

***PUBLIC - RE REDACTED FOR PUBLIC INSPECTION***

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

In the Matter of )  
 )  
Connect America Fund ) WC Docket No. 10-90  
 )  
Accipiter Communications Inc. Petition for )  
Waiver of the Commission's Rules Implementing )  
Reform of Universal Service Support )

**PETITION FOR TEMPORARY WAIVER**

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April 18, 2012

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**SUMMARY**

Accipiter Communications Inc. ("Accipiter"), respectfully requests temporary waiver of certain of the rules adopted in the Commission's *Report and Order*, FCC 11-161, released November 18, 2011 in WC Docket No. 10-90. There are fundamental errors in the methodology and assumptions underlying the rules both in general and as applied to Accipiter. Moreover, the rules do not account for the fact that Accipiter is an early stage company that is growing rapidly. Although the current rules lack the clarity necessary to perform an accurate evaluation, it appears that the application of the Commission's new rules and policies to Accipiter, without alteration or temporary waiver, could have a deleterious impact on the company.

Immediate application of the current rules and non-finalized preliminary formulas adopted in the *Report and Order* to Accipiter will undermine Accipiter's ability to recover its costs and would be directly contrary to the public interest. There are several fundamental problems raised by the *Report and Order* that, left unchanged or unclarified, will have a serious financial impact on Accipiter. The *Report and Order* is based upon methodologies and assumptions which are in some cases plainly erroneous and in other cases fail to address the real cost drivers for a carrier such as Accipiter. As Accipiter has demonstrated in its Petition for Reconsideration, submitted in this docket on December 29, 2011, these methodologies are in many instances flawed and subject to erroneous inputs. The Commission has compounded this problem by failing to provide sufficient information regarding its methodology to enable Accipiter to predict accurately the long term financial effects of the new rules – meaning that Accipiter cannot predict with certainty the scope of the financial impact that the *Report and Order* will cause. Notwithstanding that the rules will begin to affect Accipiter in July, the Commission still has not provided this needed clarification.

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Further, the *Report and Order* fails to account properly for the unique circumstances an expanding carrier like Accipiter confronts. The critical factor for Accipiter is subscriber growth. Accipiter's current per line costs are a product of the fact that it is at an early stage of network deployment. Unlike the majority of ILECs Accipiter is expanding its service and adding new subscribers. But for the effects of the *Report and Order*, Accipiter expects robust growth to continue and, given reasonable time, Accipiter will grow to serve sufficient access lines to be beyond the effect of the caps and limitations established in the *Report and Order*. If, on the other hand, Accipiter is not afforded this limited additional time to grow, the Commission's new regime could cause Accipiter to fail, default on its loans and cease serving its subscribers, some of whom have no service alternative. In that event, the effects of the Commission's new rules would be not only arbitrary and capricious, but also confiscatory as to Accipiter and directly contrary to the goals of the Communication Act for Accipiter's subscribers. Accordingly, Accipiter respectfully submits that the public interest will best be served by granting Accipiter a temporary waiver to allow the company to continue expanding service and gain sufficient subscribers, as well as provide time for the FCC to adjust and finalize its rules, so that application of the rules does not cause the company to fail.

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**PETITION FOR TEMPORARY WAIVER**

Accipiter Communications Inc. ("Accipiter"), pursuant to Section 1.3 of the Commission's rules, 47 C.F.R. § 1.3, hereby requests temporary waiver of certain of the rules adopted by the Commission's *Report and Order*, FCC 11-161, released on November 18, 2011 (the "*Report and Order*" or "*Order*") in the above-captioned proceeding. As shown below the application of the Commission's new rules and policies to Accipiter, without alteration or waiver, could have a deleterious impact on the company and would be contrary to the public interest.

**I. INTRODUCTION.**

At this time it is not possible to compute precisely the effect of the new rules on Accipiter. Not only have the rules not been finalized in certain instances, but the correction of certain errors in the methodology underlying the rules will affect Accipiter as well as other carriers. Because of the interaction of the effects of these changes, Accipiter cannot precisely predict what the final result will be. In the absence of the necessary clarification, Accipiter has attempted to calculate the effect of the rules on Accipiter based upon its own assumptions and the provisions of the rules as they stand now. Accipiter thus seeks a temporary waiver which

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will minimize the impact of these USF changes until six months following the time when the formulas authorized by the rules are finally clarified. At that time, Accipiter will seek a further temporary waiver if necessary. Grant of this waiver will assure that the company can maintain services to existing subscribers including those for whom Accipiter is the only service alternative.

Accipiter therefore respectfully requests waiver of the FCC rules as follows:

- Accipiter requests waiver of Section 54.302 of the FCC Rules (\$250.00 per line cap) until either December 31, 2014 or December 31, 2015.<sup>1</sup> This waiver request is predicated on the assumption that the regressions caps do not apply to Accipiter. Once they do apply, Accipiter may need to modify this waiver request.
- Accipiter requests a waiver of the FCC rules so that the regression caps would not apply to Accipiter until six months after the FCC has made updated regression cap formulas publicly available and corrected the errors and incorrect assumptions and methodologies in its regression cap formulas.<sup>2</sup>

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<sup>1</sup> The FCC has not clarified which line count will be used to calculate the per line cap. If the Commission uses Accipiter's 2009 loop count and applies the line counts from the NECA studies, which are two years in arrears, Accipiter will require a waiver of the \$250 per line cap until December 31, 2015. If the Commission uses Accipiter's 2011 loop count but updates the loop count currently there, because these counts are substantially higher, Accipiter will require this waiver only until December 31, 2014.

<sup>2</sup> *Connect America Fund*, Report and Order and Further Notice of Proposed Rulemaking, WC Docket No. 10-90, FCC 11-161, ¶¶ 210-26 (rel. Nov. 18, 2011).

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- Once these regression cap assumptions and methodologies have been corrected, clarified, and finalized, Accipiter may require a modification of its waiver to account for those changes.

The most relevant circumstance unique to Accipiter which justifies the grant of this waiver is the company's current stage of investment and subscriber growth. In recent years the company made significant investments to extend its network into previously unserved areas. The company is now positioned to add customers with relatively smaller incremental capital expenditures and operating expenses. For this reason, Accipiter's ongoing subscriber growth can be expected to average down the company's USF support to levels that are within the limitations defined by the FCC Order. However, if the rules are applied immediately, according to Accipiter's estimates of the effect of the FCC's unfinalized formulas the company will fail.

At this time, quantifying the duration of the needed waiver is difficult due to the lack of clarity and finalization of the new USF procedures set forth in the *Report and Order*. However, given that the Commission has decided to implement these procedures as early as July 1, 2012, Accipiter must seek a waiver now out of an abundance of caution. Accipiter intends that the waiver be granted for a limited duration, but without finalization of the rules and clarity as to their implementation Accipiter cannot accurately quantify the length of time that the waiver will be required.<sup>3</sup>

Accipiter requests this temporary waiver because:

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<sup>3</sup> Importantly, Accipiter's waiver request is based upon the FCC rules as Accipiter presently understands them and the FCC's unfinalized regression formulas. Once the rules are clarified, Accipiter will be able to determine how long the waiver will be needed. Significant change in the rules would potentially result in significant change in the required waiver.

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- The FCC rules are based upon erroneous assumptions and methodologies as applied to Accipiter.
- Without a waiver, based upon Accipiter's projections as to the effect of the rules, immediate application of the unmodified rules to Accipiter could cause it to become insolvent.
- Without waiver the company will be unable to support services to approximately \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* telephone subscribers who have no terrestrial alternative for telephone or broadband services<sup>4</sup>. Further, the existing network investment could not be used to extend service to approximately \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* additional establishments that currently have no terrestrial telephone or broadband service alternative.
- Grant of the waiver is consistent with USF purposes and will ensure the availability of robust voice and broadband services to previously unserved areas.
- Failure to grant a waiver will lead to needless confiscation of Accipiter's property. Accipiter is an early stage growing company. Accipiter believes its ongoing growth will allow it to come within the FCC's new per-line limitation within a relatively short time.

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<sup>4</sup> While some of these telephone subscribers also have access to wireless voice services, Accipiter's network provides the backhaul circuits to the wireless providers' towers serving the area. If Accipiter's network was eliminated, these wireless towers would no longer be connected to the PSTN.

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- The stated purpose of the FCC’s reform as applied to rate-of-return carriers is to provide “incentives for rational investment and operation.” Accipiter’s investment in the company’s service area was initiated several years ago with the understanding that growth would bring the company’s costs in line with normal investment and operational costs. The company can achieve compliance with the FCC’s USF limitations if it is allowed to continue to grow in its service area. The FCC order recognizes the need for a transition period for implementing USF reforms. Depending upon the changes that are made to the rules when they are finalized, Accipiter may require more time than the transition period currently proposed by the FCC. However, the time period for which Accipiter’s waiver is likely needed is reasonable considering stage of development of Accipiter network and the service life of telecommunications plant in which Accipiter has recently invested.
- Granting the requested waiver would avoid an unnecessary risk of default by Accipiter on its existing \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* in RUS debt.

**II. WAIVER OF THE COMMISSION’S RULES IS WARRANTED**

Waiver of the Commission’s rules is appropriate where “particular facts would make strict compliance inconsistent with the public interest.” *AT&T Wireless Services, Inc. v. FCC*, 270 F.3d 959, 965 (D.C. Cir. 2001), citing *Northeast Cellular Tel. Co. v. FCC*, 897 F.2d 1164, 1166 (D.C. Cir. 1990). The Commission may waive its rules for “good cause” if “special circumstances warrant a deviation from the general rule and such deviation will serve the public

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interest.” *Northeast Cellular*, 897 F.2d at 1166. In support of its waiver request, Accipiter provides the following information as directed in paragraph 542 of the FCC’s *Report and Order*.

**A. Density characteristics**

Accipiter is an Incumbent Local Exchange Carrier holding a Certificate of Convenience and Necessity (“CC&N”) granted by the Arizona Corporation Commission (“ACC” or “Arizona Commission”) to provide local telephone service to a study area of 1,010 square miles northwest of Phoenix, Arizona. There are approximately 4,600 inhabited residences within the study area<sup>5</sup>,

and most of the area is very sparsely populated. As of December 2011 Accipiter serves

\*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* regulated loops (\*\*BEGIN

CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* residential and \*\*BEGIN CONFIDENTIAL

[REDACTED] END CONFIDENTIAL\*\* business) on \*\*\*BEGIN CONFIDENTIAL [REDACTED]

[REDACTED] \*\*\*END

CONFIDENTIAL. Essentially all of the company’s lines may be reached with high speed

Internet services. Of these, \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* lines are

served by fiber-fed digital loop carrier systems and the remainder are served by fiber-to-the-

home (“FTTH”) facilities. Accipiter’s fiber network serves customers contained in seven

distinct population centers.

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<sup>5</sup> Accipiter serves a four square mile area immediately South of its Lake Pleasant exchange area that is not included in its study area. Accipiter’s petition for study area waiver for that territory was denied by the Wireline Competition Bureau on September 1, 2010. Accipiter filed an Application for Review with the Commission on October 1, 2010. The FCC has not acted on the Application for Review.

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Establishing cable routes in Accipiter’s geography requires construction methods that are much more costly than in other areas of the country. Accipiter’s Arizona study area contains significant areas of desert, mountains, canyons and rocky terrain. The study area also contains the entirety of Lake Pleasant, a 15 square mile reservoir which draws thousands of recreational visitors per year. \*\*BEGIN CONFIDENTIAL

[REDACTED]

[REDACTED]

[REDACTED] END CONFIDENTIAL\*\*

Accipiter was incorporated in 1995 and in that year was granted a Certificate of Convenience and Necessity (“CC&N”) by the ACC to serve portions of Maricopa and Yavapai counties in Arizona.<sup>6</sup> The original Accipiter service territory encompassed approximately 650 square miles and 115 occupied residences.<sup>7</sup> As the Arizona Commission found

“many residents of the amended proposed service area support Accipiter’s efforts to expand telephone service in the area. We heard from a number of residents of the enormous construction

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<sup>6</sup> *In The Matter of the Application of Accipiter Communications Inc. for a Certificate of Convenience and Necessity Authorizing the Construction and Operation of a Public Utility Telephone System in Portions of Maricopa and Yavapai Counties, Arizona*, Decision No. 59346 (Docket U-2847A-95-0026). (“*Accipiter CCN Order*”). It is noteworthy that Accipiter’s initial growth was seriously constrained by the pressure of an anticompetitive exclusive dealing arrangement between Cox Communications and the developer of the Vistancia subdivision that was dissolved following the commencement of investigation by the U.S. Department of Justice Antitrust Division and the Arizona Corporation Commission. This arrangement is described in Comments of Accipiter Communications, Inc., WC Docket No. 10-90, et al, 6 (filed April 18, 2011) (“*Accipiter Comments*”), which is incorporated by reference. Remnants of the arrangement, however, remain in place.

<sup>7</sup> Accipiter added additional service area as depicted on the map attached as Exhibit 1 so that its service territory now encompasses 1010 square miles.

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charges USW [US West, subsequently Qwest] has quoted to extend service to remote locations in the area. One resident commented that USW would charge \$20,000 to extend service 100 yards to his property. Another spoke of a \$200,000 charge to receive service from USW.”<sup>8</sup>

As is true in many rural service areas, the Accipiter’s service proposal was made possible by a combination of USF support provided under the Commission’s Universal Service programs and low interest loans for rural telecommunications development provided by the Department of Agriculture Rural Utilities Service. As a result of the support provided by these programs, Accipiter was able to deploy service charging rates of \$16.78 per month for residential service and \$35.78 for business service. As the Arizona Commission noted, prior to the Accipiter proposal, residents in the area were quoted prices of tens or even hundreds of thousands of dollars to pay for the extension of ordinary telephone service to their homes. The Commission’s Universal Service program and the Agriculture Department’s RUS lending program working together as intended by Congress placed these rural residents on par with residents of urban areas. Immediate application of the Commission’s new rules without waiver threatens Accipiter’s ability to continue to provide service in the areas where more service is most needed and threatens to undermine the Congressional purpose served by the RUS and USF programs.

As Accipiter has already described to the Commission, on June 20, 2006, Accipiter filed what it believed would be a routine request with the FCC for a study area waiver to include the

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<sup>8</sup> At the time the Certificate was granted, USW “provided telephone service to approximately 22 customers (“the existing subscribers”) over approximately 30 access lines”. *Accipiter CCN Order* at 3.

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Vistancia extension within its study area.<sup>9</sup> More than four years later, on September 1, 2010, the Commission denied Accipiter's study area request even though Accipiter had disclaimed any additional USF support that might flow from the inclusion of the Vistancia extension within its larger study area. The denial of the study area waiver is of direct relevance here because it precludes Accipiter from combining the low density areas of its larger service territory with a higher density area in the Vistancia development, thereby lowering its overall average costs, reducing its need for subsidy and enhancing its ability to repay its RUS loans. Denial of the waiver needlessly exacerbates what is already a difficult cost and service problem without any countervailing public benefit. It also works against the Commission's objective here to reduce high cost subsidies. Accipiter's Application for Review of the waiver denial has been pending since September 2010 with no action by the FCC.

**B. Alternate providers**

Cox Communications (the only other landline provider in the Accipiter service area) operates hybrid-fiber coax network which passes approximately 3,900 homes in Accipiter's study area and provides voice and broadband services over these facilities. Accipiter's network currently passes approximately 2,100 of the homes also passed by Cox in the study area.<sup>10</sup> All of the Cox-served subdivisions are within three small areas comprising 6.5 square miles in

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<sup>9</sup> See Comments of Accipiter Communications, Inc., WC Docket No. 10-90, et al, 6 (filed April 18, 2011) ("Accipiter Comments"); Accipiter Communications Inc. Petition for Reconsideration or Clarification, WC Docket No. 10-90, et al, 6-7 (filed Dec. 29, 2011) ("Accipiter Petition") (incorporated by reference).

<sup>10</sup> Accipiter also passes approximately \*\*BEGIN CONFIDENTIAL ■ END CONFIDENTIAL\*\* homes not passed by Cox and is planning to extend its network to an additional \*\*BEGIN CONFIDENTIAL ■ END CONFIDENTIAL\*\* homes not passed by Cox.

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Accipiter's service territory. Cox does not undertake to serve the remaining 1003.5 square miles of Accipiter service territory. (See Exhibit 1).

Accipiter has already described to the Commission the particular challenges Accipiter faced in serving its service territory due to exclusive service arrangements.<sup>11</sup> In particular, the developer of a master planned development in Accipiter's service area negotiated an exclusive service arrangement with Cox Communications, including an extraordinary easement feature that made it almost impossible for any other service provider to install landline networks in the area. Although this arrangement was ultimately withdrawn following an investigation by the United States Department of Justice Antitrust Division, the existence of the arrangement prevented Accipiter from competing in the effort to gain customers in an initial sign-up in the development.<sup>12</sup>

All the homes passed by Cox are contained within subdivisions where Cox secured some form of a "preferred provider" agreement with the developer before extending its facilities. Plainly, one intent of these preferred provider agreements was to create a market environment which strangles competition for telecommunications services. The impact upon Accipiter is that either the company chooses not to serve a high-density area and thus is deprived of serving densities where economies of scale can be achieved or Accipiter serves the area at a higher cost than what would otherwise be required.

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<sup>11</sup> Accipiter Comments at 5.

<sup>12</sup> See Accipiter Comments at 5; Accipiter Petition at 5-6.

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Wireless providers have coverage in areas beyond Cox’s footprint. Signal strength is poor and sporadic in some areas, non-existent in others. To Accipiter’s knowledge wireless broadband is limited to 3G service where available and that capacity is inadequate to serve all residents with broadband. To Accipiter’s knowledge, all of the cell sites located in the rural portions of Accipiter’s study area utilize Accipiter’s transport circuits to reach the cell tower. Thus, without Accipiter’s network, these cell sites would lose connectivity to the PSTN.

**C. Accounting for Unused or Spare Equipment**

Accipiter accounts for the cost of spare equipment and facilities in the associated primary plant account, pursuant to the Uniform System of Accounts (Part 32) of the FCC’s rules. The assignment of spare equipment and facilities is performed in accordance with the Jurisdictional Separations Procedures (Part 36) of the FCC’s rules. Part 36 outlines the procedures that are to be used in assigning Central Office Equipment (COE) and Cable and Wire Facilities (CWF) to separations categories, including the assignment of spare equipment and facilities. Generally, unused or spare equipment and facilities are assigned in the same fashion as the equipment and facilities in use in the same account. Set forth below is a summary of Accipiter’s categorization procedures for CWF and COE, including unused and spare equipment and facilities.

From a CWF perspective, Accipiter has **\*\*BEGIN CONFIDENTIAL [REDACTED]**, **END CONFIDENTIAL\*\*** that carries interoffice traffic to the meet point with its tandem provider. The **\*\*BEGIN CONFIDENTIAL [REDACTED]** **END CONFIDENTIAL\*\*** connecting to a digital loop carrier (DLC) that serves end user customers. Of these **\*\*BEGIN CONFIDENTIAL [REDACTED]** **END CONFIDENTIAL\*\*** are assigned to the provision of subscriber services (Category 1 – Subscriber Loop) and the remaining **\*\*BEGIN CONFIDENTIAL [REDACTED]** **END CONFIDENTIAL\*\*** are assigned to the

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provision of interexchange services (Category 2 – Wideband and Exchange Trunk and Category 3 – Toll). The **\*\*BEGIN CONFIDENTIAL** [REDACTED] **END CONFIDENTIAL\*\*** from the DLC to the meet point with the tandem provider. All **\*\*BEGIN CONFIDENTIAL** [REDACTED] **END CONFIDENTIAL\*\*** fibers on this segment are assigned to the provision of interexchange services (Category 2 – Wideband and Exchange Trunk and Category 3 – Toll). The remainder of the CWF facilities are used in the provision of subscriber services and are therefore assigned to Category 1 – Subscriber Loop.

Central Office Equipment is assigned to separations categories based on the functionality and utilization of the equipment. All switching equipment in the local switching account, with the exception of power and common equipment, is assigned to Category 3 – Local Switching. Transmission equipment is assigned or allocated to a variety of sub-accounts based on the services provided and the utilization of the equipment, including functionality such as: Digital Subscriber Line, Exchange Wideband, Exchange Trunk, Subscriber Line, Interexchange Wideband, Toll, and Host Remote. Direct assignments to categories are made when a specific piece of equipment is used for an individual service. When a piece of equipment is used for multiple functions, the cost of that equipment is allocated based on utilization. Depending on the type of equipment, this allocation is either based on the number of customers served or the number of circuits assigned to each service. Power and common equipment are allocated across all other categories of COE based on the relative investment in each category.

**D. Corporate Operations Expenses**

The labor and benefits expense assigned in each category is based upon employee timesheets and therefore is distributed across multiple categories. The majority of the labor and benefits expense assigned to corporate operations is generated by **\*\*BEGIN CONFIDENTIAL**



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Basic Local Phone service with four calling features: Residential is priced at \$19.95/month, Business is priced at \$39.95/month. This offering is the Basic Local Phone Service with a choice of any four of Accipiter's calling features. The customer can add long distance and EAS is included.

Basic Local Phone with twelve calling features: Residential is priced at \$29.95/month, Business is priced at \$49.95/month. This offering is the Basic Local Phone Service with a choice of any twelve of Accipiter's calling features. The customer can add long distance and EAS is included.

Low Use Option Phone Service: Offered only to residential customers at \$12.00/month. This offering is a restricted phone service only allowing 25 outgoing local calls per month. Outgoing local calls in excess of 25 per month are charged \$0.20 per call. No features can be added to this phone service, however long distance service can be added and EAS is included.

Additional Service: In addition to Basic Local or Low Use Option service, the customer may subscribe to a variety of long distance and high speed Internet services as set forth below:

- Long-Distance - \$.05/minute, including U.S. and Canada.
- Unlimited Long-Distance - \$20.00/month includes U.S. and Canada.
- High Speed Internet Service
  - 1.5 Mbps down/768Mbps up -\$29.95 (Copper/DSL only)
  - 6 Mbps down/1Mbps up - \$36.95 (Copper/DSL only)
  - 6 Mbps down/1Mbps up - \$30.00 (FTTH)
  - 18 Mbps down/3Mbps up - \$49.95 (FTTH)
  - 27 Mbps down/5Mbps up - \$64.95 (FTTH)
  - 40 Mbps down/5Mbps up - \$79.99 (FTTH)
  - 60 Mbps down/5Mbps up - \$94.95 (FTTH)

All of the services listed above can be bundled. Customers who bundle receive a bundle discount. The following table sets forth Accipiter's current bundled offerings:

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Current Residential Internet/Phone Bundle Offerings (Fiber-to-the Home)

Name	Speed	Internet Price	Phone Price	Total Bundle Price
Z6 + Security Line	6 Mbps dn/1 Mbps up	\$14.26	\$12.00	\$26.26
Z18 + Security Line	18 Mbps dn/3 Mbps up	\$27.25	\$12.00	\$39.25
Z27 + Security Line	27 Mbps dn/ 5 Mbps up	\$42.25	\$12.00	\$54.25
Z40 + Security Line	40 Mbps dn/5 Mbps up	\$57.25	\$12.00	\$69.25
Z6 + Basic Phone	6 Mbps dn/1 Mbps up	\$30.04	\$16.78	\$46.82
Z18 + Basic Phone	18 Mbps dn/3 Mbps up	\$49.95	\$16.78	\$66.73
Z27 + Basic Phone	27 Mbps dn/ 5 Mbps up	\$59.95	\$16.78	\$76.73
Z40 + Basic Phone	40 Mbps dn/5 Mbps up	\$79.99	\$16.78	\$96.77
Z6 + 4Life	6 Mbps dn/1 Mbps up	\$30.04	\$19.95	\$49.99

**F. Services other than voice:**

The only non-voice service Accipiter offers on loops supported by USF is DSL/FTTH broadband Internet service. As of December 31, 2011, Accipiter's residential Internet take rate for Fiber-to-the-Home users was \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* and the residential Internet take rate for DSL was \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\*.

**G. Procedures for Allocating Shared and Common Costs Between Incumbent LEC Regulated Operations and Other Unregulated or Unsupported Operations**

Accipiter has developed a Cost Allocation Manual (CAM) which provides account level procedures for the allocation of costs. The CAM is attached as Exhibit 2.



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- a. [REDACTED]
  - b. [REDACTED]
  - c. [REDACTED]
  - d. [REDACTED]
  - e. [REDACTED]
3. [REDACTED]  
[REDACTED]  
[REDACTED] END CONFIDENTIAL\*\*

Approximately \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* of Accipiter’s subscribers would have no other provider available to provide terrestrial voice and broadband services. Approximately \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* subscribers would have another wireline provider available, but that provider would enjoy a monopoly which had previously been undone through efforts of the Arizona Corporation Commission and the U.S. Department of Justice.

**K. Analysis of financial forecast**

Accipiter has attempted to determine the duration of the requested waiver. Unfortunately the final implementation of the rules is still unclear and, as proposed, the reform measures make predicting the future impact of the rules impossible. In an effort to establish parameters for the waiver request the company has prepared two forecasts. The first forecast (Exhibit 5) shows the effect of application of the \$250 per line cap under the assumption that the regression caps do not apply. Two versions of this forecast are provided because the FCC has not clarified whether loop counts for calendar year 2010 or 2011 will be used for the calculation of the cap. As shown, Accipiter’s rapid growth in line count removes the effect of the \$250 per line cap in

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either 2014 or 2015, assuming that the regression caps do not apply. The second forecast (Exhibit 6) shows the effect of the application of the regression caps as accurately as Accipiter is able to estimate it at this time. Because the regression analysis has not been finalized by the FCC precise calculation is impossible.

As Accipiter has previously shown to the Commission and as understood by Accipiter, the expense limitations proposed through the quantile regression method are based upon grossly inaccurate inputs for Accipiter. Peer reviews and other industry comments confirm that the currently proposed formula requires major revision from both a statistical and practical standpoint. Since Accipiter is experiencing subscriber growth which reduces its average costs, Accipiter believes that if the FCC develops a reasonable methodology for limiting capital expenditures and operating expenses, Accipiter will experience minimal (if any) revenue reductions from this aspect of the order and a limited duration waiver will be needed if one is needed at all.

However, working with the formulas as currently proposed by the FCC, the forecasted results of the proposed reforms on Accipiter's operations are dire. Accipiter's prediction shows that absent a waiver, the company will **\*\*BEGIN CONFIDENTIAL** [REDACTED]

[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED]  
[REDACTED] **END CONFIDENTIAL\*\***

The financial forecast presented in Exhibit 6 relies upon a number of assumptions. First, Accipiter used a network construction plan which provides a balance of funding in suburban

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density areas and currently unserved rural density areas. The suburban investment is included to offset Accipiter's high costs in the rural area and thus balance the study area investment to meet FCC requirements and lower Accipiter's dependence upon USF support. The rural investment is included because of Accipiter's regulatory role as the carrier of last resort in its ACC-approved service territory to extend service to unserved residents of the service area. Additionally, Accipiter's future financing from RUS will include a balance of rural and suburban investment.

Incremental operating expenses are based upon Accipiter's recent growth history. Operating expenses do not grow in proportion to subscriber counts because the new subscribers increase Accipiter's economies of scale.

USF revenues were limited according to Accipiter's understanding of the FCC's unfinalized regression formula applied to each year of the forecast. Accipiter assumes that working loops represent the only independent variable that will change during the forecast period (i.e. independent variables relying on census information remain static).

It is also worth noting that the currently proposed regression formulas reduce Accipiter's USF support below the \$250 per line per month limitation established by the FCC. However, if regression is not implemented in July 2012 or if the regression formulas are modified in a way to provide less severe cuts to Accipiter's revenues, the company will likely still require a temporary waiver of the \$250 per line per month limit. The ultimate needed duration of the waiver is dependent upon the lines the FCC will use to calculate the limit and the modification made to the regression caps. Accipiter has been informed verbally by USAC staff that the limit will be calculated based upon the most recently reported working loops, which in Accipiter's case for the August 2012 limitation would be **\*\*BEGIN CONFIDENTIAL** ■ **END**

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CONFIDENTIAL\*\* working loops reported in the company’s 2011 cost study by July 31, 2012 but that information has not been confirmed by the FCC.

Some parties have suggested that the number of lines used to calculate the \$250 per line limit for the period July 2012 through June 2013 will be the working loops reported in the 2010 cost study. In Accipiter’s case the year-end 2010 working loops of \*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\* would more drastically limit the company’s support in 2012 and subsequent years such that a more extended waiver would be required.<sup>13</sup>

1. Net income:

Negative net income means that Accipiter’s TIER metric falls below 1.0. When TIER falls below 1.0 Accipiter’s RUS loan covenants require the company to submit and RUS to approve a TIER recovery plan. If Accipiter cannot gain approval and maintain compliance with an acceptable TIER recovery plan, Accipiter will be in default of its loan covenants. If the new rules and unfinalized formulas as Accipiter understands them are applied immediately and no temporary waiver is granted, Accipiter would not be able to structure a reasonable TIER recovery plan and would default on its loans.

2. Cash flow:

Although Accipiter’s forecast shows that \*\*BEGIN CONFIDENTIAL [REDACTED]

[REDACTED]

[REDACTED]

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<sup>13</sup> This demonstrates how the new rules fail to account for the important differences between an ILEC like Accipiter which is *gaining* subscriber lines and many other ILECs which are *losing* lines.

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] END CONFIDENTIAL\*\*

The company cannot reduce operating expenses enough to achieve positive net income and cash flow. Many expenses are based on existing investments that cannot be undone. To the extent that cash expenses are above what can be recovered under the new rules, the FCC fails to consider that:

- The company is still gaining economies of scale that will significantly reduce its cost per subscriber;
- Because the company is in a growth cycle costs are structured to meet demands for growth. As that growth occurs unit costs are reduced because of the increased loop count. This is evident in Accipiter’s forecast and it is characteristic of any growing business like Accipiter;

**III. FAILURE TO MODIFY OR WAIVE THE RULES WOULD RESULT IN AN UNCONSTITUTIONAL TAKING**

Accipiter has shown that application of the rules to Accipiter, without modification or waiver, would prove confiscatory. The Federal Constitution generally protects utilities from being limited to a charge for their service that is so low as to be confiscatory in that it effectively precludes them from recovering their costs. *See, e.g., FPC v. Hope Natural Gas*, 320 U.S. 591 (1944); *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 307 (1989). A regulatory order becomes confiscatory where the result is “so unjust as to destroy the value of its property for all the purposes for which it was acquired.” *Covington & Lexington Turnpike Road Co. v. Sandford*, 164 U.S. 578, 597 (1896) Where the rates imposed by regulation threaten a utility’s “financial

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integrity,” those rates may be deemed “so unjust as to be confiscatory” and to represent a taking in violation of constitutional protections. *See Duquesne Light Co.* at 307, 312 (1989). “If the rate does not afford sufficient compensation, the State has taken the use of utility property without paying just compensation and so violated the *Fifth* and *Fourteenth Amendments*. *Id.* at 308.

As Accipiter has already demonstrated, the changes embodied in the *Report and Order* jeopardize Accipiter’s financial integrity to such an extent that they represent an unconstitutional taking.<sup>14</sup> The changes imposed by the *Report and Order* are so abrupt that they will provide Accipiter with no opportunity to recover its costs. If the *Report and Order* is enacted in full according to the Commission’s proposed timeframes without alteration or waiver, Accipiter’s projections show it will suffer such a severe loss in revenues that the company will become insolvent. Accipiter simply cannot afford to absorb such losses and, further, cannot adjust its rates sufficiently in order to account for these changes. In parts of its service territory, Accipiter faces competition – meaning that customers would simply switch away from Accipiter’s service in the event Accipiter attempted to raise rates sufficiently to make up for the losses. Even in those areas where Accipiter is the sole service provider, the rate increases necessary for Accipiter to survive would leave many customers unable or unwilling to continue to purchase service from Accipiter and thus without service. As these customers abandon the network, Accipiter would be faced with an even smaller subscriber base from which to recover its costs by charging ever higher unaffordable rates.

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<sup>14</sup> *See id.* at 7-10; *id.* at Exhibit 1.

**IV. FAILURE TO MODIFY OR WAIVE THE RULES WOULD BE ARBITRARY AND CAPRICIOUS**

Accipiter has catalogued a number of fundamental errors in the Commission's *Report and Order* which, absent correction or waiver, will have a serious effect on the company.<sup>15</sup> Application of the Commission's rules, which are based on flawed methodologies and are subject to erroneous inputs, to Accipiter would be arbitrary and capricious.

**A. Failure to Waive the \$250 Cap on Monthly Per-Line Support Would Be Arbitrary and Capricious.**

1. The Order Fails to Recognize that Growing Companies Will Require Decreasing Support.

An agency's determinations will be considered "arbitrary and capricious" if the agency "relied on factors which Congress had not intended it to consider, entirely failed to consider an important aspect of the problem, offered an explanation for its decision that runs counter to the evidence before the agency, or is so implausible that it could not be ascribed to a difference in view or the product of agency expertise." *Motor Vehicle Manufrs. Ass'n. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). Factors considered in evaluating an agency's conclusions include whether "the agency examine[d] the relevant data and articulate[d] a satisfactory explanation for its action including a rational connection between the facts found and the choice made." *Id.* "The agency's explanation cannot 'run[] counter to the evidence,' and it must 'enable [a court] to conclude that the [agency's action] was the product of reasoned decision making.'" *Kristin Brooks Hope Ctr. v. FCC*, 626 F.3d 586, 588 (D.C. Cir. 2010)

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<sup>15</sup> See *id.* at 10-22.

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The \$250 monthly per-line cap fails to take into account the economic realities confronted by an expanding carrier like Accipiter. Such a carrier requires significant new investments before customers can be added. However, a growing carrier will need less support per line over time as customers can be added in lower-cost increments. Thus, while the immediate imposition of the \$250 monthly per-line cap could be financially detrimental to Accipiter, the company will reduce costs below this cap as it continues to add customers. Delaying the implementation of the cap by just a few years would substantially reduce or eliminate the effect of the cap on Accipiter. In fact, Accipiter presently estimates that it will be out from under the cap as early as the second quarter of the year 2014.

2. Application of the Cap to 2010 Expenses and Loops is Arbitrary and Capricious.

The Commission's application of its newly-adopted rules to 2010 expenses and loops is arbitrary and capricious decision-making. Accipiter reasonably and rationally made decisions about 2010 investments and expenses based on the rules that were in place in 2010. In applying its rules to 2010 expenses and loops, the Commission "entirely failed to consider an important aspect of the problem," failed to provide a reasonable explanation connecting the "facts found and the choice made," *Motor Vehicle Manufrs. Ass'n*, 463 U.S. at 43.

Application of the rules to 2010 expenses and loops further runs afoul of the statutory requirement that there be "specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service." 47 U.S.C. § 254(b)(5). Application of newly-adopted rules to previously-incurred expenses is in no way consistent with the Congressional directive that support should be "predictable," and would punish Accipiter for reasonable investment decisions that cannot be reversed to account for the Commission's new rules.

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**B. Application of the Regression Caps to Accipiter Would be Arbitrary and Capricious.**

As Accipiter has already shown, it is unclear from the *Report and Order* how the regression caps the Commission has developed will actually be applied. It is thus not completely clear how severe the impact on Accipiter will be. Accipiter has already requested that the Commission correct and clarify how the caps are calculated so that Accipiter and other carriers will understand how the caps are to be applied in practice and be better able to estimate the impact of the *Report and Order*. In particular, Accipiter requested that the Commission clarify whether, when the caps are implemented on July 1, 2012, they will apply to Accipiter's 2010 cost study, and thus affect revenues received in July 2012 or instead will apply to 2012 costs which, in turn, will affect USF revenues received in 2014.<sup>16</sup>

In any event, the regression caps imposed by the *Report and Order* suffer from a number of legal and factual flaws. As discussed in greater detail below, in this case, a number of the Commission's conclusions in the *Report and Order* reflect arbitrary and capricious decision-making.

1. The Regression Caps Are Based on the Pursuit of a Flawed Objective.

The objective of the *Report and Order* appears to be the development of a method to cap the cost recovery of all high-cost ILECs, regardless of circumstance. The Commission's approach fails to achieve a more reasonable and appropriate objective of identifying which high-cost ILECs may legitimately be outliers due to particular considerations, including population

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<sup>16</sup> Accipiter Petition at 17-18.

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density, terrain, and operating environment, and which entities are outliers due to waste, fraud or other inefficiencies. The Commission's failure to distinguish between these circumstances is irrational and reflects a failure to consider facts in evidence before the agency concerning the specific challenges Accipiter, and other carriers, face in delivering service.

2. The Report and Order Lacks Clarity Regarding Implementation.

It is unclear from the *Report and Order* how the regression caps the Commission has developed will actually be applied. In particular, when the caps are implemented on July 1, 2012, it is not clear whether the caps will apply to Accipiter's 2010 cost study, and thus affect revenues received in July 2012 or apply to Accipiter's 2012 costs which, in turn, will affect USF revenues received in 2014. In creating its financial forecast of the potential impact of the *Report and Order*, Accipiter has used a worst-case assumption – namely that the Commission intends for the caps to apply to Accipiter's 2010 cost study, which will have a devastating effect on 2012 revenues. This lack of clarity serves to underscore the problems the *Report and Order* has created – Accipiter cannot even be certain of the impact of the *Report and Order*.

3. The Report and Order Relies on Flawed Data.

The census data which the Commission uses in its model in the *Report and Order* are subject to a substantial degree of error. In any model, where there are errors or inaccuracies in the inputs, those data flaws will also create errors or inaccuracies in the outputs of the model. The *Report and Order* does not address this significant problem.

Part of the input error is created by the Commission's use of the TeleAtlas tool to define study areas. This tool is notably flawed for Accipiter, as is evidenced by a map showing the errant study area relied on by the Commission compared with Accipiter's actual study area. The difference in these respective study areas is shown on Exhibit 1, attached hereto. While the

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Commission's model assumes an Accipiter study area encompassing 30.5 square miles, Accipiter's actual study area encompasses 1,010 square miles – an extraordinary error by any measure and one that is certain to produce a flawed result. Even when the correct study area boundary is used to collect the census data used for the FCC model inputs, the process is still produces substantial input errors. Census block boundaries and study area boundaries are not always coterminous. Applying the FCC's methodology, where a study area boundary contains the centroid of a particular census block, that census block data is counted for the carrier as if the entire block was served. For carriers like Accipiter which serve low density areas adjacent to high-density areas, this introduces significant errors in inputs. When Accipiter attempted to use the company's actual study area boundaries to query census blocks with centroids located within the boundaries, Accipiter's 1,010 square mile study area yielded results which included census blocks containing 103 square miles of area outside the company study area. Likewise the results omitted 94 square miles of area that is within the company's study area. The magnitude of these errors can be concealed within the net effect, which only overstates the company's square mileage by nine square miles. Thus, the model employed by the Commission appears to be incapable of predicting the correct study area data for Accipiter.

Further, Accipiter requested that the Commission staff provide a list of census blocks that were used to generate input data based on the TeleAtlas boundary used for Accipiter so that Accipiter could attempt to verify how the model was working and why its results were so inaccurate – but the staff refused to provide such a list. Ultimately, Accipiter sought to replicate the FCC's data through a time-intensive and costly trial and error process but Accipiter has no way of confirming that the result reached is the same as that relied upon by the Commission. Reliance on flawed data is plainly arbitrary and capricious. Moreover the Commission's failure

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to provide underlying data that would allow Accipiter to understand and replicate the Commission's conclusions also raises serious Administrative Procedure Act ("APA") and fundamental due process issues.

Under the APA, "[i]t would appear to be a fairly obvious proposition that studies upon which an agency relies in promulgating a rule must be made available during the rulemaking in order to afford interested persons meaningful notice and an opportunity for comment." *Am. Radio Relay League, Inc. v. FCC*, 524 F.3d 227 (D.C. Cir. 2008). Pursuant to the APA's notice and comment requirements, "[a]mong the information that must be revealed for public evaluation are the 'technical studies and data' upon which the agency relies [in promulgating rules]." *Chamber of Commerce v. SEC*, 443 F.3d 890, 899 (D.C. Cir. 2006) (citation omitted). This is so because "it is especially important for the agency to identify and make available technical studies and data that it has employed in reaching the decisions to propose particular rules" to allow interested parties to provide useful input or criticism. *Conn. Light & Power Co. v. Nuclear Regulatory Comm'n*, 218 U.S. App. D.C. 134, 673 F.2d 525, 530 (D.C. Cir. 1982). Disclosure of such information allows commenting parties to point out where information relied upon by the agency is erroneous or where the agency may be drawing improper conclusions from that information. *Nat'l Ass'n of Regulatory Util. Comm'rs v. FCC*, 237 U.S. App. D.C. 390, 737 F.2d 1095, 1121 (D.C. Cir. 1984). "It is not consonant with the purpose of a rule-making proceeding to promulgate rules on the basis of inadequate data, or on data that, [to a] critical degree, is known only to the agency." *Portland Cement Ass'n v. Ruckelshaus*, 486 F.2d 375, 393 (D.C. Cir. 1973).

Further, where a party requests and is denied access to information upon which an agency's decision is based, such a denial may constitute a due process violation. *See, e.g., Brock*

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*v. Roadway Express*, 481 U.S. 252, 265 (1987). In this case, without access to the information upon which the Commission's decisions were based, Accipiter has little or no ability to understand and, if necessary, challenge the Commission's decision-making process.

Withholding this information effectively denies procedural due process rights, because Accipiter cannot test and verify the Commission's conclusions which, in turn, could effectively preclude Accipiter from recovering its costs.

4. The Report and Order Relies on Flawed Independent Variables.

The independent variables that are ultimately contained in the Commission's regression formula do not appear to faithfully capture the factors that may influence a carrier's costs, or help to explain why a carrier has costs that are notably higher than the national average.

First, the Commission's model uses the number of loops as an independent variable. This approach fails to account for the trajectory of growth of an expanding carrier like Accipiter. Carriers must frequently incur costs before customers are added. As a result, growing carriers generally have significantly higher initial costs while they are expanding. By way of example, Accipiter's regulated loops increased by **\*\*BEGIN CONFIDENTIAL [REDACTED] END CONFIDENTIAL\*\*** from the 2009 cost study to the 2010 cost study, which reflects the second highest percentage gain observed among the companies included in the data the Commission provided. On average, the 720 carriers contained in the Commission's dataset experienced an eight percent *decrease* in the number of regulated loops. Because of these differences, data applicable to these carriers is unlikely to be reflective of Accipiter's cost structure.

Second, the Commission's use of housing units as a variable fails to account for housing units in a carrier's service area that are unserved. This may be relatively rare, but Accipiter confronts this scenario both because there are homes in very rural locations in its service territory

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that are still unserved by Accipiter's facilities and because Accipiter is unable to feasibly serve homes in two developments in its service territory because of an exclusive service arrangement between the developer and Cox Communications similar to the one discussed above. Errors in census block data as described above can also overstate or understate the housing unit factor.

Third, the Commission's use of the number of census blocks as a proxy for population density is arbitrary and capricious. The census blocks may mathematically fit the Commission's regression model, but using the number of census blocks as a measurement of scale is arbitrary and unreasonable. While the Census Bureau employs certain criteria for constituting the boundary of a census block, the actual definition of the boundary appears to be more of an art than a science, and the variation in census block consistency is likely most significant in rural areas. Further, it is not at all clear why it is appropriate and reasonable to compare costs among carriers merely because they have the same number of census blocks in their study area. A particular carrier's costs may significantly exceed the norm because the carrier's service area is among the most sparsely populated in the nation – as is the case with Accipiter. It is plainly arbitrary and unreasonable to cap that carrier's cost support for existing investment based on the number of census blocks in the carrier's service area especially since errors in census block data can also lead to an overstatement or understatement of the census block factor.

Fourth, the Commission's consideration of the percentage of water in the service area to help account for terrain variations is seriously flawed. The Commission failed to consider much more significant terrain features that will impact costs, such as soil type, geographical considerations including mountains or canyons, and costs of rights-of-way, among other things. These features are largely independent of the percentage of water in a service area, but have a significantly greater effect on the costs of service. The failure to account for these factors is

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arbitrary and capricious. Here too errors in census block data can lead to overstatement or understatement of the percent water factor.

Fifth, as noted, the Commission's model appears to have used the wrong data with respect to the land area served by Accipiter. The model attributes to Accipiter a service area of 30.5 square miles. In fact, Accipiter's service area is approximately 1,010 square miles. But, when Accipiter adds up the land area in the census blocks assigned to Accipiter's service area using the Commission's methodology, the area includes 103 square miles outside the company study area and excludes 94 square miles that are within the company study area. Errors of this magnitude in the data used by the FCC to build its model demonstrate that application of the model as it presently stands would be arbitrary and capricious.

Sixth, the Commission's inputs for housing units, land area and number of census blocks are further delineated according to the Census Bureau's categorization of each census block as "urbanized area," "urbanized cluster," or "non-urban." The Census Bureau has not yet published the categorizations for Accipiter's census blocks, which makes it even more challenging for Accipiter to forecast the regression results. However, examination of the coefficients the Commission's model uses with respect to the rural or urban categorization yields counterintuitive results. For example, if a census block is recategorized from a rural assignment to an urbanized cluster assignment, the model's capped output for cable and wire facilities will increase based on the housing unit factor, decrease based on the land area factor, and decrease based on the census block factor. If the census block is recategorized from an urbanized cluster to an urbanized area the model's capped output will decrease for housing units, decrease for land area, and increase for census blocks. This result appears to be nonsensical and thus is arbitrary and capricious.



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**EXHIBIT 1**  
**[REDACTED]**

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**EXHIBIT 2**  
**[REDACTED]**

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**EXHIBIT 3**  
**[REDACTED]**

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**EXHIBIT 4  
[REDACTED]**

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**EXHIBIT 5  
[REDACTED]**

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**EXHIBIT 6  
[REDACTED]**