

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

REPLY COMMENTS OF
ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.

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Executive Summary

The record before the Bureau amply documents the problems inherent in using a national model to attempt to estimate the forward-looking costs of insular price cap local exchange carriers (“LECs”) and to determine the amount of CAF Phase II support for which they will be eligible. Insular price cap LECs face unique challenges and incur corresponding costs that are completely unlike the price cap LECs serving the contiguous Lower 48 States. Neither the ABC Coalition model nor other proposals offered in the record to date factor in these challenges and costs. If the Bureau attempts to establish support for insular price cap LECs based on a nationwide model, consumers in those service areas will be at a disadvantage. If the Bureau does not address the challenges and costs faced by insular price cap LECs in a meaningful way – either by developing a model that is targeted to their unique circumstances or by continuing to provide them with a minimum level of support based on their CAF Phase I support amounts while relaxing the CAF Phase II build out requirements – insular price cap LECs will be unable to rise to the broadband challenge adopted by the Commission in its *USF/ICC Transformation Order*. ACS urges the Bureau to choose one of these options for determining the amount of CAF Phase II funding that it will make available to insular price cap LECs. ACS highlights herein some of the key issues that remain unaddressed, but that are critical for rational business decision-making for carriers faced with deploying infrastructure and offering service based on CAF Phase II support. ACS also rebuts a number of competitors’ claims and proposals that demonstrate a lack of understanding of the demands of serving high-cost insular areas such as Alaska.

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REPLY COMMENTS OF ALASKA COMMUNICATIONS SYSTEMS GROUP, INC.

Alaska Communications Systems Group, Inc., on behalf of its operating subsidiaries (“ACS”),¹ hereby replies to the comments submitted July 9, 2012 in response to the request of the Wireline Competition Bureau (the “Bureau”) in the above-captioned dockets for comments on model design and data inputs for Phase II of the Connect America Fund (“CAF”).²

I. OVERVIEW

Most commenters who addressed these issues agree that a reasonable model would be based on a greenfield approach, estimate total cost to build throughout the study area, measure

¹ In this proceeding, Alaska Communications Systems Group, Inc. represents four local exchange carrier subsidiaries, ACS of Alaska, Inc., ACS of Anchorage, Inc., ACS of Fairbanks, Inc., and ACS of the Northland, Inc. (collectively, the “ACS ILECs”), as well as ACS Wireless, Inc., ACS Long Distance, Inc., ACS Internet, Inc., and ACS Cable, Inc. Together, these companies provide wireline and wireless telecommunications, information, broadband, and other network services to residential, small business and enterprise customers in the State of Alaska and beyond, on a retail and wholesale basis, using ACS’s statewide and interstate facilities.

² *Wireline Competition Bureau Seeks Comment on Model Design and Data Inputs for Phase II of the Connect America Fund*, Public Notice, WC Dockets 10-90 and 05-337, DA 12-911 (Wireline Competition Bur. rel. June 8, 2012) (the “*Model Design/Data Inputs Public Notice*”).

terminal value of zero at the end of the support period, and include up-to-date cost inputs.³

However, carriers serving rural and insular areas express skepticism that any national model can successfully estimate the costs associated with deploying broadband in insular areas. Rural service providers rightly observe that the Bureau is obligated to adopt a methodology that will produce support reasonably calculated to ensure that eligible telecommunications carriers (“ETCs”) can recover their forward-looking costs of deploying broadband as required by the Commission at prices that are affordable to consumers. Insular carriers point out that service providers in the contiguous Lower 48 States do not labor under the same constraints as insular carriers, including the short construction seasons, extremes of weather and geography, lack of road access or local power source, unavailability of terrestrial telecommunications transport, and thousand-mile plus gaps between local networks and Internet access points. Nor do carriers in the Lower 48 serve areas with the levels of poverty faced by those in insular areas. Were the Bureau to design a model that cannot incorporate these types of factors, it would fail to accomplish the goals of the statute and the Commission. Moreover, any model the Bureau adopts for Phase II must use accurate local inputs to ensure that the resulting support is adequate for the construction, operation, and maintenance of the required facilities. Similarly, the model must incorporate realistic “take rates” for broadband services.

ACS continues to urge the Commission to tailor its approach for providing CAF Phase II support to insular price cap local exchange carriers (“LECs”), either developing a separate model

³ See generally Comments of Alaska Communications Systems Group, Inc., *Connect America Fund*, WC Docket No. 10-90, *et al.* (filed July 9, 2012) (“ACS Comments”); Comments of the United States Telecom Association, AT&T, CenturyLink, FairPoint Communications, Frontier Communications, Verizon, and Windstream Communications, *Connect America Fund*, WC Docket No. 10-90, *et al.* (filed July 9, 2012) (“ABC Coalition Comments”); and Comments of the National Association of State Utility Consumer Advocates, *Connect America Fund*, WC Docket No. 10-90, *et al.* (filed July 9, 2012) (“NASUCA Comments”).

specifically targeted for insular price cap LECs or continuing to provide insular price cap LECs with their current frozen and incremental CAF Phase I support in lieu of support based on a model.⁴ ACS already has put on record Alaska-specific inputs covering transport unique to Alaska,⁵ but ACS continues to develop additional inputs that are Alaska-specific. This Alaska data would be an instrumental component in developing an insular-specific price cap LEC model. ACS needs a reasonable amount of time to complete this data-gathering process as it will involve analysis of outside plant in more than 80 wire centers, but the work has already begun.

Regardless of the direction the Bureau takes in disbursing CAF Phase II support to insular price cap LECs – whether by a one-size-fits-all nationwide model, a separate insular specific model, or continuation of frozen and incremental CAF Phase I support – the comments demonstrate that there are other important concerns that must be factored into the Bureau’s decisions. For example, the Bureau does not appear to address what it expects to happen to supported services and infrastructure deployed using CAF II support after that support terminates, at the end of five years. Understanding whether further support will be made available to the provider-of-last-resort (“POLR”), or its facilities will be bought out by the next

⁴ See ACS Comments at i and 3-5.

⁵ See ACS Data Submission, *Wireline Competition Bureau Seeks Comment on Potential Data for Connect America Fund Phase One Incremental Support*, FCC Public Notice in WC Docket Nos. 10-90 and 05-337, DA 12-137 (rel. Feb. 6, 2012) (filed March 30, 2012); ACS Data Submission, *Wireline Competition Bureau Seeks Comment on Potential Data for Connect America Fund Phase One Incremental Support*, FCC Public Notice in WC Docket Nos. 10-90 and 05-337, DA 12-137 (rel. Feb. 6, 2012) (filed March 9, 2012); ACS Data Submission, *Wireline Competition Bureau Seeks Comment on Potential Data for Connect America Fund Phase One Incremental Support*, FCC Public Notice in WC Docket Nos. 10-90 and 05-337, DA 12-137 (rel. Feb. 6, 2012) (filed February 29, 2012); ACS Data Submission, *Request for Connect America Fund Cost Models*, FCC Public Notice in WC Docket Nos. 10-90 and 05-337, DA 11-2026 (rel. Dec. 15, 2011) (filed February 13, 2012).

supported provider, are critical to the decision-making process of a POLR such as ACS, which generally does not recover its infrastructure investments in as little as five years.

The Bureau's efforts to develop a methodology for disbursing CAF Phase II support is a broader undertaking than simply developing a model upon which to base support amounts. ETCs will need to know more about the parameters of accepting and declining such support. ACS addresses below a number of points made by other commenters, and corrects a number of misstatements made by some commenters.

II. DISCUSSION

A. **Insular Price Cap Carriers Are Similarly Situated, But Also Have Many Characteristics of Rate-of-Return Carriers, Which Further Demonstrates the Need For Unique Treatment In Determining CAF Phase II Support.**

1. Insular Price Cap Carriers Are Different From Other Carriers.

The Commission has singled out the insular price cap LECs for special consideration for any model that might be applied to them, recognizing their unique circumstances, specifically the costs they face in serving Alaska, Hawaii, Puerto Rico, the U.S. Virgin Islands, and Northern Mariana Islands.⁶ The information submitted by the price cap carriers that serve these insular areas demonstrates their unique circumstances, and the comments submitted by other insular price cap LECs in response to the Bureau's *Model Design/Data Inputs Public Notice* emphasizes the unique difficulties faced by insular price cap LECs that distinguish their cost of providing

⁶ The Commission directed the Bureau to "consider the unique circumstances of [Alaska, Hawaii, Puerto Rico, the U.S. Virginia Islands and Northern Mariana Islands] when adopting a cost model" and to "consider whether the model ultimately adopted adequately accounts for the costs faced by carriers serving these areas." *Connect America Fund*, WC Docket No. 10-90, *et al.*, Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, 17737-38, ¶ 193 (2011) (*USF/ICC Transformation Order*).

service from that of the price cap LECs serving the contiguous 48 States.⁷ These unique difficulties necessitate a unique solution – whether by developing a separate model to address the costs of insular price cap LECs,⁸ or ensuring a nationwide model addresses the special characteristics of serving these uniquely high cost areas,⁹ or continuing to provide insular price cap LECs with frozen and incremental CAF support in lieu of support based on a model.¹⁰

Though ACS’s Alaska service territory has even less in common with the service territories of the price cap LECs in the Lower 48, ACS shares some characteristics with other insular price cap LECs. ACS faces some of the same service challenges and unusual costs in

⁷ Both Virgin Islands Telephone (“VITELCO”) and Puerto Rico Telephone (“PRTC”) stress the significantly higher initiation, operation, and maintenance costs in serving their customers, specifically costs that are not factors, or at least regular factors, for carriers serving the contiguous United States. ACS is not unlike VITELCO and PRTC, which must incur higher costs related to shipping needs, topography, climate, power, and damage from severe storms. *See* Comments of Virgin Islands Telephone Corporation, *Connect America Fund*, WC Docket No. 10-90, *et al.*, at 5-6 (filed July 9, 2012) (“VITELCO Comments”) and Comments of Puerto Rico Telephone Company, Inc., *Connect America Fund*, WC Docket No. 10-90, *et al.*, at 7-8 (filed July 9, 2012) (“PRTC Comments”).

Perhaps one of the most significant costs and uniformly similar cost faced by ACS, VITELCO, and PRTC that is incurred by insular price cap LECs, but not price cap LECs in the contiguous Lower 48 States, is the cost of transport to Internet peering locations that are hundreds and thousands of miles away. *See* PRTC Comments at 7 (“The lack of an Internet peering location in Puerto Rico requires that middle mile transport be provided via undersea cable from Puerto Rico to peering points located in the continental U.S. via undersea cable. The need for transport via undersea cable systems introduces costs that will not be present in a national model that assumes backhaul via fiber to a point on a regional ring within the same LATA.”) *See also* VITELCO Comments at 4 (“A review of certain underlying assumptions of the CQBAT model identified on the record indicates that these costs are significantly understated for Internet data traffic to and from the USVI (and most likely for other non-CONUS areas as well). The CQBAT model assumes the Internet peering location always is located at a regional tandem within the Local Exchange Carrier’s (‘LEC’) LATA. In the case of Vitelco, however, the Company must transport Internet data traffic to Internet peering locations in the state of Florida, a distance of over 1,100 miles.”)

⁸ *See* ACS Comments at 6-7. *See also* PRTC Comments at 1.

⁹ *See* VITELCO Comments at 7-9. *See also* Comments of the Telecommunications Regulatory Board of Puerto Rico, *Connect America Fund*, WC Docket No. 10-90, *et al.*, at 8 (filed July 9, 2012).

¹⁰ *See* PRTC Comments at 1; VITELCO Comments at 7; ACS Comments at 3-5.

providing voice and broadband service to customers, though ACS must deal with far greater transport distances and extremes of weather and terrain than even the other insular carriers face.

2. Insular Price Cap Carriers Have Key Characteristics In Common With Rate-of-Return Carriers.

What may not have been immediately clear is the similarity of ACS and other insular price cap LECs to Rate-of-Return (“RoR”) LECs. The concerns of RoR LECs are not unlike the concerns of insular price cap LECs. The Bureau should consider many of the arguments made by RoR carriers for not applying a nationwide price cap model to RoR carriers as relevant in determining how to set CAF Phase II support for insular price cap LECs. Certainly the cost drivers for RoR carriers – population density, distance, terrain, and region – are as noted above cost drivers for insular price cap LECs.¹¹ More specifically, the service difficulties and significant service costs faced by insular price cap LECs are not unlike the characteristics of rural RoR carriers, which are “located in discrete and effectively confined regions of the country,” such that “nationally based assumptions and parameters are too general to produce valid estimates.”¹²

ACS agrees with the RoR Association Comments that there are errors in the large public data sources relied upon in developing a nationwide one-size-fits-all model and that these errors can result in a number of inaccuracies, which RoR carriers argue cannot be “statistically buffered or absorbed” in the same manner as price cap LECs such as AT&T, CenturyLink, or Frontier.¹³ The same is true for insular price cap LECs. ACS raised the same issue in its comments, stating

¹¹ See Comments of the National Telecommunications Cooperative Association, Organization for the Promotion and Advancement of Small Telephone Companies and the Western Telecommunications Alliance, *Connect America Fund*, WC Docket No. 10-90, *et al.*, at 4 (filed July 9, 2012) (“RoR Association Comments”).

¹² See RoR Association Comments at 4.

¹³ See RoR Association Comments at 4.

that “an accurate picture of relative costs between insular and non-insular carriers cannot result from the use of the one-size-fits-all model since the estimation error systematically present across mainland carriers is in no way similar to the error in the estimates for insular carriers.”¹⁴ The variations that insular price cap LECs encounter in serving areas that are particularly high-cost and difficult to serve based on “factors such as lack of road access, lack of municipal power, lack of terrestrial transport, extreme climate conditions, thousand-mile separations between points of network presence, and non-contiguous Internet access points”¹⁵ are similar to the “reasons why broad-gauge modeling assumptions that may produce a reasonable outcome for price cap carriers overall [and ACS contends this is true only for price cap carriers in the Lower 48 States] cannot be simply applied to discretely located rural RoR carriers.”¹⁶

ACS also shares the concerns of the RoR carriers about applying network design assumptions that are geared toward price cap LECs in the contiguous Lower 48 States to insular price cap LECs. The RoR carriers emphasize that they “have deployed a wide variety of network designs in order to effectively and efficiently serve their customers. No single set of modeling assumptions can properly capture this diversity.”¹⁷ The same is true for insular price

¹⁴ ACS Comments at 6-7.

¹⁵ ACS Comments at 7.

¹⁶ RoR Association Comments at 3-4. Similarly, ACS agrees that the concerns raised in the Nebraska Rural Comments also apply to insular price cap LECs. *See also* Comments of the Nebraska Rural Independent Companies, *Connect America Fund*, WC Docket No. 10-90, *et al.*, at 7 (filed July 9, 2012) (“Nebraska Rural Comments”) (“While the model on which the Commission is seeking comment to require broadband build-out in some price cap carriers’ areas may reasonably estimate the overall cost to serve of price cap carriers [and ACS submits this is only applicable for price cap carriers in the contiguous Lower 48 States], this would likely be in part because any model errors are more likely to cancel out when averaging costs over the larger price cap carriers, and averaging will not cancel out these errors. Therefore, RoR carriers, because of their generally smaller size, have more at risk from the inaccuracies that are unavoidable with any engineering cost model.”)

¹⁷ ROR Associations Comments at 5.

cap LECs. The choices of possible technologies on which the Bureau contemplates basing its one-size-fits-all model – fiber-to-the-premises (“FTTP”), fiber-to-the-node (“FTTN”), and digital subscriber line (“DSL”) – are wholly inadequate for purposes of modeling costs for insular price cap LECs. As ACS stressed in its comments, “[t]he three proposed technology options fail to capture several network solutions employed in the State of Alaska.”¹⁸ Similar to the conditions faced by other insular price cap LECs, as well as many rural RoR carriers, “[t]he weather, soil, terrain, and vast expanses of land and water in Alaska dictate that carriers serving customers integrate a variety of technologies, many of which are not contemplated by the Bureau.”¹⁹ Any model, whether it be a separate insular price cap model or a nationwide price cap model, must include and adequately account for the unique requirements to serve and connect Alaskans – including satellite, microwave, and undersea cables.

Failure to include in any model the critical technology components of what is required to serve insular price cap LECs will, as the Nebraska Rural Comments so aptly state, “produce flawed results and have potentially devastating policy implications for universal service”²⁰ and “produce areas that will continue to be unserved and will render this entire exercise as futile for areas for which there is no bidder [if the price cap LEC “refuses a state-level commitment to deploy broadband as required by the model”].”²¹ ACS urges the Bureau to refrain from “using a single approach,” which “will produce both inaccurate and unrealistic results.”²² ACS agrees that “[t]he best indicator of broadband costs in rural RoR [and ACS submits, in insular price cap

¹⁸ ACS Comments at 8.

¹⁹ ACS Comments at 8.

²⁰ Nebraska Rural Comments at 7.

²¹ Nebraska Rural Comments at 8-9.

²² RoR Association Comments at 5.

LEC] areas is the *actual cost* of the deployed networks.”²³ Any model applied to insular price cap LECs must be based on the actual costs of deploying networks in those areas; this may include fiber and DSL, but it also must include satellite, microwave, and undersea cables.

3. ACS Stands Alone In Facing Challenges Unique to Serving Alaska.

One way in which ACS is different from most other price cap LECs as well as the RoR LECs is that, while it is a small company and serves five rural study areas characterized by very high costs, ACS would be hard-pressed to accept a statewide commitment under the CAF Phase II requirements. ACS’s six study areas vary greatly in a number of respects, including geographic size, density, population, road miles, miles of outside plant, network architecture, type of facilities deployed (especially transport facilities) and distance to network points of presence.²⁴ For these reasons, ACS questions the wisdom of a statewide CAF Phase II requirement in Alaska. It is not clear what the Bureau expects will happen to service in the hardest-to-serve areas if a price cap LEC declines to exercise the Statewide Right of First Refusal and, as a result, no longer is entitled to receive even the current levels of support. Certainly there are larger implications than possibly that broadband won’t be deployed in areas served by a price cap LEC that declines CAF Phase II support. A price cap LEC that declines

²³ See RoR Association Comments at 5 (emphasis in original).

²⁴ For example, the Sitka and Glacier State study areas are both rural, but they have vastly different network characteristics based on differences in the disbursed nature of the population being served and the means of accessing the population served. The Sitka study area has more than 50 exchanges that are located primarily in the Alaska “Bush.” These exchanges are geographically disbursed and are located off the road system. In fact, travel to service these exchanges must be made by airplane and flying to these locations is dependent on suitable weather. Accordingly, the remote locations in the Sitka study areas – for example, Prince of Wales Island; St. Paul; St. George; Kaltag and Koyukuk, which are nearest of these remote locations to Fairbanks; and Atka, which is furthest out on the Aleutian Chain – must be served predominantly by satellite or microwave transport. Yet the Glacier State study area (with the exception of the island of Kodiak), which also covers rural areas, is located on the road system and its exchanges are served by fiber transport, rather than satellite and microwave.

CAF Phase II support will also lose the universal service support that it needs to maintain and operate the networks over which voice services are provided. This may put customers in these areas at risk of losing affordable voice services.

4. Continuing to Provide Frozen and Incremental Phase I Support Remains a Viable Alternative for Insular Price Cap LECs in Phase II.

If the Bureau determines that developing a model tailored to the difficulties and costs faced by insular price cap LECs is administratively infeasible, the Bureau is authorized to continue providing insular price cap LECs with the frozen and incremental Phase I support that they receive today.²⁵ Furthermore, ACS agrees with the VITELCO Comments that the Bureau should continue providing insular price cap LECs with frozen Phase I support “if the Bureau concludes that the model ultimately adopted will not provide sufficient support to those areas.”²⁶ VITELCO has indicated that continuing frozen Phase I support payments for insular price cap LECs amounts to approximately \$83 million, which is less than five percent of the total \$1.8 billion CAF Phase II budget.²⁷ As ACS pointed out in its comments, continuing to support insular price cap LECs with frozen and incremental Phase I support, but without the statewide CAF Phase II build out requirements, is a reasonable and cost effective means of providing insular price cap LECs with CAF support in Phase II.²⁸

B. The CQBAT Model, And Any Similar Nationwide Model, May Appropriately Set CAF Phase II Support For Price Cap LECs in the Lower 48 States, But Without Modification Application of Such a Model Will Harm Insular Price Cap Carriers.

²⁵ See *USF/ICC Transformation Order*, ¶ 193.

²⁶ VITELCO Comments at 7.

²⁷ See VITELCO Comments at 8.

²⁸ See ACS Comments at 3-5.

As similar as ACS and other insular price cap LECs are to each other, and as many characteristics they share with RoR carriers, they are distinct from the price cap LECs serving the contiguous Lower 48 States. It is this distinction that makes the CQBAT model supported by the ABC Coalition insufficient for purposes of establishing the amount of CAF Phase II support to be provided to insular price cap LECs.

The ABC Coalition Comments provide a lengthy argument for selecting their proprietary model upon which to base CAF Phase II support for price cap LECs.²⁹ ACS cannot say whether the ABC Coalition proposals are well suited to price cap LECs serving the contiguous Lower 48 States – their model is too opaque to be analyzed by anyone outside the coalition, as ACS has observed in these dockets and the Bureau has agreed – but the overall one-size-fits-all model concept simply does not provide sustainable universal service support for insular price cap LECs.³⁰ The ABC Coalition Comments do not offer any accommodations to the model in order to address the unique difficulties and associated high costs of serving insular price cap LEC areas. The lack of such model accommodations is highlighted by the results of the ABC model, which would reduce ACS’s current support by two-thirds.³¹

That the flawed assumptions underlying the ABC Coalition model are not appropriate for application to ACS and other insular carriers also is demonstrated by the outcome of the their model, which allocates 95 percent of the total CAF Phase II budget to price cap LECs serving the

²⁹ See ABC Coalition Comments at 6-7.

³⁰ It makes little sense for ACS to devote much time or space in these reply comments to noting specifically where it agrees or disagrees with the ABC Coalition Comments because taken as a whole, the one-size-fits-all model advocated is wholly insufficient to provide insular price cap LECs with adequate universal service support and in fact would harm price cap LECs’ ability to continue serving their customers.

³¹ See ACS Comments at 4.

contiguous states.³² It is not unreasonable that the ABC Coalition would support the CQBAT model, which serves its members own interests by advocating that most of the available CAF Phase II support be set aside for price cap LECs in the Lower 48, but the Bureau's responsibility is to address the needs of all price cap LECs, including the insular price cap LECs. There is no support in the record for a finding that such an allocation would serve the universal service goals of the Communications Act by any measure. Similar to the findings in a number of landmark court cases on ratemaking, ACS believes the Bureau should be focused on the total effect, impact, and end result of the methodology that it contemplates using in order to disburse CAF Phase II support.³³ ACS believes the record shows that the end result of establishing the amount of universal service support available to insular price cap LECs based on a methodology that does not account for the unique challenges and costs faced by insular price cap LECs – when that is exactly what the Bureau has been directed to take into account – will be that there will be insufficient universal service support available to any carrier that chooses to serve these insular areas.

It is simply asking too much to require a single model to be able to accurately estimate costs for the relatively homogenous price cap carriers in the Lower 48 and to be able to account for the unique circumstances found in Alaska, as well as the unique circumstances found in other insular price cap LEC areas. If the Bureau cannot with reasonable effort develop its own model that truly accounts for costs differences among the various price cap LECs, it must instead set aside a reasonable portion of the CAF Phase II budget to insular price cap areas – based on the

³² VITELCO Comments at 8-9.

³³ See generally *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989); *FPC v. Hope Nat. Gas Co.*, 320 U.S. 591 (1944); *Washington Gas Light Co. v. Baker*, 188 F.2d 11 (D.C. Cir.) (1950).

unique cost characteristics of their service areas – and develop an alternative to the ABC model for allocating support among the insular price cap LECs. ACS already has provided some of the data necessary to estimate Alaska-specific costs and continues to develop additional inputs. In the interim, the Bureau should rule that insular price cap LECs will continue to receive Phase I support, rather than be forced into a model that will not produce a reasonable result for Alaska and other insular areas.

C. The Bureau Must Address What Is Expected At the End of the Five-Year CAF Phase II Support Term.

At least one critical piece of the analysis seems to be missing altogether from the *Model Design/Data Inputs Public Notice*: what will happen to the supported infrastructure and services at the end of the five-year support period if the price cap LEC accepts support on the terms provided? It is unclear whether support simply will end, or will be entirely redesigned, and a possible new recipient chosen. If the area continues to be unable to sustain a broadband provider without support and the next provider is not required to buy out the previously supported provider, much of the benefit of the current investment supported by CAF Phase II as well as the previous universal service regime – specifically, the remaining life in the infrastructure, a portion of which presumably will be undepreciated -- would appear to be lost. Notably, many of the assets required for broadband service in Alaska and other insular areas have a depreciation schedule set by the Commission that ranges from 10 to 20 to 30 years. It makes no sense to terminate universal service support in five years unless the assets are completely paid for by the five-year mark. At a minimum, if there is to be a buy-out and assumption of the current infrastructure, both the terms of such a transaction and the parameters of the service obligation must be established. If individual carriers will have an opportunity to justify continuation of their support, the criteria for such continuation should be established at the outset. Otherwise

incumbent LECs will be further incented *not* to accept CAF Phase II funding, casting the prospects of broadband deployment in certain areas further in doubt.

D. Competitors to Price Cap LECs Make Unrealistic Claims and Proposals For Allocating CAF Phase II Support.

A number of competitors to price cap LECs have submitted claims and proposals regarding the distribution of CAF Phase II support with a theme that their proposals will prevent inefficient use, or even misuse, of the CAF Phase II support.³⁴ It could be that these commenters lack an understanding of the true costs and difficulties of serving places like Alaska as a provider of last resort (“POLR”). Whatever the reason may be, several commenters err in their characterization of the high-cost program or the intentions of the price cap LECs. While the following responses are far from exhaustive, ACS believes it is important to set the record straight on a number of the most egregious points from the comments of these competitors.

Comments of the American Cable Association. The American Cable Association (“ACA”) alleges that the “Commission should expect that if it utilizes a greenfield cost model with current public interest obligations, the price cap LECs would act rationally and take the extra support and either invest it where the return is greater or increase dividends.”³⁵

Apparently, the ACA is not familiar with the cost of serving areas such as rural Alaska. ACS does not expect there to be any “extra support” under the CAF Phase II program. Indeed, if there were “extra” money, the Commission would not need either a low-end threshold or a ceiling on the per-line costs that could be reimbursed under CAF Phase II, nor would the RAF be

³⁴ See generally Comments of the American Cable Association, *Connect America Fund*, WC Docket No. 10-90, *et al.* (filed July 9, 2012) (“ACA Comments”); Comments of ViaSat, Inc., *Connect America Fund*, WC Docket No. 10-90, *et al.* (filed July 9, 2012) (“ViaSat Comments”); Comments of the Joint Michigan Competitors, *Connect America Fund*, WC Docket No. 10-90 (filed July 9, 2012) (“Michigan Competitors Comments”).

³⁵ ACA Comments at 10.

necessary. In reality, ACS expects the CAF Phase II fund to be inadequate except in a small percentage of Alaska locations. ACS expects that it will spend far more over the next three years than it will receive for the CAF Phase I build out in order to complete the mandatory broadband coverage required for Phase I.³⁶ Contrary to ACA's assertion, the envisioned levels of CAF Phase II support will not determine whether there will be greater returns or higher dividends in Alaska, but rather whether there will be continued broadband deployment in the state at all. ACS challenges ACA to demonstrate to the Bureau where the alleged "extra" money is.

ACA proposes that the "cost model should model the lowest-cost approach available to potential recipients for delivering wireline service to ensure that recipients receive only the amount necessary 'to deliver service that satisfies' the adopted public interest obligations and no more."³⁷ As discussed above, possibly unlike in the Lower 48, there is no single lowest cost approach in Alaska and ACS questions what network technology could reach 100% of unserved locations in Alaska for cost lower than that produced by the ABC Coalition cost model, which as set forth above, is inadequate. The costs of serving the most difficult areas of Alaska and other insular price cap LECs are ignored by such a simplistic proposal. As ACS and other insular price cap LECs have repeatedly stressed, the ABC Coalition model grossly underestimates the build out costs for insular price cap LEC areas.

ACA urges the Commission to "employ a brownfield DSL network as the basis for the cost model since it most accurately reflects the infrastructure price cap LECs would deploy when given the freedom to employ any technology to meet the public interest obligation."³⁸ ACS has

³⁶ ACS expects to spend more than it might otherwise justify in contemplation of the CAF Phase II obligation to provide broadband service to even more locations.

³⁷ ACA Comments at 10 (citation omitted).

³⁸ ACA Comments at 11.

supported the use of a green-field network design for any model the Bureau adopts, noting that a brown-field approach to network design could introduce competitive disparities and produce anomalies in support levels.³⁹ ACS further cautions the Bureau that use of a brown-field network design will put incumbent LECs at a competitive disadvantage vis-a-vis cable competitors, which have no POLR obligations and further which are not rate regulated in Alaska (except for Juneau, Alaska), allowing them to subsidize their broadband build out. A new regime of universal service support should place all recipients of funding on an equal footing, which ACS contends should mean that all support recipients be judged on a new network, whatever the technology.

Building on a brownfield deployment proposal, ACA also proposes that the Bureau “model all costs for areas unserved by broadband, but for served locations model only the operational expenses with the provision that support be capped at the previous high-cost support amount for that location.”⁴⁰ ACS contends that ignoring CapEx and capping support at levels adopted for voice-only networks will never bring broadband to rural Alaska. Further, ACA’s proposal is backwards. Areas currently served by broadband because of existing support should not be *capped* at current support levels, but rather should received *at least* as much support as they currently do because of the additional requirements imposed by CAF Phase II. There is a very simple reason that many areas across the country are unserved by broadband today – because it is extremely difficult and costly to serve these areas and without adequate support to bring broadband to these areas there is no business case to build and operate broadband facilities.

³⁹ See ACS Comments at 9-10.

⁴⁰ ACA Comments at 19.

In establishing benchmarks to determine areas where support should be provided, ACA argues that the Commission should “focus first on establishing an objective methodology upon which to determine the low-end benchmark ... [and] the target low-end benchmark [should] be equivalent to the average revenue offset per subscriber that price cap LECs would reasonably expect in areas where they face no competition.”⁴¹ ACS submits that this argument is based on a self-serving analysis that is designed only to keep the universal service fund as small as possible, but will not ensure that support is sufficient to achieve the statutory objectives set forth by Congress and enacted by the Commission. ACA’s argument fails because it ignores the importance of affordability in determining the lower benchmark, especially in insular areas. A lower benchmark of \$80 as assumed in the current ABC model may be appropriate for some locations, but not for others. As a result, it becomes difficult to determine what revenue can be “reasonably expected.”

In response to the Bureau’s request for comment on data source issues, ACA has agreed with the Bureau that carriers should be required to document their plant mix, document the age of their plant, and document the geographic location of inferior gauge copper plant.⁴² If the Bureau adopts a brownfield approach and implements such plant documentation requirements, then the model should estimate the cost of documenting and upgrading the actual existing plant to the level required to support the Commission’s mandated broadband speeds, rather than an assumed average baseline level of brownfield deployment. However, ACS submits that a cost-benefit analysis of such documentation requirements would take many years to complete and would be labor intensive. Carriers are already being required to do more – expand service and

⁴¹ ACA Comments at 21.

⁴² ACA Comments at 25.

provide better service and submit to additional regulatory oversight – with less resources, both revenue and staff. Beyond the time and labor required to complete the documentation, there would be more time and labor required to validate the results and address disputes. ACS questions what the real benefit would be for expending such resources when the better direction for a new support regime is a greenfield approach to network design, where all recipients of support start on an equal footing and need only justify the going-forward costs of their facilities.

ViaSat Comments. ViaSat claims that it “has demonstrated with the Commission’s own empirical evidence, satellite broadband is the most cost-effective solution for approximately 47 percent of the homes that the Commission deemed ‘unserved.’”⁴³ While satellite is one piece of the technology puzzle needed to provide voice and broadband services to the most difficult and highest cost areas of Alaska, it is just that – one piece of the puzzle. As ACS has documented in this proceeding, use of many technologies is needed to meet the Commission’s broadband expansion goals, at least in Alaska. ACS questions whether satellite can be relied upon exclusively in the most rural parts of Alaska. ACS is not aware of any coverage maps demonstrating satellite coverage at the prescribed broadband speeds in any part of Alaska north of Anchorage; further, speed and latency would need to be tested before consumers are relegated to relying on satellite as an exclusive means of broadband access. Finally, if the Commission elects to support satellite service in lieu of terrestrial service, then it must relieve the carriers of their state and federal obligations to provide voice and broadband to those locations.

Michigan Competitors Comments. Acknowledging that CAF Phase II support is intended to be provided for a period of five years, the Michigan Competitors attempt to pull the rug out from underneath recipients of any such support on the basis that “given the distinct likelihood

⁴³ ViaSat Comments at 5 (citation omitted).

that some unsubsidized competitors would be able to more quickly provide broadband service to certain of these same areas within the five-year period, competitors should have the opportunity in the future to petition the Commission to remove an area from the subsidized list once a competitor is providing service to such area.”⁴⁴

This proposal suspends all economic reality about investments, risks, and returns, but also demonstrates an utter lack of understanding about how broadband networks are built, operated, and maintained. Already, price cap LECs are questioning how they could justify deploying, operating, and maintaining otherwise uneconomic broadband infrastructure with only a five-year commitment of CAF Phase II support. It is nearly impossible to fathom how the Bureau would justify changing the Commission’s policy to allow support to be pulled out from underneath the accepting carrier even as soon as one year into the five-year period. No price cap LEC could accept such business terms as the conditions for the investments that it would be required to make. Adoption of the Michigan Competitors’ proposal would drive all areas eligible for support to auction immediately, and do so in a way that would dramatically undercut the Commission’s broadband deployment goals. If a similar condition were imposed on competitive bidders in such an auction, *i.e.* that they would lose support in any area where the incumbent LEC or another incumbent LEC began offering broadband, such a condition would be sure to drive the bidding far above levels that would prevail in a more predictable business environment.

III. CONCLUSION

For the foregoing reasons, ACS urges the Bureau to develop for Phase II CAF support a separate model that captures the unique geographic characteristics, network deployment

⁴⁴ Michigan Competitors Comments at 5.

challenges, and service profile of the insular price cap LECs and the ACS incumbent LECs in particular. Alternatively, the Bureau should exempt the ACS incumbent LECs from any Phase II CAF model and build out requirements, and authorize the continued support of the ACS incumbent LECs under CAF Phase I. A national CAF II model, as currently conceived, will not capture the special conditions that carriers face in Alaska and other insular areas, nor provide for sufficient support to cover the costs of offering reasonably comparable voice and broadband services at affordable prices, as mandated under the Communications Act.⁴⁵

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⁴⁵ *Model Design/Data Inputs Public Notice at 2, citing Connect American Fund, WC Docket No. 10-90, et al., Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, 17737-38, ¶ 193 (2011).*