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

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337

APPLICATION FOR REVIEW

Accipiter Communications Inc. ("Accipiter"), pursuant to Section 1.115 of the Commission's rules, 47 C.F.R. § 1.115, hereby requests review by the Commission of the Wireline Competition Bureau's ("Bureau's") Order issued on April 25, 2012 in the above-referenced dockets (the "Bureau Order").[1]

I. QUESTIONS PRESENTED AND FACTORS WARRANTING RECONSIDERATION BY THE COMMISSION.

As required by Section 1.115(b)(1) of the Commission's Rules, 47 C.F.R. § 1.115(b)(1), Accipiter presents the following questions for review of the Bureau Order by the Commission: (1) whether the methodology adopted by the Bureau complies with the statutory requirement that universal service support be "specific, predicable and sufficient"[2] and with Commission precedent and policy; and (2) whether the Bureau was incorrect in concluding that application of benchmarks to support payments does not constitute retroactive rulemaking. Commission review is appropriate pursuant to Section 115(b)(2)(i).

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[1] *Connect America Fund, High-Cost Universal Service Support*, Order, WC Docket Nos. 10-90, 05-337, DA 12-646 (April 25, 2012).

[2] 47 U.S.C. § 254(b)(5).

II. THE BUREAU ORDER DOES NOT COMPLY WITH STATUTORY REQUIREMENTS.

Section 254(b)(5) of the Communications Act of 1934 as amended, 47 U.S.C. § 254(b)(5), requires "specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service." The Bureau Order fails to comply with this requirement in at least three ways. First, the Bureau's methodology suffers from fundamental flaws which lead to irrational results. Second, the results of the Bureau's methodology are so unpredictable that application of this methodology effectively prohibits companies from making reasonable and rational investment decisions. Third, the Bureau Order fails to follow the Commission's mandate that carrier costs should be compared to those of similarly situated carriers.

A. The Bureau's Methodology Suffers From Fundamental Flaws Which Must Be Corrected.

1. The Use of Inaccurate Input Data to Construct the Model Produces an Inaccurate Model.

As the Bureau acknowledges, a number of commenters questioned the accuracy of the study area boundaries based on TeleAtlas wire center data.[3] In particular, the Rural Associations pointed to data suggesting that 144 of the 357 study areas for which NECA has actual boundaries are not accurate within five percent, 80 are not accurate within 20 percent, a significant number differ by more than 50 percent, and a few are wholly inaccurate.[4] As Accipiter has already noted to the Commission, the census data which the Commission uses as inputs to its model in the *Report and Order* are subject to a substantial degree of error.[5] In any model, errors or

[3] Bureau Order at ¶ 24.

[4] *Id.* citing Rural Association Comments, Appendix D at 3-4.

[5] Accipiter Petition for Reconsideration and Clarification, 12-14 , WC Docket No. 10-90, filed December 29, 2011.

inaccuracies in the inputs will flow through and create errors or inaccuracies in the outputs of the model.

The Bureau's response to these significant input errors is to establish a waiver process for carriers affected by the benchmarks to correct errors in their study area boundaries, and to issue a Public Notice to begin collecting study area data.[6] The latter step represents a viable approach to developing a more accurate model, which the Bureau clearly recognizes is necessary. However, the interim solution of allowing carriers to individually update data and then have this data subject to flawed formulas is no solution at all – this approach does nothing but impose arbitrary penalties on rate-of-return carriers. The coefficients which the Bureau Order adopts to calculate capped costs are locked in place for 2012 and 2013 despite the fact that they are plainly flawed because they are based on flawed inputs.[7] A formula with flawed coefficients cannot produce correct results merely through the correction of independent variables. In fact, a correction in the inputs to a flawed formula is just as likely to produce results with even *more* significant errors.

The Bureau Order does not acknowledge this clear error in its approach. Rather, the Bureau attempts to justify the July 1 implementation of formulas based on flawed inputs by stating that: "In many cases, more accurate boundaries would not change whether or not a particular company is capped or not by the benchmark methodology. And the streamlined, expedited waiver process we adopt to correct boundaries in the near-term will address those specific instances where an inaccurate boundary could result in a company losing more support than it would otherwise."[8] This is a surprising conclusion given that no one knows how the model will change in 2014 when corrected inputs are used to rebuild the model. The

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[6] Bureau Order at ¶ 27.

[7] *Id.* at ¶ 41.

[8] *Id.* at ¶ 28.

Commission should carefully consider the Bureau's contention and the very real possibility that carriers will find out in 2014 that they were incorrectly penalized in 2012 and 2013 based on the rigid application of flawed formulas.

2. The Use of Proxies Introduces Additional Error into the Modeling.

The Bureau uses proxies to serve as a representation of the actual cost-driving variables which determine which companies are "similarly situated." However, a proxy is only useful where it closely correlates with the actual variable for which the proxy serves as a substitute. The Bureau offers no analysis of the correlation fit between the variables it intends to represent and the proxies used for those variables. Without such analysis, the model is vulnerable to poor proxy selection, which introduces additional and unreasonable error into the model results.

This problem is illustrated by the Bureau's selection of the natural logarithm of the number of road miles as a proxy for total loop length. The Bureau observes that "the number of road miles in a study area should correlate with the cabling required to serve that area."[9] While the logical conclusion would be that longer cable routes require higher capex costs, the model results actually show the opposite effect – that a carrier with more road miles (and by proxy longer cable routes) has a capex cap which is lower than its "similarly situated" peers. Even though this non-intuitive result is deemed not statistically significant for capex,[10] the variable and its coefficient remain in the model's formula and are allowed to lower a carrier's capex cap.[11] The Order fails to acknowledge this non-intuitive result and neglects to include analysis for the correlation between the actual cost-driving variable and its proxy. This serves as

[9] *Id.* at ¶ 86.

[10] *Id.* at ¶ 88.

[11] This is found as the negative coefficient of -0.208 assigned to the "LnRoadMiles" variable in Table 3. *See id.* at page 43.

strong evidence that the current model is poorly conceived and fatally flawed and that its application is not likely to lead to reasonable outcomes.

In general, using proxies in a model built upon inaccurate input data exacerbates modeling errors. Even if a proxy variable can be determined as strongly correlated with the actual cost-driving variable and is deemed to be statistically significant in the model, such qualifications are useless when they are built upon a model of flawed inputs.

Finally, it is ironic that the Bureau choses to use proxies based on third party data instead of securing actual cost-driving input data which may be obtained easily through requests to rate-of-return carriers. As an example, the lengths of cable routes are maintained by all carriers to comply with the FCC's accounting requirements. Adding this input as a data line on the annual cost study would be a relatively costless requirement for carriers and would provide the FCC with an accurate measurement of a significant cost-driving metric. Instead the Bureau chose to use a third-party database to mine data for a poorly defined and inadequately justified proxy.

3. Timing Discrepancies in the Updating of Data Introduce Bias in the Model.

The various inputs into the Bureau's model are updated according to different schedules. For example, costs, loops and undepreciated plant are updated annually. However, census data is updated every ten years, and is released on varying dates. It is not clear when, how or if road crossing and road miles data will be updated. Updating the data incrementally based on new information will inevitably create bias in the results until all of the data on which the model relies is updated.

All three of these factors, flawed input data, the use of proxies, and data that is updated according to different schedules, combine and compound to create cascading errors in the output of the model. The result is a methodology that is fundamentally flawed, prone to additional and different errors over time and not likely to produce reasonably rational or predictable results.

B. The Bureau Order Fails to Achieve the "Predictability" Required for Universal Service Support.

1. Carriers Cannot Reasonably Predict CAPEX and OPEX Limits.

The Bureau Order states that the argument that implementing benchmarks will undermine the predictability or sufficiency of support "effectively seeks reconsideration of the Commission's policy judgment to adopt a rule imposing limits on capex and opex in the first instance, which is beyond the scope of this order to implement a methodology as directed by the Commission."[12] Accipiter disagrees. The fundamental issue is not the adoption of limits in the first instance, it is the question of whether the methodology for adopting specific limits complies with the statutory requirement that support be predictable and sufficient. Here, while carriers can predict support levels for 2013, it is impossible to predict those levels for 2014 and beyond. Investment decisions must be made over a much longer time horizon than the FCC's approach contemplates.[13] The statutory requirement that support be "predictable" reflects this reality. In this case, the methodology implemented by the Bureau does not allow a carrier such as Accipiter to predict what its capex and opex limits will be in the future. A carrier thus has no way to make even vaguely accurate predictions regarding the level of support it will receive, and thus has no reasonable ability to make prudent investment decisions. The Bureau's passing observation that concerns that support amounts will fluctuate and lack predictability are "speculative and unpersuasive" is vague, arbitrary, capricious and reflects no serious appreciation of the actual problem.

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[12] Bureau Order at ¶ 41.

[13] Freezing investment decision making works directly against the FCC's goal of promoting the deployment of broadband services in rural areas.

2. The Bureau's Methodology is Heavily Influenced by Subjective and Changing Factors.

The Bureau claims that, in any event, predictability concerns are unpersuasive because, under both the new and previous systems, "a certain amount of unpredictability exists because a carrier's support depends in part on a national average that changes from year to year, and companies 'can only estimate whether their expenditures will be reimbursed through HCLS.'"[14] This sidesteps the fact that a substantial amount of the unpredictability in the new approach is due to the Commission's subjective and changing selection of inputs to the methodology for calculating benchmarks, rather than the objective reality of the current system reflected in the national average cost per loop.[15] For example, the Bureau has made a number of subjective determinations in selecting which variables are included in the model, the level of statistical significance that qualifies a particular variable for inclusion, and which data sources to use when constructing inputs for the model. All of these decisions, and others, may be subject to revision by the Bureau from year to year. The casual assertion that there is a "certain amount of unpredictability" in the old system seeks to conflate a modest degree of uncertainty with a wholly unpredictable methodology that is subject to change each year.

3. There Are No Constraints on the Ability to Redesign the Model.

In part because the Commission has not put in place constraints on its ability to redesign models each year, there is no reasonable way for a carrier to understand enough about the model

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[14] Bureau Order at ¶ 41, citing *Connect America Fund; A National Broadband Plan for our Future; Establishing Just and Reasonable Rates for Local Exchange Carriers; High-Cost Universal Service Support; Developing a Unified Intercarrier Compensation Regime; Federal-State Joint Board on Universal Service; Lifeline and Link-Up; Universal Service Reform – Mobility Fund*, Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, ¶¶ 222, 539-544 (2011) ("USF/ICC Transformation Order").

[15] Carriers can estimate the changes in national average loop cost from year to year. They cannot know what those working on the model in future years will subjectively deem significant years hence.

to make informed investment decisions or make reasonable financial forecasts. Further, the Commission requires the submission of buildout plans by 2013, and will review carriers' progress on that plan each year thereafter.[16] The Commission has not explained how carriers can reasonably forecast for 2014 and beyond without knowing what the regression models will be.

As an example, if a carrier makes an investment today, the carrier knows there will be an incremental increase in capex, opex, loops and percent undepreciated plant. Based on these factors, the carrier can calculate the cap impact for 2012 and 2013, but only because the formulas are locked in for those years. For 2014, the coefficients could change dramatically, but carriers do not know the magnitude or even direction of those changes, and do not even know that the same variables will stay in the formula. The carrier would thus be subject to uncertainty and unpredictability every year after 2014. While the Commission intended that the "new rule will discourage companies from over-spending relative to their peers,"[17] in reality carriers cannot even be confident that efficient investments will ensure falling under the caps, because "efficient" investments as defined by the model are only judged with respect to the independent variables the Bureau selects – carriers do not know how those variables will change from one year to the next.

C. The Bureau Order Fails to Comply with the Commission's Requirement that Costs Should be Compared to Similarly Situated Carriers.

The Commission requires that "companies' costs be compared to those of similarly situated companies."[18] The Bureau Order fails to comply with this requirement. The Bureau uses selected independent variables to determine "similarly situated" companies.[19] Capex and

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[16] Bureau Order at ¶ 36, citing USF/ICC Transformation Order at ¶ 587.

[17] *Id.* at ¶ 7.

[18] USF/ICC Transformation Order at ¶ 217.

[19] Bureau Order at ¶ 10, n. 24.

opex limits are derived based on the independent variables applicable to each company. However, if a particular cost-driving characteristic is not addressed by the independent variables the Bureau has elected to consider, a carrier with costs driven by that characteristic will not be compared to companies that are in fact "similarly situated." For example, the Bureau hypothesized that more stream crossings might increase a carrier's capex costs. However, the Bureau concluded that this variable was not statistically significant for capex, and thus stream crossings are excluded from the Bureau's 2012-2013 formulas.[20] As a result, those carriers which truly have higher costs due to the need to cross streams cannot have their cap adjusted for that factor, and thus are not correctly compared to "similarly situated" carriers.

D. The Commission Should Take Several Steps to Correct the Bureau Order.

To correct the flaws in the Bureau Order, the Commission should take a number of steps. First, the Commission should delay implementation of the model until the Bureau collects accurate input data upon which a more accurate, rational model can be constructed. Second, after new formulas are finalized, the Commission should delay implementation of support limits for one year to provide carriers with sufficient time to understand the model, understand its impacts, and file for and receive waivers, if needed, in sufficient time to avoid calamitous results from immediate implementation. Finally, the Commission should "lock in" independent variables and coefficients for a specific period of time, not less than ten years, to satisfy the statutory requirement that universal service support be predictable.

III. THE BUREAU ORDER ERRONEOUSLY CONCLUDES THAT APPLICATION OF THE BENCHMARKS DOES NOT CONSTITUTE RETROACTIVE RULEMAKING.

The Bureau concludes that the application of benchmarks to limit HCLS payments does not constitute retroactive rulemaking. According to the Bureau, a rule does not operate

[20] Bureau Order at ¶ 114.

retroactively merely because it applies to conduct preceding the enactment of the rule; rather, a rule operates retroactively if it "takes away or impairs vested rights acquired under existing law, or creates a new obligation, imposes a new duty, or attaches a new disability in respect to transactions or considerations already past."[21] The Bureau goes on to conclude that, "[a]lthough application of the benchmarks may affect the amount of support a carrier receives for expenditures made in 2010 (or before), it does not change the legal landscape in which those expenditures were made."[22]

In fact, for some carriers, the Bureau Order has precisely the effect of attaching "a new disability to transactions or considerations already past." Accipiter has been able to deploy service through a combination of USF support and low interest loans for rural telecommunications development provided by the Department of Agriculture Rural Utilities Service ("RUS"). By altering the levels of USF support that Accipiter can expect to receive for expenditures already made, the Bureau Order has the potential to affect the loan transactions between Accipiter and the RUS. Both Accipiter and the RUS relied upon the statutorily required sufficiency and predictability of USF revenues when entering loan contracts, and Accipiter's investments reflect an obligation by the company to extend service to previously unserved areas. The Bureau Order effectively alters the underlying facts upon which RUS loan contracts were based and, therefore, constitutes retroactive rulemaking.

IV. CONCLUSION

For the foregoing reasons, Accipiter respectfully requests that the Commission reconsider the Bureau Order.

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[21] Bureau Order at ¶ 37 (citations omitted).

[22] *Id.* at ¶ 38.

Respectfully Submitted

/s/ Patrick Sherrill

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