CAF.

iv. Special Access

The TSP provides an option to enable an electing carrier to remove its special access costs from its interstate revenue requirement prior to the implementation of the freeze. The carrier would agree to cap the special access rates with a resulting incentive to establish rate offerings to market its special access at or below the capped rates.

IV. The TSP Is Consistent with Congressional and Commission USF Principles

The TSP will operate to restore needed stability to the operations of rural incumbent telephone companies in a manner that is wholly consistent with the requirements of the Act and the Commission's objectives. It will operate in a manner that ensures the continued provision of universal service and the deployment of advanced networks in rural areas, advancing the financial stability of carriers and the communities they serve, thus providing a firm foundation for rural job creation and maintenance.

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21 See, Attachment ,"Operational Specifics of the Transitional Stability Plan Option," Sec. III.B.

A. Implementation of the TSP Fulfills the Statutory Directive

Section 254(b) of the Act directs the Joint Board and the Commission to "base policies for the preservation and advancement of universal service" on principles including (1) quality services should be available at just, reasonable and affordable rates; (2) all regions of the Nation should have access to advanced telecommunications and information services; (3) reasonably comparable services at reasonably comparable rates should be available in rural and urban areas; and (4) specific, predictable and sufficient support mechanisms should be available to preserve and advance universal service.[22] The TPS satisfies each of these statutory principles.

The preservation of a methodology that ensures an opportunity for return of investment already deployed to meet rural universal service goals is critical to preserve existing universal service and provide for the survival of those entities with a proven history of advancing service.[23] In the TSP's bifurcated approach, frozen interstate legacy costs, are, by definition, specific and predictable, and will be recovered from the existing USF mechanism, which is, again by definition, sufficient to recover these costs. New or increased costs to provide broadband universal service under the Commission's evolving definition will also be targeted, defined and specifically funded pursuant to the established accountability standards built into rate-of-return regulation, or pursuant to a model adopted by the Commission to identify appropriate and permissible expense levels. The resulting system will ensure just, affordable and reasonably

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22 47 U.S.C. § 254(b).

23 As of April 6, 2011, 30 Senators had joined in a letter to the Chairman of the Commission "encourag[ing] the development of a support mechanism framework that does not jeopardize current or hamper future private sector and federal lending program investment," pointing specifically to existing investment in rural areas. Letter from Senator Mark Begich, Senator John Thune, *et al*. to Julius Genachowski, Chairman, FCC (dated April 6, 2011) ("April 6 Letter").

comparable rates in rural areas and urban areas without jeopardizing current operations and rational planning for future investment.

B. Implementation of the TSP Fulfills Commission Principles

1. The TSP promotes a modernized and focused USF.

One of the FCC's fundamental goals is to "[*m*]*odernize and refocus USF and ICC to make affordable broadband available to all Americans and accelerate the transition from circuit-switched to IP networks, with voice ultimately one of many applications running over fixed and mobile broadband networks. Unserved communities across the nation cannot continue to be left behind.*"[24] Under the TSP, additional funding requests are tied to the need of the rural carrier to make investment or incur additional expenses in order to maintain or expand the provision of universal broadband service. Recognizing that access charges were designed to provide implicit network support in an era of growth of circuit-switched services, the TSP provides an option to move forward with reduction in access charges in order to transition reliance on network support away from access revenues.

2. The TSP supports fiscal responsibility.

The Commission also seeks to "[*c*]*ontrol the size of USF as it transitions to support broadband, including by reducing waste and inefficiency*."[25] The TSP optional freeze provides a constraint on the existing legacy recovery mechanism. The only additional funding available to the electing carrier will be tied directly to the Commission's objective to expand and maintain existing universal service and the provision of broadband service. Accordingly, any such

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[24] NPRM at para. 10.

[25] *Id*.

funding will be distributed from the CAF, which will target the funding to these explicit, effective goals.

3. The TSP promotes accountability.

The FCC states that it will "[*r*]*equire accountability from companies receiving support, to ensure that public investments are used wisely to deliver intended results. Government must also be accountable for the administration of USF, including through clear goals and performance metrics for the program.*"[26] The TSP provides funding for existing expenses and established investment subject to the Commission's audit processes. Additional funding is only provided subject to the accountability the FCC seeks.

With respect to the Commission's acknowledgement that "clear goals and performance metrics" are required, the TSP requests that the FCC set the clear definition of what level of universal service may be supported by funding – the purpose is to ensure that rural carriers are never again left in the breach where the FCC suggests that it may not provide funding for investment decisions made in good faith to deploy advanced network. The FCC should be clear in setting out what service levels it deems "used and useful" and eligible for funding in order that broadband service may be defined and measured, and investment appropriately targeted.

4. The TSP supports meaningful incentives.

The FCC states that it wants to "[*t*]*ransition to market-driven and incentive-based policies that encourage technologies and services that maximize the value of scarce program resources and the benefits to all consumers.*" The TSP provides rural companies with meaningful incentives to manage their business within the frozen interstate revenue requirement. Recognizing the current reality of scarce program resources, any additional funding requests are

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[26] *Id*.

tied into the Commission's objective of targeting funding to the provision of broadband with accountability and fiscal responsibility as discussed above.

The proposed revenue requirement freeze provides the foundation for achieving an incentive plan that recognizes the distinct network conditions and circumstances of rural service provision. Under traditional incentive plans geared toward densely populated areas where carriers could reasonably predict reduced expenditure needs and growing use, focusing on capping rates was an accepted approach. But in rural areas, focus on revenues, as opposed to rates, is more appropriate because the opposite conditions hold — increased infrastructure needs and diminishing use of access minutes. Accordingly, the incentives that arise from a revenue requirement freeze for RoR carriers (accompanied by the safety "floor" of the ability to request an upward adjustment upon an appropriate cost demonstration or on the basis of approved model benchmarks) operate to encourage efficiencies, which are rewarded with a continued opportunity for the rural carrier to recover its costs and a fair return.

The overall structure of the TSP operates as an incentive to target new investment for universal service purposes, as reviewed and approved by the Commission. As the incumbent recovers its legacy investment, it will benefit by reviewing investment and deployment opportunities to upgrade its universal service offerings.

V. Additional Attributes of TSP

A. The TSP provides a "glide path" to permanent reform.

Consistent with the Commission's desire to approach intercarrier compensation reform without the harmful disruptions that could arise from a flash-cut approach,[27] the TSP provides an appropriate "glide path" to more permanent reforms, with measured steps toward necessary modifications. One of TSP's primary goals is to establish an initial freeze for the portion of a

[27] *See, e.g.,* NPRM at para. 17.

carrier's revenue requirement that will be recovered under a framework that operates in a manner similar to that currently in place. Smoothing this transition for the recovery of established investment is a "safety-valve" access to additional recovery, if the carrier can demonstrate the necessity for such increase above its frozen revenue requirement. Additional recovery from funding, resulting from additional expenses necessary to meet an evolving universal service standard or to maintain universal service, will be recovered from the newly established CAF. Similarly, the TSP proposes a transitional period within which to reduce access charges, again facilitating a path toward reform.

The TSP also addresses the Commission's criticism of RoR regulation by providing for a transition to an incentive plan adapted to the specific circumstances faced by rural incumbent carriers, retaining cost-based recovery as a necessary safety valve to accommodate universal service requirements in specific instances. Under the TSP guidelines, the opportunity for the Commission to constrain CAF funded investment and expenses either through the utilization of benchmarks or through the review of specific investment and expense proposals would alleviate its stated concerns regarding the possibility that RoR encourages inefficiency, provides "no barriers" to investment, and rewards imprudent investment.[28]

B. The TSP incorporates a fair and reasonable framework to ensure that rural carriers are not denied a meaningful opportunity to recover investment made in good faith.

The TSP's cornerstone is its recognition of the requirement for a mechanism that offers the opportunity to recover established investment and expenses. This concern for the recovery of existing costs incurred to provide universal service is echoed by policy makers[29] and is implicit

[28] *See*, e.g., NPRM at para. 171.

[29] *See, e.g.,* April 6 Letter, *supra* n. 19.

within the concept of an appropriate transition. The TSP proposes to freeze the revenue requirement to recover existing costs within the existing funding established for rural RoR carriers, and reduces that funding requirement each year as existing investment is depreciated. As a result, additional funding becomes available for new investments and expenses funded by the CAF. This measured approach is consistent with a reasoned and reasonable exercise of rulemaking authority because it avoids the harshness of a flash-cut and the even greater injustice of retroactive rulemaking that would deny rural RoR carriers the opportunity to recover existing investments and expenses undertaken to provide universal service.

While the Commission may, in hindsight, criticize the investment decisions of particular carriers, it nonetheless recognizes that "those carriers are often acting in the best interests of their customers and communities – and in a manner consistent with or even encouraged by our current rules."[30] And even as the Commission criticizes RoR generally, it does recognize that RoR carriers have made "significant progress in extending high speed Internet access services in their territories, in part due to the operation of the Commission's 'no barriers to advanced services' policy."[31]

The revenue requirements here at issue have been deemed lawful,[32] have been subject to the Commission's audit authority, and should, therefore, be and remain subject to full cost

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30 NPRM at para. 173.

31 NPRM at para. 170.

32 RoR carriers generally file rates pursuant to "streamlined" treatment, under which such rates "shall be *deemed lawful* and shall be effective 7 days (in the case of a reduction in rates) or 15 days (in the case of an increase in rates) after the date on which the rates are filed with the Commission unless the Commission takes action . . .before the end of the 7-day or 15-day period, as appropriate. 47 U.S.C. § 204(a)(3).

recovery. Blocking that recovery would be manifestly unfair and unlawful.[33] Rather, the Commission should, as described in the TSP, afford appropriate recognition of the legitimacy of past investment under existing rules while simultaneously establishing a blueprint for moving forward.

C. The TSP may be implemented quickly and efficiently

Another benefit of the TSP is that its provisions may be implemented promptly and without additional proceedings. As described in the attached Operational Specifics of the Transitional Stability Plan Option, the required steps for implementation are minimal. Other proposals, however, entail matters potentially affecting jurisdictional separations and recovery, and would, therefore, require the Commission to refer the matter to the Joint Board for further proceedings.[34]

VI. The TSP Improves Upon the Commission's Proposed Rule Revisions for Rural Rate-of-Return Carriers

A. The current situation requires immediate action.

The Commission's plan does not include a component for immediate action. However, under current conditions, (1) the recovery of past investment, and therefore current financial stability, is uncertain; (2) the conditions for recovery of future investments by rural RoR carriers are unclear and unpredictable, resulting in the stifling of investment; and (3) the resulting instability in the carriers' business climate depresses

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[33] A new legal consequence for past conduct necessarily invokes an inquiry into the concept of retroactivity. And retroactive application of a new rule will be denied "when to apply the new rule to past conduct or to prior events would work a 'manifest injustice.' " *Clark-Cowlitz Joint Operating Agency v. FERC*, 826 F.2d 1074, 1081 (D.C.Cir.1987) *See also* Bowen v. Georgetown University Hospital, 488 U.S. 204 (1988); *Verizon Tel. Cos. v. FCC*, 269 F.3d 1098 (D.C.Cir.2001)

[34] "The Commission shall refer any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations, which it institutes pursuant to a notice of proposed rulemaking. . . to a Federal-State Joint Board." 47 U.S.C. § 410(c).

their ability to create and maintain jobs, and otherwise contribute to the economic well-being of the widely-spread rural communities served by rural incumbent telephone companies. Further, the *status quo* continues to erode. Accordingly, prompt implementation of the Alliance's TSP is vastly superior to doing nothing and allowing the growth of uncertainty and erosion of the current situation. Prudent businessmen will not act in face of continued uncertainty, and the market will ultimately reflect the expense of continued delay.

B. The Commission's proposal does not ensure the provision of a meaningful opportunity for the recovery of existing investment.

As discussed above, the current recovery mechanisms will not achieve the objective of ensuring recovery of existing investment because a cap on the HCF ultimately will result in carriers recovering only a portion of their investment. The continuing reliance on a capping mechanism only perpetuates this fundamental problem with the existing high-cost USF mechanism.

As rural companies invest more in their networks, the application of the high cost formula assigns more and more cost recovery in the aggregate to the HCL fund, and as this occurs, the aggregate revenue requirement will continue to grow far above the cap. The result is a growing cost recovery gap for all rural companies. Simply changing the formula for the distribution of limited universal service funding, as proposed in the NPRM, only exacerbates the existing problem. By applying a new distribution formula to a limited fund, some rural RoR carriers will receive more funding than they would obtain under the existing rules; others will receive less; but none will have the opportunity to recover their costs without charging inordinate rates to rural consumers for universal service.

Operating under a cap where all share common funding, no company can predict what funding it will receive to recover costs on a going-forward basis because it cannot predict what additional pressures on the limited fund will develop as a result of investments by other companies that require funding. As the aggregate funding requirement grows, the funding for each individual company unpredictably declines since each company's share of the limited funding will have to be reduced. In the long run, all rural companies are harmed because the system encourages additional investment with no meaningful opportunity to recover costs under a capped fund. The TSP squarely addresses this issue within the constraint of the existing funding for rural RoR carriers, provides certainty, predictability and restores the financial stability necessary to encourage infrastructure investment in rural America.

C. TSP ensures fairer distribution of limited funding.

Absent fair access to recovery mechanisms, companies that have made significant fiber or other investments in reliance on existing rules, RUS financing and Broadband stimulus commitments will not have an opportunity, under a limited fund, to recover their good faith investment without raising customer rates far above the "comparable" level. The TSP plan, however, provides for fairer access to funding by ensuring that (1) all companies would have an opportunity to recover their existing costs; and (2) no company would be unintentionally misled or encouraged into making additional investment without a reasonable assurance of an opportunity to recover the costs of providing universal service.

Under the existing rules, companies make an investment decision based on reliance on funding, but they cannot predict the severe impact on their own cost recovery that occurs as the demand on the limited fund grows and all companies fall short in their cost recovery. An unintended consequence of the proposed rules set forth in the NPRM effectively operate to encourage some rural carriers to make investment on the basis of short-term increases in funding support which will quickly evaporate as the total funding requirement grows further and further above the capped fund. The inequity of this effect is heightened by the fact that, given the reality of a limited fund, the only source of additional funding for one company under these proposals is to reduce funding to another carrier needed to recover investments and expenses already incurred to provide universal service.

Furthermore, companies that need to incur additional expenses to provide broadband at a 4/1 level will not have an opportunity to recover the expenses, under a limited fund, without raising customer rates far above the "comparable" level. Just as fundamental fairness demands that those companies that made good-faith decisions under existing rules not be penalized, equity also requires that companies that have not yet initiated network upgrades be granted a meaningful opportunity to obtain additional funding to recover the interstate revenue requirement associated with the additional costs necessary to provide universal service.

Finally, TSP implementation would result in a fairer cost recovery mechanism than the implementation of a model implemented in the absence of an opportunity to recover actual costs. No model sufficiently provides for every circumstance, so the opportunity to prove costs must be allowed. The safety valve element of the TSP is, therefore, critical, and responsive to the recognition that a one-size–fits-all approach is rarely, if ever, appropriate.

VII. Conclusion

The TSP's objectives, together with its implementation plan set forth in the Attachment to these Comments, are wholly consistent with the Commission's goals in reforming intercarrier compensation and universal service programs. The TSP provides for the refocus and strengthening of the USF; it promotes a transition to lower switched access rates; it provides meaningful incentive regulation while allowing recovery of established investment and expenses in conjunction with the maintenance of "safety valve" elements of rate-of-return regulation fully subject to the Commission's review.

Both the existing USF distribution rules for rural RoR carriers and the proposed revision of those rules set forth in the NPRM perpetuate the uncertainty and unpredictability in the provision of USF funding required to provide universal service in rural America. The TSP offers an immediate opportunity to address that critical statutory contradiction. By adopting the TSP, the Commission can, consistent with the intent of the Act, ensure the provision of universal service mechanisms that provide predictability and sustain universal service in rural areas in a manner consistent with the objectives set forth in the NPRM.

Rural economic development, job creation and job preservation are largely dependent on the telecommunications infrastructure deployed and maintained in rural America. In the vast areas of rural America served by rural RoR carriers, the nation's rural telephone companies remain constant in their commitment to the provision of universal service to their communities. The rural companies and the consumers they serve look to the Commission to act expediently to remove the financial uncertainty and lack of predictability that currently mars the universal service mechanism. By restoring stability and predictability, the Commission can remove both the looming threat of financial inviability that rural carriers face, and the barriers that uncertainty has raised to infrastructure deployment.

Accordingly, the Alliance urges prompt adoption of the TSP as a first step in implementing necessary reforms.

Respectfully submitted,

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Transitional Stability Plan Option

I. **Establish an Interim Universal Broadband Service Requirement**

Adopt the proposed 4 Mbps down / 1 Mbps up broadband speeds as an interim universal service standard subject to annual review and adjustment to maintain reasonably comparable rates and services in rural areas with those available in urban areas.

II. Provide Revenue Assurance/Stability for recovery of established investment and operating expenses by providing rate-of-return carriers with the option to freeze their existing interstate revenue requirement, subject to upward and downward adjustments consistent with the Commission's universal service objectives.

A. Freeze each electing rural ROR carrier's interstate revenue requirement (including high cost loop fund support) as of a date certain (e.g., December 31, 2012), subject to adjustments to reflect additional committed capital and increased expenses resulting from RUS or Broadband stimulus project commitments, and adjustments needed to provide an expanded definition of universal service.

As a result of the initial interstate revenue requirement freeze, the electing carrier's existing aggregate USF funding and interstate access revenue requirement (including ICLS) will be constrained and reduced each year, as discussed below. In the event that the electing carrier subsequently incurs additional capital or operational expenses needed to provide universal service and, as a result, requires additional universal service support, any such support will be derived from the Commission's new Connect America Fund (CAF); and any such additional expenses shall be identified separately within the appropriate Part 32 account.

Each company currently subject to rate-of-return regulation may make an election to utilize this methodology to determine its future interstate revenue requirement by submitting notice of its election to the Commission by July 1, 2012.

1. Determination of first annual period interstate revenue requirement for an electing carrier.

(a) For the first annual period during which this election is effective for a cost company, the electing company's total interstate revenue requirement will be based on the electing company's most recent cost of service study adjusted consistent with item (c) below.

(b) For an electing company that is an average schedule carrier, the electing company's total interstate revenue requirement will be the sum of that company's prior year settlement from the National Exchange Carrier Association ("NECA") pool, prior year subscriber line charges, and prior year USF revenues, adjusted consistent with item (c) below.

(c) The electing company's initial interstate revenue requirement, as established by section (a) or (b) above shall be adjusted to reflect any additional depreciation expense and adjustment to the return on investment necessary to reflect additions to capital investment arising from capital commitments incurred by the electing company prior to December 31, 2011 as a result of participation in Rural Utility Service ("RUS") financing or RUS or NTIA broadband stimulus programs, or other capital commitments made prior to December 31, 2011. With regard to any such capital commitments, revenue requirements shall be adjusted in accordance with Part 32 and Part 36 regulations as additional plant is placed into service.

2. Determination of subsequent annual period adjustments to the interstate revenue requirement of an electing carrier.

The subsequent period interstate revenue requirement for each electing company will be reduced in accordance with the carrier's election to utilize option (a) or (b) below. The electing company shall make a one-time determination of which option it will utilize and notify the Commission of its election concurrent with the provision of the company's notice to the Commission required by Section A, above.

(a) The electing company's interstate revenue requirement shall be reduced annually by that amount equal needed to reflect the reduction in the company's total regulated plant in service less accumulated depreciation as determined annually in accordance with Part 32 of the Commission's rules for purposes of conducting a cost of service study pursuant to Part 36 of the Commission's rules.

(b) Alternatively, the electing carrier may elect that its interstate revenue requirement shall be reduced annually by the total of 3% reduced by one-half of the nationwide CPI inflation factor.

B. ***Maintaining a Rate of Return Safety Valve Process***

Carriers committed to the provision of universal service must have reasonable assurance of a meaningful opportunity to recover the costs of providing universal service through the continued application of RoR where necessary.

In the event an electing carrier requires additional funding in order to support the provision of an expanded definition of universal service or to maintain the provision of universal service, any funding provided in accordance with the rules proposed below will be derived from the CAF with the following exception.

The electing company may make a one-time only election to return to full rate-of-return regulation and determine its interstate revenue requirement in accordance with the effective jurisdictional separations rules in effect for the determination of the interstate revenue requirement for the subsequent periods in effect at the time of the election, including the utilization of any model adopted by the Commission for the purpose of identifying permissible expense levels to provide universal service in the carrier's study area.

Support requirements from the CAF for an electing carrier will be established in accordance with the following procedures.

1. An electing company seeking CAF support will file cost support to justify the requested increase by July 1 of the year prior to the period for which the company seeks the adjustment. The cost support information will be submitted in a format consistent with FCC Rules Parts 32 and 36; additional proposed capital investment to provide broadband connectivity in accordance with the Commission's (evolving) definition of universal service will be directly assigned to the interstate jurisdiction consistent with the Commission's determination that the provision of broadband transmission service is jurisdictionally deemed interstate. Similar to tariff filing rules, the carrier will provide a description and justification together with the cost support information to demonstrate that the additional investment and expenses proposed for inclusion in the interstate revenue requirement will be used and useful. Any resulting increase in funding will be provided through the CAF.

(a) In order to avoid uncertainty and instability, the FCC will process any request for adjustment to the interstate revenue requirement within no more than 5 months of the date of application, consistent with the underlying policy set forth in Sec. 204 of the Act.

(b) Approved operational expense increases will be added to the company's annual interstate revenue requirement beginning with the following annual period subsequent to the approval. Any such operating expenses shall be separately identified within the company's Part 32 accounting records as "additional CAF funded interstate expenses" and any such expenses will not be subject to the reductions provided by section A.2.(b), above.

(c) Approved capital expense increases (the annual depreciation expense and authorized return on the proposed additional investment) will be added to the company's annual interstate revenue requirement beginning with the following annual period subsequent to the approval. Any such capital expenses shall be separately identified within the company's Part 32 accounting records as "additional CAF funded interstate expenses" and maintained separately within the Part 32 account categories associated with plant and depreciation.

(d) Funding associated with approved adjustments increasing the company's interstate revenue requirement will be distributed from the Commission's Connect America Fund ("CAF"). Depending on how the Commission elects to establish its rule for funding from the CAF, the funding of needed capital investment could alternatively be achieved through one-time funding of requests for capital investment funding.

C. Interstate Revenue Sources

1. Frozen interstate revenue requirement is recovered from Subscriber Line Charges (SLCs), interstate access charge revenues (NECA pooled settlements or individual company billed and kept access revenues) and USF.

2. For electing RoR companies, all elements of High Cost USF support are combined. Recognizing that the High Cost Loop fund is capped, that portion of the capped fund associated with the funding of the electing carriers in 2011 will be established and frozen; the remaining High Cost Loop Funding will continue to be available to the rate-of-return carriers that do not elect the incentive Transitional Stability Plan.

The total USF payment to an electing carrier is derivatively derived:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

Similar to current pooling practices, companies will receive a monthly USF payment from USAC based on projections.

The USF distribution will also include funding from any prospective restructure mechanism established by the FCC to offset revenue losses resulting from reductions in intrastate and interstate access rates contemplated by the FCC.

The access revenue component for an electing company may be obtained either on an individual company basis or a pooled basis within the NECA pools (see, Sec. III, below).

An annual true-up process within USAC will be needed to address long-falls or shortfalls.

III. Intercarrier Compensation – Access Charge Transition

The Transitional Stability Plan proposes two options for rural rate-of-return carriers:

A. Maintain Current Switched Access Charges and Follow The Transition Ultimately Established By The FCC For Rural RoR Carriers.

(1) Pooling – for those electing cost companies that are in the NECA tariff and pools, they will continue to follow the same process that they follow today with the following exception. Instead of providing NECA with an annual cost of service study, the electing company will provide NECA annually with revisions of the results of the cost study utilized to establish the company's initial frozen interstate revenue requirement (see, Sec. II A. 1.); the revisions will reflect the authorized adjustments made consistent with the procedures set forth in Section II, A. 2a. The frozen annual cost of service study, subject to reductions provided in Section II A. 2, will become the basis for determining the electing company's interstate access revenue requirement in the same way that the annual cost of service study submitted by each cost company is utilized today. The electing company's pooled access settlement revenue is utilized in the formula set out in Sec. II C. 2. for the determination of the company's USF funding requirement:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

The treatment of average schedule companies electing to participate in the transitional incentive plan option should not require any adjustment within the pooling process. The average schedule company's total annual average schedule settlements are utilized as the "interstate access revenues" in the formula set forth above. With respect to the adoption of a prospective intrastate access charge transition by the Commission, the "Total Interstate Revenue Requirement" will include the amount of intrastate revenue reduction created by reducing intrastate access rates which will be recovered from the RM.

(2) Electing companies that are not in the NECA Pool – any such company may elect to continue to follow the same process that they follow today with the following exception. Instead of revising its annual tariff filing on the basis of an annual cost of service study, the electing company will determine and justify its annual rate filing on the basis of the cost study utilized to establish the company's initial frozen interstate revenue requirement (see, Sec. II A. 1.) with revisions made annually to reflect the authorized adjustments made consistent with the procedures set forth in Section II, A.2.

The revised annual cost of service study will become the basis for the electing company's interstate access filing pursuant to the same process by which the annual cost of service study submitted by each cost company is utilized today. The electing company's resulting interstate access revenue requirement will then be utilized in the formula set out in Sec. II C. 2. for the determination of the company's USF funding requirement:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

With respect to the intrastate access charge transition, "Total Interstate Revenue Requirement" will include the amount of intrastate revenue loss resulting from intrastate access charge reductions that is shifted to the interstate jurisdiction for recovery from the RM.

B. Access Charge Incentive Option

A rate-of-return carrier may alternatively make an election to utilize price-caps in a manner similar to the option provided to mid-size carriers, utilizing the same rates as the mid-size carriers utilize. The rates will ultimately transition further in accordance with a transition established by the FCC that recognizes the need for revenue recovery from the CAF established RM to replace the lost access revenues.

This option for small rural rate-of-return study areas is distinct from the option provided to the mid-size carriers. Under the mid-size carrier price cap plan, the ICLS element was frozen on a per line basis, and ICLS recovery would diminish as lines are lost, regardless of the fact that there was no reduction in the cost to the carrier to provide carrier of last resort ("COLR") service throughout its study area.

Under this option in the Transitional Stability Plan, the ICLS (or equivalent funding) is not reduced because the total interstate revenue requirement has been frozen (subject to the adjustments provided in Sec. II A.). Operationally, the result is the same as lowering the access charge and recovering the resulting lost access revenues from the CAF RM. The electing company's total interstate access revenues will be utilized in the formula set out in Sec. II C. 2. for the determination of the company's USF funding requirement:

USF Payment = Total Interstate Revenue Requirement less Interstate access revenues less SLC revenues

To the extent that the FCC subsequently directs a further transition of the (interstate) access charge rates, the resulting access revenue loss will be recovered from additional CAF RM payments.

With respect to any intrastate access charge transition authorized by the Commission, "Total Interstate Revenue Requirement" will include the amount of intrastate revenue requirement shifted to the interstate jurisdiction by the Commission; the resulting additional interstate revenue requirement will be recovered from the RM.

3. Additional Special Access Option

A carrier electing the Transitional Stability Plan incentive proposal should have the additional option to remove its special access costs from its interstate revenue requirement prior to the implementation of the interstate revenue requirement freeze provided for in Sec. II A. Under this option, the carrier would agree to cap its special access rates.

As a result, the carrier would have the incentive to market its special access at or below the capped rates because the revenues would be subject to bill and keep; and these revenues would not offset the interstate frozen revenue requirement (which would have already been reduced to reflect the removal of special access costs).