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August 3, 2012

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Marlene H. Dortch
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: **Notice of Written Ex Parte**
Connect America Fund, WC Docket No. 10-90
High-Cost Universal Service Support, WC Docket No. 05-337

Dear Ms. Dortch:

Matanuska Telephone Association (“MTA”) submits this letter in support of the Application for Review filed by the National Exchange Carrier Association, Inc. *et al.* in the above-referenced proceedings.¹ The Application urges the Commission to immediately set aside the *Benchmarks Order* because the formulas and resulting caps used in the Quantile Regression Model (“Model”) are based on erroneous data.² MTA supports the Application but understands that overhauling the entire Model may take many months. In the meantime, the Commission, or the Bureau based on delegated authority, should fix obvious errors that are inconsistent with the Commission’s stated intent. Specifically, the Model’s negative Alaskan CapEx coefficient demands immediate consideration and should be eliminated and the model re-run for those carriers negatively affected by this coefficient.

I. INTRODUCTION AND BACKGROUND

As MTA explained in recent meetings with the Commission,³ Paragraph 23 of the *Benchmarks Order* seeks to create an Alaskan coefficient that accounts for

¹ See *Application for Review of the National Exchange Carrier Association, Inc., National Telecommunications Cooperative Association, Organization for the Promotion and Advancement of Small Telecommunications Companies, and Western Telecommunications Alliance*, WC Docket Nos. 10-90, 05-337 (filed May 25, 2012) (“Application for Review”).

² *In the Matter of Connect America Fund; High-Cost Universal Service Support*, Order, WC Docket Nos. 10-90, 05-337, Order, 27 FCC Rcd 4235 (rel. Apr. 25, 2012) (“*Benchmarks Order*”).

³ See *Letter to Marlene H. Dortch from Thomas J. Navin*, WC Docket Nos. 10-90, 05-377 (filed Aug. 2, 2012).



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the additional costs that providers will face in deploying and providing broadband in Alaska. This approach is consistent with the Commission's longstanding position "that the costs incurred to provide local telephone service are generally higher in Alaska than the lower 48 states."⁴ And it is consistent with general available cost information, including the Army Corp of Engineers ("ACE") Construction Cost Manual, which confirm that the cost of providing communications services in Alaska exceeds the rest of the nation.⁵

But—contrary to the Commission's intent—the Model's data results in a -0.6223 Alaskan CapEx coefficient that actually penalizes rural carriers in Alaska, even though they face higher network deployment costs. In essence, the Model concludes that deploying service in Alaska is cheaper than deploying service in the rest of the country, which is plainly not the case.

The effect of the current negative Alaskan CapEx coefficient is incompatible with economic reality and the Commission's intention in Paragraph 23 of the *Benchmarks Order*. Accordingly, at the very least, the Commission should grant the Application for Review, in part, and replace the negative CapEx coefficient with a positive coefficient. Alternatively, the Bureau should clarify that the current negative Alaskan CapEx coefficient is erroneous and either establish a positive coefficient consistent with the Commission's intent in Paragraph 23 of the *Benchmarks Order* or rerun the model with no Alaskan CapEx coefficient for negatively affected carriers.

II. ALASKAN COMMUNICATIONS PROVIDERS FACE HIGH COSTS THAT THE COMMISSION MUST CORRECTLY ACCOUNT FOR IN ITS MODEL.

Alaskan providers face many high costs that preclude the provision of broadband and voice services absent adequate federal funding. These costs stem from, among other things, the state's unique geography and topography⁶, low

⁴ *In the Matter of Arctic Slope Telephone Association Cooperative, Inc.*, Order, 13 FCC Rcd 24217, 24223, ¶ 15 (rel. Dec. 22, 1998) ("*Arctic Slope Order*").

⁵ *Civil Works Construction Cost Index System*, U.S. Army Corps of Engineers, EM 1110-2-1304 (Mar. 31, 2012) ("*ACE Construction Cost Manual*").

⁶ Alaska is the largest state in the union. *State of Alaska Hazard Mitigation Plan 2010*, Division of Homeland Security and Emergency Management, at 4, available at http://ready.alaska.gov/plans/documents/SHMP_2010_UPDATE_ENTIRE_FINAL_COMPLETE.pd
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population density⁷, limited infrastructure⁸, and harsh climate.⁹ Notably, the FCC, the Army Corp of Engineers, other federal agencies, and a bevy of third-party reports all agree that these factors make starting and running a business in Alaska an extremely costly endeavor—much more costly than in the rest of the country.

f (Oct. 2010) (“*Alaska Hazard Mitigation Plan*”). It covers 570,374 square miles – roughly one-fifth of the total land area of the continental United States. *Alaska QuickFacts from the U.S. Census Bureau*, United States Census Bureau, <http://quickfacts.census.gov/qfd/states/02000.html> (last visited Aug. 2, 2012) (“*Alaska QuickFacts*”). From north to south, Alaska measures 1,420 miles, about the distance between Denver, Colorado, and Mexico City, Mexico. From east to west, it measures nearly 2,400 miles, about the distance from Savannah, Georgia, to Santa Barbara, California. *Alaska Hazard Mitigation Plan* at 5. It is not uncommon for an incumbent local exchange carrier (“ILEC”) in Alaska to serve numerous small exchanges, none of which are contiguous. Additionally, an ILEC in Alaska may have a service area of over one thousand square miles. The vast size of Alaska and the distance that must be traversed to reach customers create immense barriers to provision of voice and broadband services. Additionally, Alaska has many mountainous areas, over 3,000 rivers, and 5,000 glaciers, which all add significant operational costs.

⁷ Despite being the largest state in the union, Alaska supports a total population of merely 710,231 people. *Alaska QuickFacts*. The average population density of Alaska is 1.2 persons per square mile. *Id.* Given the low population level of the vast majority of rural villages and communities in Alaska (most have fewer than 2,000 residents), few businesses would be motivated to build telecommunications facilities in the state without the prospect of USF support.

⁸ The road system in Alaska—which consists of 15,329 miles of road statewide—is also very limited, which further increases the costs of deploying and maintaining communications infrastructure. *Alaska Hazard Mitigation Plan* at 23. Alaska has approximately .04% of all roads in the United States, and one mile of road for every 38 square miles of land area. In comparison, the United States average is less than one mile of road to every one square mile of land. *Id.* As a result, the state has over 200 remote, rural locations that are accessible only by air, water or snowmobile. A work project often requires that a crew be flown in from a distance of over one hundred miles. In most rural areas, virtually every piece of plant and work equipment must be delivered by plane, seasonal barge, or “cat-train” when the ground is frozen and snow-covered. The lack of road access materially increases construction and maintenance costs.

⁹ Further, the costs of Alaskan providers are significantly impacted by arctic conditions, such as: (1) the duration of the winter, which limits construction time; (2) snow effects (*e.g.*, snow cover, drifts, and loading); (3) wind load; (4) absolute temperatures (*e.g.*, extreme cold leads to brittleness of many materials); (5) “chill temperature”, which affects work crews in the field; (6) freeze thaw cycles in the presence of moisture (*e.g.*, frost heaves, pole jacking); (7) permafrost; and (8) storm frequency.

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Consistent with the economic realities of operating in Alaska, Paragraph 23 of the *Benchmarks Order* seeks to create an Alaskan coefficient that ensures that the Model correctly accounts for the high costs that providers face in deploying and providing broadband in Alaska. Specifically, the order states:

We also agree with commenters who emphasized that carriers serving particular areas such as Alaska, Tribal lands, and national parks could face unique challenges ... *Alaskan commenters argued that Alaska is unique because of its harsh climate and other factors; accordingly, the methodology now includes a variable indicating whether or not the study area is in Alaska. Benchmarks Order, ¶ 23* (emphasis added).

And Commissioner Clyburn—in remarks before the Senate Committee on Indian Affairs—affirmed that the Model was supposed to account for Alaska’s high costs. Specifically, Commissioner Clyburn highlighted “the unique challenges of serving remote areas of Alaska”¹⁰ and explained that “we included an Alaska specific variable to reflect different costs within that area.”¹¹

A. The FCC Repeatedly Has Concluded that Alaskan Communications Providers Face Extremely High Costs.

The *Benchmarks Order* was not the first time the Commission acknowledged the high costs of serving Alaska. The Commission has long-emphasized “that the costs incurred to provide local telephone service are generally higher in Alaska than the lower 48 states.”¹² The Commission has recognized “the

¹⁰ *Universal Service Fund Reform: Ensuring a Sustainable and Connected Future for Native Communities*, Before the S. Comm. on Indian Affairs, 112th Cong., Oral response of Commissioner Clyburn to question posed by Senator Udall (2012), available at <http://www.indian.senate.gov/hearings/hearing.cfm?hearingid=7c8d7cc581c286db1a78617d93320ce1&witnessId=7c8d7cc581c286db1a78617d93320ce1-1-1>.

¹¹ *Id.* (written statement of Commissioner Clyburn), available at <http://indian.senate.gov/hearings/upload/Mignon-Clyburn-testimony060712.pdf>.

¹² *Arctic Slope Order* at 24223, ¶ 15; see *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 8918, ¶ 255 (rel. May 8, 1997) (“We require that mechanisms developed and selected for rural carriers reflect the higher operating and equipment costs attributable to lower subscriber density, small exchanges, and lack of economies of scale that characterize rural areas, particularly in insular and very remote areas, such as Alaska. We also require that cost inputs be selected so that the mechanisms account
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significant challenges that carriers serving Alaska face,”¹³ noting that “Alaska has very different attributes and related cost issues than do the continental states.”¹⁴ When it comes to universal service reform, the Commission has explained that “it is important to ensure [its] approach is flexible enough to take into account the unique conditions in places like Alaska, ... such as its remoteness, lack of roads, challenges and costs associated with transporting fuel, lack of scalability per community, satellite and backhaul availability, extreme weather conditions, challenging topography, and short construction season.”¹⁵

B. The Army Corp of Engineers (“ACE”) Construction Cost Manual Concludes that Alaska Has the Highest Costs in the Nation.

The ACE’s recently-released “Civil Works Construction Cost Index System” manual highlights that construction costs in Alaska are higher than anywhere else in the country.¹⁶ The purpose of the engineering manual is to

for the special characteristics of rural areas in its cost calculation outputs. We recognize the unique situation faced by carriers serving Alaska and insular areas may make selection of cost inputs for those carriers especially challenging.” (emphasis added); *id.* at 8945, ¶ 314 (“The Joint Board noted that ... carriers serving Alaska have limited construction periods and serve extremely remote rural communities.”).

¹³ *In the Matter of Connect America Fund, et al.*, WC Docket No. 10-90, *et al.*, Third Order on Reconsideration, 27 FCC Rcd 5622, 5633, ¶ 29 (rel. May 14, 2012) (stating that the Commission “appreciate[s] the significant challenges that carriers serving Alaska face”).

¹⁴ *In the Matter of High-Cost Universal Service Support et al.*, WC Docket No. 05-337, *et al.*, Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, 24 FCC Rcd 6475, 6505, ¶ 13 (rel. Nov. 5, 2008) (“The requirements that we adopt for disbursement of high-cost universal service support do not apply to providers operating in Alaska, Hawaii, or any U.S. Territories and possessions. We find that these areas have *very different attributes and related cost issues* than do the continental states.”) (emphasis added).

¹⁵ *In the Matter of Connect America Fund, et al.*, WC Docket No. 10-90, *et al.*, Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, 17828, ¶ 508 (rel. Nov. 18, 2011) (“[I]t is important to ensure our approach is flexible enough to take into account the unique conditions in places like Alaska, ... such as its remoteness, lack of roads, challenges and costs associated with transporting fuel, lack of scalability per community, satellite and backhaul availability, extreme weather conditions, challenging topography, and short construction season.”).

¹⁶ *ACE Construction Cost Manual.*

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“provide historical and forecasted cost indexes for use in escalating [ACE] civil works project costs.”¹⁷ Specifically, the manual contains indexes which the ACE uses to escalate or inflate project costs to current or future price levels. This is accomplished by using the “State Adjustment Factors” contained in the manual, which enable users to estimate the project cost in one state by adjusting it based on the cost from another state.¹⁸

According to the ACE’s indexes, the lowest cost state in 2012 is North Carolina with a factor of 0.77 while Alaska is the highest cost state with a factor of 1.19. Using the ACE’s formula, if a project in North Carolina costs \$1, that same project would cost \$1.55 in Alaska. In other words, for every dollar a provider must spend to construct infrastructure in North Carolina, a provider would be expected to spend \$1.55 in Alaska.

C. Other Sources Confirm the High Cost of Doing Business in Alaska.

Wireless Deployment “Cost Estimator”. The high deployment costs in Alaska are also confirmed by a commonly-used, vendor-based resource that estimates the costs of deploying wireless equipment in different geographic areas. Specifically, the “cost estimator” available at the URL cited below helps vendors estimate deployment costs on a state-by-state basis.¹⁹ Not surprisingly, Alaska is the highest cost state.

KPMG Report. KPMG recently released a study that compared the costs of doing business in over 110 cities worldwide. The study reported that Alaska is a

¹⁷ *Id.* at 1.

¹⁸ In developing these indexes, the ACE used data for “actual” labor, equipment, and materials along with data from several sources including OMB, Producer Price Indexes and other publically available data. The data provided in the manual reflects the CapEx costs present in the telecommunications industry. Much of what drives costs where there is a need to build or maintain infrastructure on a large scale are labor costs, transportation costs, and existing infrastructure (*e.g.*, roads, housing). With Alaska relatively isolated from the rest of the United States, along with a lack of basic infrastructure, the cost for labor and materials to construct anything in the State is very high.

¹⁹ *Pricing Variances*, WirelessEstimator, <http://www.wirelessestimator.com/zipintro.cfm#> (last visited August 3, 2012).

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very expensive place to do business, reporting that “Anchorage and Honolulu—the two cities examined that are not in the Lower 48 US states—both have business costs that are significantly higher than in other US cities and represent the most expensive U.S. cities examined in this study.”²⁰

U.S. Department of Agriculture “Cost of Doing Business in Alaska” Issue Paper. The U.S. Department of Agriculture’s Forest Service recently emphasized the unique costs of conducting business in Alaska. Specifically, the Forest Service explained that “[i]n order to manage national forests in Alaska to a standard consistent with the rest of the agency, ‘Unit Cost Funding’ for the Alaska Region must be higher than regions in the Lower 48.”²¹ Specifically, “[h]igher salaries, higher cost of materials and supplies, and higher transportation costs all combine to increase our unit costs of providing goods and services to our customers and reduce the portion of our budget we can ‘get to the ground.’”²²

III. THE COMMISSION SHOULD ELIMINATE THE NEGATIVE ALASKAN CAPEX COEFFICIENT BECAUSE IT IS IRRECONCILABLE WITH ECONOMIC REALITY AND ITS GOAL OF ACCOUNTING FOR ALASKA’S HIGHER COSTS.

As explained above, Paragraph 23 of the *Benchmarks Order* seeks to create an Alaskan coefficient to ensure that the Model accounts for the high costs of serving Alaska. But—contrary to this intention—the Model results in a -0.6223 Alaskan CapEx coefficient that penalizes rural carriers in Alaska that face higher network deployment costs than providers in other states.

Alexicon, an independent consulting firm, recently analyzed how the negative Alaska CapEx coefficient impacts the CapEx limit calculation for HCLS.

²⁰ *Competitive Alternatives: KPMG’s Guide to International Business Location Costs*, KPMG LLP, at 53 (2012), available at http://www.competitivealternatives.com/reports/2012_compalt_report_vol1_en.pdf; see *America’s Top States for Business 2011*, CNBC (2011), <http://www.cnbc.com/id/41666606> (last visited Aug. 3, 2012) (CNBC compared states based on 43 measures of competitiveness. Alaska was ranked 49th worst for doing business.).

²¹ *Cost of Doing Business in Alaska*, U.S. Department of Agriculture – Forest Service, at 1 (2010), available at http://www.fs.usda.gov/Internet/FSE_DOCUMENTS/stelprdb5252557.pdf.

²² *Id.*

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Specifically, based on Alexicon's analysis, the -.6223 Alaska CapEx coefficient translates into a cost of deploying capital infrastructure in Alaska that is approximately 46% less costly than deploying the same infrastructure in the rest of the country.

Such a result cannot be reconciled with the Commission's and Bureau's recognition "that the costs incurred to provide local telephone service are generally higher in Alaska than the lower 48 states."²³ It also runs counter to the ten-year study by the U.S. Army Corp of Engineers, as well as numerous other data sources, which show that capital projects cost significantly more in Alaska than the rest of the country.

At bottom, the negative CapEx coefficient is arbitrary and capricious because it is incompatible with the Commission's intent to recognize the higher costs of providing service in Alaska in the operation of the Model and with the economic reality of providing communications services in Alaska. Accordingly, the Commission should grant the Application for Review in part and replace the negative CapEx coefficient with a positive coefficient. Alternatively, the Bureau should clarify that the current negative Alaskan CapEx coefficient is erroneous and either establish a positive coefficient consistent with the Commission's intent in Paragraph 23 of the *Benchmarks Order* or rerun the model with no Alaskan CapEx coefficient for negatively affected carriers.

²³ *Arctic Slope Order* at 24223, ¶ 15.



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Thank you for your attention to this matter.

Sincerely,

/s/ Tom Navin

Thomas J. Navin

Counsel for Matanuska Telephone Association

Cc: Chairman Genachowski
Commissioner McDowell
Commissioner Clyburn
Commissioner Rosenworcel
Commissioner Pai
Amy Bender
Angie Kronenberg
Christine Kurth
Carol Matthey
David Goldman
Matthew Berry
Michael Steffen
Julie Veach