Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
Universal Service Reform – Mobility Fund	)	WT Docket No. 10-208
	)	
ETC Annual Reports and Certifications	)	WC Docket No. 14-58
	)	
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 07-135
	)	
	)	
Developing an Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	

Reply Comments of the Rural Broadband Alliance

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SUMMARY

The Rural Broadband Alliance (the "RBA") respectfully submits Reply Comments in response to the Further Notice of Proposed Rulemaking ("FNPRM") issued by the Federal Communications Commission ("FCC" or "Commission") on June 10, 2014. The RBA focuses primarily in these Reply Comments on the Comments filed by other parties regarding proposals for "Longer-Term Reforms for Rate-of-Return Carriers" set forth by the FCC in the FNPRM.[1] In addition, the RBA offers in these comments proposals for specifics to facilitate the implementation of the Commission's proposal as an option for rural rate-of-return carriers to transition from traditional support mechanisms to a new Connect America Fund for rate-of-return territories specifically designed to meet the Commission's overall objective to support voice and broadband-capable networks in areas that the marketplace would not otherwise serve and to ensure that consumers in rural, insular and high-cost areas have access to reasonably comparable services at reasonably comparable rates to consumers living in low-cost areas.[2]

Accordingly, the RBA's Reply Comments also include a specific response to the Commission's invitation to parties to provide "proposals for the design of this Connect America Fund to make more efficient use of universal service funds and encourage the deployment of broadband-capable networks, working within the existing budget of $2 billion for rate-of-return territories."[3] As set forth in these Reply Comments, the RBA concurs with those parties that offered both constructive proposals and a constructive

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[1] FNPRM, paras. 267-269.
[2] FNPRM, para. 267.
[3] FNPRM, para. 268.

process to modify the Connect America Fund ("CAF") model for price cap carriers to meet the needs of consumers residing in territories served by rate-of-return carriers. As an additional consideration, the RBA proposes the inclusion of a "fail-safe" mechanism in conjunction with any model utilized to determine universal service funding to an area served by a rate-of-return carrier in order to ensure that the process results not only in predictable funding levels, but also funding that is sufficient to achieve and maintain the universal service goals in the territory served by the rate-of return carrier.

In setting forth its long-term proposals for rate-or-return carriers, the Commission noted, "[W]e would not implement the limitation on recovery of new investment through the existing mechanisms until the new Connect America Fund was in place and operational." As the Commission winds down the existing HCLS and ICLS mechanisms for those rate-of-return carriers that elect this option, the RBA proposes that a transitional CAF mechanism should be available in order to provide both needed and targeted support for new investment in the areas served by those rate-for-return carriers. Accordingly, the RBA proposes the interim utilization of a CAF 1 fund for rate-of-return carriers that incorporates aspects of the CAF 1 funding mechanism for price cap carriers, together with modifications to better ensure that the distribution of funding is consistent with the guidance the Commission has provided with respect to the establishment of a stand-alone broadband funding mechanism for rate-of-return carriers.[4]

The RBA respectfully submits that the FCC's long-term proposals for rural rate-of-return carriers implemented as recommended herein together with the recommendations proposed for the design of a Connect America Fund for rural rate-of-

[4] See, FNPRM at para. 269.

return carriers will result in more efficient use of universal service funds and "meet the Commission's overall objective to support voice and broadband-capable networks in areas that the marketplace would not otherwise serve and to ensure that consumers in rural, insular and high-cost areas have access to reasonably comparable services at reasonably comparable rates" to consumers living in low-cost areas.[5] The RBA recognizes, however, that the long-term proposal of the Commission pursuant to which "HCLS and ICLS would become the mechanisms to recover only past investment" [6] represents a significant paradigm shift to which many rural companies and their associations and advisers object, as reflected by the Comments submitted in response to the FNPRM.

Accordingly, the RBA urges the Commission to adopt the long-term proposals set forth in the FNPRM[7] together with the RBA's rule implementation proposal and the recommended design for a rate-of-return carrier Connect America Fund as an option, but not a requirement, for rate-of-return carriers.

[5] FNPRM, para. 267.
[6] *Id.*
[7] *Id.*

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Reply Comments of the Rural Broadband Alliance

I. The Longer-Term Reforms for Rate-of-Return Carriers Set Forth By The Commission In The FNPRM Constitute A Sound Foundation For Much-needed Reform Of The Universal Service Distribution Rules For Rural Rate-of-Return Carriers.

A. The FCC's longer-term reform proposals for rate-of-return carriers can form a foundation that efficiently and effectively promotes universal service objectives in high cost to serve rural areas.

The RBA is deeply appreciative to the current Commission and its Wireline Competition Bureau leadership both for several actions adopted in the Seventh Order on Reconsideration and for several proposals set forth in the FNPRM issued on June 10, 2014 in this proceeding. Collectively, the actions taken by the Commission in eliminating the benchmark rule and adjusting the termination of the Safety Net Additive mechanism together with both near-term and longer term reform proposals for rate-of-return carriers have the potential to better achieve the Commission's universal service objectives in territories served by rate-of-return carriers: "to support voice and broadband-capable networks in areas that the marketplace would not otherwise serve and to ensure that consumers in rural, insular and high-cost areas have access to reasonably comparable services at reasonably comparable rates" to consumers living in low-cost areas.[8]

The Commission has proposed "a rule under which no new investment would be included in cost studies used for the determination of HCLS and ICLS after a date certain, and HCLS and ICLS would become the mechanisms to recover only past investment occurring prior to that date certain. Over time, the amount recovered through HCLS and ICLS would diminish, and all new investment would be recovered through a new Connect America Fund for rate-of-return territories . . ."[9]

The RBA respectfully submits that the adoption of this rule in the manner proposed herein together with the well-crafted implementation of a new Connect America Fund ("CAF") for rate-of-return carriers, as recommended below, will advance the deployment and maintenance of universal service with high-speed broadband capability in rural areas, and restore much-needed economic stability by providing predictability in the rate-of-return carrier universal service distribution mechanisms.

With respect to the implementation of the proposed rule and the design of a CAF for rate-of-return carriers, the Commission observes:

> If the Commission were to adopt such a rule, we would not implement the limitation on recovery of new investment through the existing mechanisms until the new Connect America Fund was in place and operational. We welcome stakeholder proposals for the design of this Connect America Fund to make more efficient use of universal service funds and encourage the

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[8] *Id.*

[9] *Id.*

> deployment of broadband-capable networks, working within the existing budget of $2 billion for rate-of-return territories.[10]

In reviewing the initial Comments filed by parties in response to the *FNPRM*, the RBA was disappointed to observe that few rural stakeholders responded to the invitation of the Commission to offer a proposal for the design of a long-term CAF for rate-of-return carriers in conjunction with the proposed rule to utilize HCLS and ICLS only to recover prior investment after a date certain. The RBA respectfully responds to the Commission's invitation, as set forth below. (See, Section II, *infra*).

B. The FCC's longer-term reform proposals for rate-of-return carriers can be implemented as an option.

The initial comments in response to the *FNPRM* are not only devoid of any proposal developed on the foundation of the long-term reform proposal offered by the FCC, but, in fact, those representatives of rural rate-of-return carriers that filed comments generally rejected the Commission's proposed rule.[11] In contrast, and as discussed further below, the RBA has previously proposed revisions to the universal service distribution rules that, similar to the Commission's proposed rule would: 1) wind-down the current rate-of-return carrier support mechanisms; 2) replace those mechanisms with a new CAF for rate-of-return carriers; and 3) clearly separate the utilization of the old mechanisms to recover investments made prior to a date certain from the utilization of a new CAF for rate-of-

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[10] *FNPRM,* para. 268.

[11] See, e.g., Comments of ERTA at pp. 3-6; Comments of the Rural Associations at pp.25-27. In contrast, however, several rural telecom stakeholders have commented on how the Commission's proposal may be adopted to serve the public interest and promote universal service objectives. *See, e.g.,* Comments of the Nebraska Rural Independent Companies ("NRIC") at p. 37 Nebraska and Comments of the Concerned Rural ILECs at p. 17.

return carriers to recover new investment and additional support for ongoing operating expenses in high-cost-to-serve areas.

Change is hard. "Change is hard because people overestimate the value of what they have—and underestimate the value of what they may gain by giving that up."[12] It is fully understandable that the preponderance of comments from representatives of rural rate-of-return carriers rejects the notion of moving to totally new support distribution mechanisms, and that many in the rural telecom industry instead propose modifications to the existing system.[13]

With tweaks and modifications along the way, the existing high-cost recovery mechanisms for rate-of-return carriers have been in place since 1984 when access charges and the USF were implemented. Similar to the circumstances of technological evolution in telecommunications that have led to the present need for change in cost recovery mechanisms for rate-of-return carriers, the advent of today's access charge and USF mechanisms was the result of needed response to technological change that arose from digital technology that enabled competitive long distance service and resulted in the break-up of the Bell System.

The implementation of access charges and USF in 1984 provided rural local exchange carriers with new mechanisms to recover costs that were formerly obtained from a system called "settlements" that involved "division of revenues" that were generally conducted with the Bell System company connecting to the rural carrier's local network. It

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[12] James Belasco and Ralph Stayer, *Flight of the Buffalo* (1994)

[13] *See, e.g.,* Comments of the Rural Associations, pp.6-26; Comments of Alexicon pp. 6-7; Comments of the Small Company Coalition, pp. 2-7.

is difficult thirty years later to imagine the apprehension with which the rural industry moved from the "settlements" system it knew to these new mechanisms.

With over thirty ensuing years of history utilizing access charges and the current USF mechanisms, there are few in leadership roles in rate-of-return companies, associations or advisors who are aware of the past paradigm shifts in cost recovery and rate design mechanisms that worked well over many years for both the rate-of-return carriers and the consumers residing in the rural communities that they serve. There are even fewer who have had any operational experience with mechanisms other than those that rely on jurisdictional cost studies and participation in access revenue pooling. Accordingly, it is not surprising that the vast majority of advisors and associations upon which rural rate-of-return carriers rely for guidance and representation in matters under consideration in this proceeding would naturally develop and propose plans based on maintaining jurisdictional cost studies, pooling, and the utilization of the existing support mechanisms with modifications.[14]

The RBA, functioning as a "think-tank" with no ongoing interest for or against the continuation of the existing mechanisms, approached the challenges of the National Broadband Plan and the Commission's subsequent *NPRM*[15] and concluded that the rural rate-of-return industry would be best served by winding-down the utilization of the

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[14] It should be noted, however, that the rural rate-of-return industry is served by several forward-looking consulting advisory firms that have actively encouraged rural companies to consider and implement concepts including de-pooling, detariffing, consolidation, and other efforts to amortize expenses and obtain efficiencies in the provision of service to higher-cost-to-serve rural areas.

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

existing support mechanisms and transitioning to new mechanisms that better targeted support and more accurately reflected network usage and the evolution to broadband. As a result, the RBA concluded that on a going-forward basis, USF support mechanisms could be simplified and need not rely on jurisdictional cost studies and access revenue pooling.

The RBA also concluded that many in the rural industry may generally "overestimate the value" of the current mechanisms and "underestimate the value of what they may gain by giving that up." In summary, the RBA questioned the continued need for jurisdictional cost studies in a broadband world when the Commission has determined that the provision of broadband is "interstate" in nature: if the fundamental service is entirely deemed interstate, there are no costs to allocate to the intrastate jurisdiction. Similarly, the RBA questioned the continued need for access revenue pooling under the rules and regulations regarding intercarrier compensation adopted by the Commission in the *USF/ICC Transformation Order*.

Taking this bottom-up approach to determine what framework would best fulfill universal service objectives, the RBA questioned the need and value of the cost study and pooling processes and the associated ICLS and HCLS support mechanisms. As a result, the RBA reached the conclusion that rate-of-return carriers and their consumers would be served best by adopting a course similar to that which the Commission has proposed in the *FNPRM*.

The RBA, however, is quick to recognize and underscore that this approach may not be the only viable course for rate-of-return carriers. Moreover, consideration should be afforded to alternative proposals such as the Rural Associations' proposals for Data Only

Broadband ("DOBB") support and the Capital Budget Mechanism (CBM)[16] and the Universal Service Fund Broadband proposal developed by the Small Company Coalition (SCC),[17] as well as to any other proposals intended to promote the ability of rate-of-return carriers to deploy and maintain universal service and high capacity broadband service to consumers residing in the high-cost areas they serve. Recognizing that no single proposal or path may be best for every rate-of-return carrier or the consumers residing in the territories they serve, the RBA urges the Commission to adopt the recommendations proposed herein for the implementation of the proposed rule set forth in the *FNPRM* regarding the ICLS and HCLS mechanisms together with a Connect America Fund designed for rate-of-return carriers as described in Section II below **as an option for rate-of-return carriers**.

Providing rate-of-return carriers with optionality is consistent with past Commission practice. For example, companies utilizing average schedules have had the option to convert to the calculation of their access revenues and USF support on the basis of actual costs; rate-of-return carriers have had the option of participating in the NECA access tariff and pools or de-pooling; some services may be offered on a tariff or detariffed basis; and Part 61.39 of the Commission's Rules and Regulations provides rate-of-return carriers with an optional framework pursuant to which carriers could develop access rates.

Recognizing that providing rate-of-return carriers with options may facilitate the Commission's universal service objectives, the Commission should give further consideration to the proposals submitted by the Rural Associations and the SCC. Similarly, the adoption of the ITTA proposal contemplated in the *FNPRM* to provide rate-of-return

[16] Comments of the Rural Associations, pp. 9-12.

[17] Comments of the SCC, pp. 2-7.

carriers with a transition framework for a voluntary election by rate-of-return carriers to receive model-based support will provide an additional valuable option.[18]

The RBA respectfully submits that any proposal or set of alternative proposals adopted by the Commission should enable every rate-of return carrier to:

1. Obtain support needed to recover existing investment (unless the investment is deemed unlawful under the Commission's existing rules);

2. Obtain support at the level needed to sustain existing operating expense levels (unless an expense is deemed unlawful under the Commission's existing rules); and

3. Provide clarity with respect to what additional support will be available to the carrier to deploy future network upgrades to meet universal service and broadband service requirements and before the carrier incurs additional investment or operating expense commitments.

The RBA respectfully submits that an option for rate-of-return carriers that includes the adoption of the FCC's proposed ICLS/HCLS rule, implemented as recommended herein, together with the establishment of a CAF for rate-of-return carriers, as described below, is responsive to each of these requirements and will, accordingly, foster the ability of rate-of-return carriers to expand and maintain universal service with broadband capability in the territories they serve.

C. The FCC's longer-term reform proposals for rate-of-return carriers can be implemented in a manner that addresses the concerns for stability and certainty that have adversely affected the provision of universal service by rural rate-of-return carriers.

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[18] The RBA notes that the voluntary alternative regulation plan set forth by ITTA incorporates many conceptual aspects consistent with the proposals RBA sets forth in these Reply Comments and with the Transitional Stability Plan proposed by RBA in its April 18, 2011 Comments in response to the *NPRM*.

The RBA appreciates the Commission's recognition of the concerns of rate-of-return carriers regarding the need for stability and predictability in the USF mechanisms, and the impact these concerns have on the provision of universal service. In deciding to eliminate the benchmark rule that utilized the Quantile Regression Analysis ("QRA") methodology to determine limitations on operating and capital expenses incurred by rate-of-return carriers in the provision of universal service that would be subject to USF support, the FCC noted:

> We now conclude that eliminating the benchmarking rule at this time is a prudent step that should enable rate-of-return carriers to evaluate realistically the impact of the reforms adopted in the *USF/ICC Transformation Order* on their business operations and extend broadband-capable infrastructure where economically appropriate. . . .[19]
>
> Given the perception of and concerns with the benchmarking rule, however, we conclude it is appropriate to eliminate it while we consider options to increase incentives for efficient investment of universal service funds.[20]

The RBA especially appreciates the Commission's recognition that even perceptions of uncertainty in how the USF mechanisms operate can adversely effect the provision of universal service.

The Commission also expressed its continuing concerns with the "misaligned incentives" inherent in the HCLS mechanism and the current distribution rules[21] and noted that the elimination of the benchmark rule does not eliminate the need to establish "alternative ways to ensure that rate-of-return carriers have structural incentives to operate efficiently and make prudent expenditures with universal service support."[22]

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[19] *FNPRM* at para. 134.

[20] *Id*. at para. 136.

[21] *See generally, FNPRM* at paras. 136 and 259.

[22] *FNPRM* at para. 136.

The RBA agrees, and articulated these concerns and "addressed the need to restore stability and to provide certainty in order to foster the development and maintenance of universal service in rural service areas in a manner consistent with the overall objectives of the National Broadband Plan" at its first meeting with Commission staff members and at every meeting thereafter.[23]

The RBA was established in 2010 subsequent to the FCC's issuance of the National Broadband Plan that called for major overhaul in the rules and regulations for rate-of-return carriers regarding both universal service funding and intercarrier compensation. Several of the RBA's organizers were among those within the rural rate-of-return carrier industry who had long called for reform of the intercarrier compensation and USF rules in order to meet the changing operational conditions resulting from the evolution of broadband.[24]

RBA's organizers and its rural telephone company supporters fully understood the need to reform both intercarrier compensation and universal service support mechanisms including: reforming the USF contribution mechanism to reflect a better correlation with the use of the network; better targeting of universal service funding and the elimination of

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

[24] *See, e.g.*, "It Is Time To Act On Intercarrier Compensation Reform," by Keith Oliver published in the OPASTCO Advocate, November-December 2003; Letter from Keith Oliver on behalf of Home Telecom and PBT Telecom to Marlene H. Dortch, Secretary, FCC, WC Dkt. No. 01-92 (filed November 2, 2004); "The Back Page - Change Or Die," by Steve Kraskin, March 27, 2014, https://drive.google.com/file/d/0B6nuKaxn4OTbZE9BQVg3eHF4UjA/edit?usp=sharing;

funding based on “identical support” and other flawed USF distribution rules; and reducing cost recovery reliance on switched access services. The RBA also understood the need to address and correct the uncertainty and the instability imposed on rural rate-of-return carriers by the cap on HCLS funding that was established long before the Commission established an overall budget for the USF in *USF/ICC Transformation Order*. Other factors, including the annual rebasing of the HCLS cap and the algorithm-based distribution mechanism utilizing the growing national average cost per loop (“NACPL”), have exacerbated the “cliff effect” and other widely recognized deficiencies in the existing high cost support distribution system for rate-of-return carrier.[25]

Recognizing the need for reform of the existing universal service and intercarrier compensation mechanisms in order to achieve the goals of both the National Broadband Plan and the Congressional Universal Service mandate, RBA’s organizers and supporters charged the RBA with the task of developing sensible, evidence-based universal service mechanisms that would foster deployment and adoption of broadband services for all of the nation’s citizens, including consumers and businesses residing in rural, insular and high cost-to-serve areas of the nation.

In formulating its proposals, the RBA was guided by the four principles established by the Commission:

1. Modernize USF and ICC for broadband;
2. Fiscal Responsibility;
3. Accountability; and
4. Market-driven policies.[26]

[25] *See*, *FNPRM* at paras. 259-260. The RBA generally supports the Commission’s proposed “near-term” reforms set forth in the *FNPRM* at paras. 261-262 to address symptomatic issues in the existing distribution mechanism.

[26] *See, NPRM* at para. 10.

The development of the RBA proposal was additionally guided by the common-sense considerations and concerns provided by rural rate-of-return carriers, which resulted in two fundamental principles:

> 1) Ensuring a reasonable opportunity to recover the investment and operational expenses incurred in providing universal service prior to any rule changes; and
>
> 2) Ensuring clarity and predictability in a new universal service mechanism to provide recovery of needed additional investment and ongoing operational expenses in high-cost to serve areas to enable the provision <u>and maintenance</u> of an expanding level of universal service including high speed broadband connectivity.[27]

In response to the *NPRM*, the RBA filed comments that incorporated a proposal for the adoption of an elective Transitional Stability Plan ("TSP") for rate-of-return carriers.[28] The fundamental aspects of the TSP are consistent with the long-term reform proposals set forth for rate-of-return carriers at para. 267-269 of the *FNPRM*. The TSP essentially proposed a mechanism to distinguish the utilization of existing support mechanisms to recover established investment from the provision of support mechanisms for future investment and operating expenses incurred by a rate-of-return carrier in the provision and maintenance of universal service.

After establishing a date certain for the demarcation of past and future, the TSP proposed that a timeline would be established for the recovery of investment in the old mechanisms. Consistent with the proposals set forth in the *FNPRM*, the TSP proposed that future support required both for new investments and to maintain universal service in the

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[27] On a going-forward basis, additional support is not only needed to expand universal service. The RBA respectfully urges the Commission to recognize that additional support requirements arise from the cost incurred by rural rate-of-return carriers in maintaining universal service and high-speed broadband in rural areas where service was deployed under existing rules. The Nebraska Rural Independent Companies correctly note the importance of ensuring that there is no "backsliding." *See*, NRIC at pp. vi, 3, 36-37.

[28] *See generally*, Comments of the RBA filed in response to the *NPRM* in Docket Nos. 10-90 *et al.*, April 18, 2011.

territory served by the rate-of-return carrier would be distributed through a new CAF. The RBA suggested that rate-of-return carrier universal service CAF support could be model-based, and the RBA offered a proposal for a fail-safe mechanism to ensure that universal service for rural consumers is preserved in the event that facts demonstrate that the model-based support determined for any given area is insufficient.

The RBA respectfully submits that longer-term proposals for reform of USF distribution rules for rate-of-return carriers that incorporate concepts similar to those proposed in both in the TSP and in the *FNPRM* can be designed in a manner consistent with both the guidelines established by the Commission and the two fundamental principles that have guided RBA's efforts: recovery of prior expenses and clarity regarding what future support is available to enable rural rate-of-return carriers to make prudent investment and network planning decisions. Accordingly, the RBA offers below responses to the *FNPRM* inquiry set forth at para. 267-269 concerning the Commission's proposed longer-term proposals for reform in order to achieve and maintain the universal service objectives of voice and broadband-capable networks in areas that the marketplace would not otherwise serve and to ensure that consumers in rural, insular and high-cost areas have access to reasonably comparable services at reasonably comparable rates to consumers living in low-cost areas.

II. The Commission's Longer-Term Proposals For Reform Of USF Distribution Rules For Rate-Of-Return Carriers Can Be Designed In A Manner That Is Both Consistent With The Commission's Guidelines And Responsive To Concerns Of Other Parties

As discussed above, the RBA supports, in the manner recommended herein, the adoption of the Commission's proposed rule to limit the utilization of HCLS and ICLS after a date certain to recover only past investment occurring prior to that date certain together with the implementation of a new CAF for rate-of-return territories. As previously discussed, and in recognition of concerns expressed by rural rate-of-return carrier representatives regarding the adoption of the Commission's proposal, the RBA urges that the proposal for limiting the use of ICLS and HCLS to the recovery of prior expenses be adopted as an option for rate-of-return carriers, and that the Commission give further consideration to alternative proposals as additional options, consistent with the Commission's long-standing history of providing regulatory optionality.

The RBA respectfully sets forth below responses to the questions and issues raised in the *FNPRM* at paras. 267-269.

A. The Commission can adopt the proposed ICLS/HCLS rule in a non-complex manner that provides carriers with a reasonable level of certainty.

The Commission notes in the *FNPRM* that it "would not implement the limitation on recovery of new investment through the existing mechanisms until the new Connect America Fund was in place and operational," and asks, "What timeline would be an appropriate target to set for the implementation of the Connect America Fund for rate-of-return territories and the limitation on recovery of investment in the old mechanisms?"[29]

The Commission should implement a CAF for rate-of-return carriers simultaneously with the adoption of a rule limiting the utilization of ICLS and HCLS to the provision of support for prior investments. To do otherwise would deprive rate-of-return carriers of any potential additional support needed to maintain and expand the provision of universal

[29] *FNPRM* at para. 268.

service to consumers residing in the territories they serve. As discussed in Section II B, *infra*, the RBA suggests the adoption of a CAF for rate-of-return carriers that provides a transition to universal service support fully based on a rate-of-return carrier CAF model when the carrier's ICLS and HCLS support ends after prior investments are recovered.

By making a transitional amount of CAF support available to a rate-of-return carrier during the transition winding down the ICLS and HCLS mechanisms, the carrier will have an opportunity to obtain support needed to expand and maintain universal service to eligible locations. At the conclusion of the transition, when the provision of support from the old ICLS and HCLS mechanisms ends, the rate-of-return carrier would receive only support based on the CAF model designed for rate-of-return carriers.

The question of how long to maintain the provision of ICLS and HCLS mechanisms to recover past investment is an issue that may be resolved in two distinct ways: on an individual company basis or, alternatively, on a simpler uniform basis that could serve as an incentive to rate-of-return carriers to elect to utilize this option to transition from traditional "rate-of-return" regulation and support mechanisms to a model-based support system.[30] Under either scenario, the electing rate-of-return carrier would, as of the date certain designated by the Commission, freeze its regulated rate base for purposes of determining its ICLS and HCLS support.[31]

[30] Providing an incentive is consistent with the Commission's expressed interest in facilitating voluntary participation in model-based support and incentive regulation. *See May 2013 Public Notice*, 28 FCC Rcd at 7205-08, paras. 8-19.

[31] The RBA also recommends freezing or capping the carrier's existing Subscriber Line Charges (SLCs). The Rural Associations expressed concerns regarding the impact on SLCs and company-specific benchmarks, but implementation of the Commission's proposed ICLS/HCLS rule does not raise the need for company-specific benchmarks or any associated concern. *See*, Comments of the Rural Associations, p. 24.

1. Implementing the proposed rule on an individual company basis.

Should the Commission elect to implement the proposed rule on an individual company-specific basis, the company's annual loop cost calculation for purposes of determining ICLS and HCLS support would be calculated in the initial year on the basis of the frozen regulated rate base. In subsequent years, the calculation of loop costs would be based on the frozen rate base level reduced to reflect the accumulated depreciation of the capital investment in accordance with Part 32 of the Commission's rules.

If the Commission proceeds to implement the proposed rule on a company-specific basis, there would be no resulting inordinate administrative burden on either the rate-of-return carrier.[32] The only additional administrative requirement undertaken by the electing rate-of-return carrier under this company-specific approach would be the reporting of the annual reduction in the frozen loop costs resulting from depreciation of the capital investment.[33]

Under this company-specific approach, recovery from the ICLS and HCLS mechanisms would continue until the frozen capital investment is fully depreciated for each rate-of-return carrier that elects this option. In addition, this approach would lead to

[32] Representatives of rural parties expressed concern that the implementation of the Commission's proposed ICLS/HCLS rule would lead to inordinate additional compliance costs. *See, e.g.*, Comments of the Rural Associations, p. 25. Pursuant to the company-specific implementation proposal set forth above, the only additional administrative function is the annual recalculation of the loop costs based on accumulated depreciation, a relatively simple calculation. The RBA is confident that many if not most rate-of-return carriers would agree that it would not be inordinately burdensome to perform this additional calculation in exchange for increased certainty and stability in the recovery of existing costs.

[33] In fact, a rate-of-return carrier electing this option could potentially reduce its administrative burdens and costs by eliminating the need to perform a cost study if it contemporaneously elected to establish its special access rates on the basis of alternative regulation.

inequitable results if it were adopted on an optional basis and an electing company's HCLS was calculated on the basis of frozen prior investment while HCLS for non-electing rate-of return carriers was calculated on the basis of current investment. The value of certainty and predictability in the provision of support for prior expenses would be lost. Accordingly, the RBA recommends the utilization of the simpler, uniform option set forth below.

2. Implementing the proposed rule on a simpler, uniform basis.

Alternatively, the Commission could elect to implement the proposed rule and provide its application to an electing rate-of-return carrier on a uniform and simpler basis that would be applicable to all electing carriers. By doing so, the Commission could also provide an incentive to transition to a new CAF model-based support mechanism for rate-of-return carriers. Under this alternative, the electing carrier would not only freeze its regulated rate base as of a date certain for purposes of calculating ICLS and HCLS support, but it would freeze and phase down the ICLS and HCLS annual support provided to it.[34]

The time period during which the frozen and phased down ICLS and HCLS support would be available to all of the electing rate-of-return carriers would be established to approximate the average remaining economic life for the depreciation of the frozen rate base capital investment of the electing rate-of-return carriers. The initial frozen ICLS and HCLS support amount for each carrier would be reduced annually by a factor that results in a reduction approximating the full depreciation of the capital investment in the rate base.[35]

[34] The Nebraska Rural Independent Companies have proposed a similar alternative. *See*, NRIC at p. 38.

[35] The RBA initially proposed the utilization of an annual 3% factor reduced by one-half of the nationwide CPI inflation factor in its April 18, 2011 comments setting forth the Transitional Stability Plan.

Under this scenario, the utilization of ICLS and HCLS would cease at the end of a recommended 10-year period (or whatever period the Commission determines as an approximation of the average depreciation schedule of the capital investment in place as of the date certain established by the Commission).[36]

With the termination of support for prior investment from the old ICLS and HCLS mechanisms, the electing rate-of-return carriers would subsequently receive universal service support on the basis of a new model-based CAF for rate-of-return carriers, as discussed further in Section II C, *infra*. In order to ensure that the electing rate-of-return carriers have an equitable opportunity to obtain support necessary for new investment needed to expand and maintain universal service and high-speed broadband connectivity within their territories, the RBA proposes the utilization of a transitional CAF 1 for the electing rate-of-return carriers as described in Section II B, *infra.*

By adopting a thoughtfully crafted CAF mechanism for rate-of-return carriers together with the adoption of this recommendation for the implementation of the proposed rule to terminate the utilization of the old ICLS and HCLS mechanisms after the recovery of investment made prior to a date certain, the Commission can advance its universal service objectives. Moreover, the implementation of this option enables the Commission to

[36] The RBA notes that a ten-year period is consistent with the timeframe the Commission established for the Connect America Phase II support awarded through the competitive bidding process at para. 35 of the *Report and Order* released in this proceeding on June 10, 2014. Recognizing the reality that any period intended to approximate the average remaining depreciation schedule of prior investment may be critically insufficient for an individual carrier, the Commission should provide a carrier with an opportunity to obtain a waiver to extend the period in an instance where good cause is demonstrated under the Commission's standard waiver process.

address efficiently and effectively the establishment of stand-alone broadband support in a manner consistent with the guidance set forth by the Commission in the *FNPRM*.[37]

B. The provision of a CAF 1 for rate-of-return carriers prior to the termination of the old ICLS and HCLS mechanisms will serve the public interest and help achieve the Commission's universal service objectives.

1. It is essential for the Commission to determine how much of the annual $2 billion rate-of-return carrier budget is required to support prior investment and ongoing operations, and how much is available to each carrier for new investment.

With respect to the proposed ICLS/HCLS rule, the Commission observes in the *FNPRM*:

> If the Commission were to adopt such a rule, we would not implement the limitation on recovery of new investment through the existing mechanisms until the new Connect America Fund was in place and operational. We welcome stakeholder proposals for the design of this Connect America Fund to make more efficient use of universal service funds and encourage the deployment of broadband-capable networks, working within the existing budget of $2 billion for rate-of-return territories.[38]

The RBA respectfully responds to the Commission's invitation to propose a design of the CAF for rate-of-return carriers within the budget limitation established by the Commission. Although the RBA does not agree that the $2 billion USF budget for rate-or-return carriers is sufficient both to provide the support required to recover both prior investment and the

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[37] *See* Section III A, *infra*. The RBA notes that the Commission has also asked, "If the Commission were to wind down the existing HCLS and ICLS mechanisms and create a new Connect America Fund for use in rate-of-return territories, what action should the Commission then take in its pending rate represcription proceeding?" *FNPRM* at para. 268. Since "rate of return" is no longer utilized to establish switched access rates, the Commission could obviate any near-term need for proceeding with rate represcription if it considered changes in establishing special access rates for rate-of-return carriers in a manner that addresses the universal service and related broadband provision considerations associated with special access.

[38] *FNPRM* at para. 268.

support necessary to meet the broadband connectivity obligations associated with universal service, the RBA recognizes the current pragmatic reality of the budget limitation.

As discussed further in Section IV, *infra*, long-term universal service objectives cannot be achieved in the absence of a fact-driven evidence based review of universal service costs and the resulting funding requirements and budget needs. In the near-term, the experiences under the benchmark rule have demonstrated that it is not sufficient to simply establishing a budget for rate-of return carriers without considering how much of the budget is required to recover the existing just and reasonable expenses to provide universal service, and how much of the budget is available to support much-needed additional investment in rural infrastructure.

The Commission's proposed rule to utilize ICLS and HCLS as mechanisms to recover only past investment occurring prior to a date certain is a useful tool in the identification of how much of the $ 2 billion budget is clearly needed to recover existing investment and ongoing operating expenses, and how much is available to support new investments. While every rate-of-return carrier would like to receive support sufficient to expand its provision of service to meet the broadband service obligations throughout its service territory, no rate-of-return carrier can survive if it does not have a reasonable opportunity first to recover the costs it has already incurred in the provision of universal service.

The experience with the now eliminated benchmark rule and the utilization of the associated QRA also resulted in heightened awareness within the rural carrier community of the importance of the RBA objectives: 1) recovery of existing investment and 2) clarity regarding what support is predictable and available for additional investments and operating expenses prior to a carrier making a financial commitment.[39]

If the Commission were to adopt and apply the proposed ICLS/HCLS rule to all rate-of-return carriers in the manner proposed herein, the Commission could develop a schedule indicating how much of the rate-of-return carrier annual budget would be utilized each year for support of prior investment and ongoing expenses, and how much of the budget would be available to support new investment and operating expenses.[40] Consistent with its own guidelines, the Commission could then establish how best to distribute that portion of the budget available for new investment and expenses "equitably and efficiently, so that all rate-of-return carriers have the opportunity to extend broadband service where it is cost-effective to do so."[41]

The RBA respectfully submits that this objective could be achieved by establishing a rate-of-return carrier CAF 1. The funding for CAF 1 would come from that portion of the rate-of-return carrier budget that is not needed to fund recovery of prior costs (including the USF rate-of-return carriers receive to offset access rate reductions). In addition, "the collected-but-not-yet-distributed support from the $2 billion annual budget for rate-of-

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[39] *See, e.g.*, Comments of the Concerned Rural ILECs at p. 5 ("Any replacement mechanism needs to focus on the recovery of existing costs and must provide incentives for meeting the voice and broadband public interest standards that the FCC has established going forward. As the FCC moves forward with near and long term USF reform, it must ensure that carriers have the ability to recover both their existing and new investments that have been and will be incurred in meeting the FCC's universal service goals.") and at p. 18 ("Allow supported carriers to calculate what their support will be, based on standard formulas that are not subject to change on a regular basis."). *See, also,* NRIC at p. 16.

[40] This straightforward, and much-needed, calculation mitigates any concern regarding the USF budget impact of adopting the Commission's proposed ICLS/HCLS rule. *See*, Comments of the Rural Associations, p. 26. Similar to the proposal set forth above, the Nebraska Rural Independent Companies correctly observe the importance of ensuring that the entire budget allocated for rate-or-return carriers is expended. *See*, NRIC at p. 7-8.

[41] *FNPRM* at para. 269.

return territories currently in the broadband reserve account should be used to kick start such a mechanism."[42]

2. If the proposed ICLS/HCLS rule is adopted as an option, a Rate-of-Return Carrier CAF 1 can be implemented within the current budget and distributed equitably to extend broadband service in the territories of the rate-of-return carriers that utilize this option.

As previously discussed, the RBA recognizes the many rural associations and advocates oppose the adoption of the Commission's proposed ICLS/HCLS rule and have submitted alternative proposals for the distribution of the rate-of-return carrier USF budget. The RBA encourages the Commission to consider the adoption of these and other viable proposals as alternative options for rate-of-return carriers in addition to the adoption of the proposed ICLS/HCLS rule and CAF for rate-of-return carriers. Recognizing that there is no "perfect" way to distribute a limited budget that will satisfy all stakeholders, the provision of optionality and the subsequent evaluation of results under each option will inform the Commission as it proceeds in the long-term.[43]

Should the Commission elect to provide rate-of-return carriers with optionality, concerns regarding "the budget implications of voluntary selections"[44] can be easily mitigated. The portion of the overall rate-of-return carrier budget allocated to companies

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[42] *See*, FNPRM at para. 269.

[43] The RBA cautions, however, that any proposal adopted by the Commission, irrespective of its provision as an option, could impede and impair universal service to rural consumers unless it clearly incorporates the three fundamental attributes previously discussed: 1) provides support needed to recover existing investment (unless the investment is deemed unlawful under the Commission's existing rules); 2) provides support at the level needed to sustain existing operating expense levels (unless an expense is deemed unlawful under the Commission's existing rules); and 3) provides clarity with respect to what additional support will be available to the carrier to deploy future network upgrades to meet broadband service requirements and needs before the carrier incurs additional investment or operating expense commitments.

[44] *See, e.g.*, Comments of the Rural Associations, p. 68.

participating in each option could be determined by aggregating the USF received by each company during a base year.

Thereafter, companies participating under one option (and the overall budget available to those companies) would not be affected by the operations of companies participating in any other option or the mechanics of that option.[45] To the extent that the annual support requirements for companies participating in any option exceeded the budget allocated for those companies, "reductions in support would be spread proportionally among all " the rate-of-return carriers participating in that option.[46]

By applying this optionality approach, the Commission can proceed to adopt its proposed ICLS/HCLS rule in the manner recommended herein together with a CAF designed for rate-of-return carriers, and simultaneously evaluate the effectiveness of proposals offered by other parties.

The establishment of a CAF 1 for rate-of-return carriers that elect to operate under the proposed rule to limit the utilization of HCLS and ICLS to the recovery of existing expenses is essential. As previously discussed, if CAF is not available until payments from ICLS and HCLS terminate, there would be no support available for new investment. As ICLS and HCLS are utilized to recover existing investment, the ICLS and HCLS payments to the carriers participating in this option will decline, thereby freeing up some of the USF budget that can be utilized to fund the CAF 1 for these carriers.

[45]The RBA believes that the impact of this proposal to apportion and segregate the budgets available to all companies electing a particular option is similar to the ITTA suggestion regarding the impact of participation in its proposed voluntary optional plan on the HCLS Cap. *See*, Comments of ITTA, p. 29.

[46] The intent of this recommendation is to provide consistency with the underlying intent of the proposal set forth by the Commission. *See*, *FNPRM* at para. 262.

The CAF 1 for rural rate-of-return carriers would be utilized to support new investment and expenses required to serve eligible locations within the carrier's service area. Similar to the utilization of the CAF 1 for price cap carriers, the funding would essentially constitute "stand-alone broadband" funding because it would be distributed and utilized to provide connections with high-speed broadband capacity, and without regard to whether the customer elects to utilize the connection for traditional switched voice service. Accordingly, the RBA encourages the Commission to utilize the broadband reserve account to provide additional funding for the rate-of-return carrier CAF 1 consistent with the consideration referenced by the Commission in the *FNPRM*.[47]

Undoubtedly, the aggregate support needed to expand universal service to eligible locations will exceed the amount of available funding in the proposed CAF 1 for rate-of-return carriers. The distribution of the limited funding available in the proposed CAF 1 for rate-of-return carriers must be equitable, efficient and provide the participating rate-of-return carriers "with the opportunity to extend broadband service where it is cost-effective to do so," as required by the Commission.[48]

Any effort to achieve the desired result inevitably confronts the need to balance two competing public policy interests: 1) providing support to connect eligible locations in the highest cost to serve areas; and 2) utilizing scarce USF resources to add as many high capacity broadband connections as possible. In order to balance these two significant, but

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[47] *See*, *FNPRM* at para. 269. To the extent the Commission decides both to utilize the broadband reserve fund as contemplated in the *FNRPM* and to permit optional plans for rate-of-return carriers as discussed above, it could also proportionately distribute the available "kick start" funding to the carriers participating in each option in the same proportion that the overall rate-of-return carrier budget is allocated to the carriers participating in each option.

[48] *FNPRM*, at para. 269.

potentially contending interests, the RBA suggests that the rate of return carrier CAF 1 annual funding amount should be apportioned to the participating rate-of-return carriers based on their relative portion of eligible locations to the total number of unserved or underserved connections of all of the rate-of-return carriers that elect the option to utilize ICLS and HCLS to recover prior expenses.[49]

C. Modifications to the CAF Cost Model for price cap carriers are required before it can be applied to rate-of-return carriers

The rate-of-return carriers that elect the option proposed herein and utilize ICLS and HCLS to recover prior expenses would no longer receive support from the old mechanisms after they have recovered their prior investments. Thereafter, the support provided to these companies would be provided from the CAF and determined on the basis of a forward-looking cost model designed for territories served by rate-of-return carriers.

1. The development of a model-based CAF for rate-of-return carriers requires modifications to the CAF model developed for price cap carriers.

The RBA is appreciative of the FCC's recognition that the CAF model designed for price cap carriers requires modifications before it could reasonably be utilized to determine support for territories served by rate-of-return carriers.[50] Although an array of commenters voiced concerns with the CAF model, few offered substantive responses to the

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[49] The Nebraska Rural Independent Companies offer another viable allocation alternative entitled the "Benchmark Method." NRIC at p. 15. NRIC also observes that, similar to the RBA proposal, the FCC can adopt a relatively simple approach whereby rate-of-return carriers electing to receive ICLS and HCLS to recover prior expenses may freeze the ICLS and HCLS support levels "and then gradually transition to a long-term CAF mechanism designed to address the specific operating characteristics of ROR Carriers and the levels of support dictated by that new mechanism." NRIC at p. 38.

[50] *See, e.g.*, *FNPRM* at par. 290 ("Here, we ask commenters to address what specific changes should be implemented in the model before using it to calculate the offer of model-based support for rate-of-return carriers that voluntarily elect to receive model-based support.")

Commission's request for proposed modifications. The most notable exception is the comprehensive set of suggestions and recommendations offered by NRIC.[51]

NRIC has set forth several aspects of the model that warrant consideration, and notes that the lack of access to the underlying data utilized to develop the CAF model for price cap carriers is an impediment to the development of more specific modifications to the model. Accordingly, NRIC proposes that the Commission establish a virtual workshop process to work toward the development of a model-based CAF for rate-of-return carriers and provide an opportunity for a more informed process inclusive of rate-of-return carriers that did not participate in the development of the price cap model.[52] The RBA agrees with NRIC recommendation and urges the FCC to adopt it.

The concerns of the rate-of-return industry with model-based support in general are well founded and set forth in the comments of several parties.[53] A critical concern is the fundamental need for precision to ensure that the model reflects the attributes of the rate-of-return carriers who generally serve pockets of the most challenging and high-cost to serve areas of the nation where larger carriers historically and currently have had no interest in serving.

In contrast, the operations of larger price cap carriers are affected by their size and their larger geographic footprint that combine areas with both higher and lower populations density. These factors, distinct from smaller rate-of-return carriers, are undoubtedly reflected in both the inputs and outputs associated with the model developed

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[51] *See,* NRIC at pp. 27-35.

[52] *Id*. at p. 27 and 34.

[53] *See, e.g.,* Alexicon at pp. 6-7; and The Rural Associations at pp. 16-17.

for larger price cap carriers. As a result, a higher degree of precision in the model development is not as critical for price cap carriers. The price cap model may underestimate support in part of the price cap carrier's territory and overestimate support in another area.

In contrast, as ITTA points out, "rate-of-return carriers serve smaller, lower density geographic areas and do not share the same flexibility to adapt to inaccuracies produced by a model."[54] Accordingly, the RBA supports continued efforts to identify and address modifications in the price cap model required to develop a model-based CAF for rate-of-return carriers.

2. The design of a model-based CAF for rate-of-return carriers should incorporate a fail-safe mechanism to ensure that support in any specific area is sufficient to fulfill universal service objectives.

No model could ever sufficiently predict in every instance and circumstance the costs of providing universal service under any and all circumstances in every territory served by every rate-of-return carrier. NRIC notes the occurrence of "exogenous and/or force majeure events" that could produce the need for additional support not predicted by a model. To address this possibility, NRIC asks for Commission confirmation of its intent to utilize "the application of the traditional waiver standard under 47 C.F.R. 1.3."[55]

The RBA respectfully submits that in addition to issues associated with exogenous changes and force majeure events, there may be instances where any model simply

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[54] ITTA at p. 33.

[55] NRIC at p. 18, fn. 33.

produces results for a particular area that will not adequately support and maintain universal service. Irrespective of models and economic theories, the reality is that there are real costs to build and operate a network to provide universal service.[56]

At best, a model is a representative prediction of these costs. Accordingly, the design of a CAF for rate-of-return carriers should provide a waiver process, as discussed by NRIC, that affords the rate-of-return carrier the opportunity to demonstrate that the just and reasonable expenses associated with the provision of universal service requires support levels greater than that predicted by the model.

The concept of a "fail-safe" is not new to the Commission. When the price cap mechanism was developed for the larger local exchange carriers, the objective of the large carriers was to escape the earnings limitations of rate-of-return regulation applied to their shrinking regulated rate base. At the same time, however, the larger carriers seeking relief from rate of return regulation sought a "fail-safe" to protect them against the possibility that the new price cap regime might not generate sufficient earnings. As a result, the Commission provided the large carriers converting to price caps with a "fail-safe" by incorporating into the price cap regulations a "low-end adjustment" mechanism that provides for rate adjustments in the event that the carrier's earnings fall inordinately.[57]

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[56]While economists and parties argue the merits of utilizing "forward-looking" or "embedded" costs, the operating reality is that any business plans on the basis of anticipated or "forward-looking" costs. In the real world, a business makes a commitment to incur a "forward-looking" cost only if it rationally concludes that it has an opportunity to recover the cost and a reasonable return on investment associated with the investment risk. Once the business makes the financial commitment and incurs the forward-looking cost, the cost becomes "embedded. This is true for all businesses - not only telecommunications businesses and not only rate-of-return carriers. Several parties have accordingly noted that a CAF designed for rate-of-return carriers must provide sufficient and predictable support required to recover the "forward-looking" costs over the economic life of the investment. *See, e.g.*, NRIC at pp. 54-56.

[57] *See*, 47 C.F.R. § 61.45(d)(1)(vii).

In the final analysis the only reason for universal service support funding is not to protect the carrier (as the low-end adjustment mechanism was intended), but to ensure that reasonably comparable rates are available to consumers residing in high cost to serve areas. The RBA respectfully submits that the design of a CAF for rate-of-return carriers that incorporates the fail-safe mechanism proposed above will not only serve the public interest by advancing these objectives, but is essential to achieve and maintain the nation's universal service objectives.

III. Adoption of the Proposed ICLS/HCLS Rule Together With The proposed CAF For Rate-of-Return Carriers Provides An Optional Plan For Rate-Of-Return Carriers That Will Advance Universal Service Objectives Within the Commission's Guidelines And Principles.

A. The proposed optional plan is consistent with the Commission's guidelines and addresses additional concerns raised by the Commission.

The adoption of the RBA's recommendations for implementing the Commission's proposed ICLS/HCLS rule together with the adoption of a CAF for rate-of-return carriers as suggested herein will provide universal service reform for territories served by rate-of-return carriers and advance the Commission's universal service objectives in a manner that is consistent with both the implementation guidance set forth by the Commission[58] and the core principles for reform adopted by the Commission in 2011.[59]

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[58] *FNPRM* at para. 269.

[59] *See, FNPRM* at para. 267 referring to "the core principles adopted by the Commission in 2011" which were set forth in the February 9, 2011 *NPRM* at para. 10.

1. The option to utilize ICLS and HCLS to recover past expenses in combination with the implementation of the recommended design for a new rate-of-return carrier CAF provides a "stand-alone" broadband funding mechanism.

The consideration of issues regarding a "stand-alone" broadband funding mechanism can be comprehensively resolved by the adoption of the Commission's proposal to utilize ICLS and HCLS to recover prior investment and to utilize a new CAF for rate-of return carriers to provide needed support for new investment.[60]

With regard to existing investment, rate-of-return carriers are understandably concerned with the adverse impact of the existing HCLS rules on the provision of support when a customer chooses to utilize a connection for stand-alone broadband service. When a rate-of-return carrier made existing loop investment, the carrier considered whether support reasonably predictable under existing rules would be sufficient to warrant the investment. With respect to the vast majority of existing loop investment by rate-of-return carriers, it is not likely that anyone would have contemplated either the possibility that the customer would subsequently utilize the loop only for broadband service or the resulting impact of that decision on the carrier's opportunity to receive support and recover the investment.

This concern is efficiently and effectively addressed by the adoption of the Commission's proposal to utilize ICLS and HCLS to recover prior investment. By implementing the proposal as recommended in the optional plan set forth herein, the rate-of-return carrier's loop costs will be frozen as of a date certain for purposes of calculating

[60] *See, FNPRM* at para. 270 where the Commission sets forth issues that arise as a result of utilizing funding mechanisms that do not distinguish support for past and future investment.

ICLS and HCLS support. As a result, the rate-of-return carrier will not lose support as a result of a customer's election to utilize the loop for broadband only.

The recommended implementation of the Commission's ICLS/HCLS proposal effectively provides a "stand-alone" broadband funding mechanism for the recovery of costs associated with past investment subsequently utilized by the consumer for "stand-alone" broadband service. The rate-of-return carrier will continue to receive support calculated in a manner consistent with the carrier's expectations when the investment was made. The carrier will receive neither additional nor reduced support for prior investment as a result of the consumer's choice to utilize a connection for broadband only.

The adoption of a CAF for rate-of-return carriers, as recommended herein, also provides a "stand-alone" broadband funding mechanism to provide support for new investment and related operating expenses. In contrast to the FCC's old rules utilizing voice service line counts in the calculation of support, the Commission has established CAF for price cap carriers as a mechanism that supports connections with the capability to provide universal service and high-speed broadband connectivity. The amount of CAF support made available to a price cap carrier is not increased or reduced on the basis of how the customer elects to utilize the supported connection.

The adoption of the CAF for rate-of-return carriers as proposed herein would similarly provide support for new investment and associated operating expenses to provide connections that enable universal service and high-speed broadband connectivity without regard to how the consumer chooses to utilize the connections. The proposed CAF for rate-of-return carriers would, accordingly, provide the "stand-alone" funding that the Commission has proposed to adopt.[61]

2. The option to utilize ICLS and HCLS to recover past expenses in combination with the implementation of the recommended design for a new rate-of-return carrier CAF is consistent with the guidelines the Commission has set forth.

In the *FNPRM*, the Commission provided specific guidance on its desired implementation of a support funding mechanism for "stand-alone" broadband.[62] The proposals set forth herein are consistent with each of the guidelines provided by the Commission.

(a) *<u>Calculate support amounts that remain within the existing rate-of-return budget.</u>*

Although the RBA continues to question whether the existing USF budget for rate-of-return carriers is sufficient, the proposals set forth herein can be implemented to calculate support amounts that remain within the existing rate-of-return budget. In fact, the utilization of the Commission's proposed ICLS/HCLS rule to recover past expenses can be implemented in the manner proposed herein to provide rate-of-return carriers with much-needed predictability concerning the receipt of support.

Pursuant to the proposed option, the Commission and carriers can calculate how much of the annual budget will be utilized to recover prior expenses and how much is available to support new investment and related operating expenses.[63] As a result, rate-of return carriers will have restored stability and would no longer be concerned that the

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[61] *FNPRM* at para. 269.

[62] *Id*.

[63] *See,* Section II B 2, supra, that further addresses how the proposals set forth herein can be implemented within the current budget.

unpredictability of rule changes and fluctuating HCLS calculations will result in the loss of opportunity to recover prior expenses. Equally significant, rate-of-return carriers operating under the proposals set forth herein will have clarity regarding what additional support is available prior to making universal service investment commitments that would not be rational in the absence of sufficient support.

(b) ***Distribute support equitably and efficiently, so that all rate-of-return carriers have the opportunity to extend broadband service where it is cost-effective to do so.***

In any instance of attempting to distribute a limited budget to multiple recipients with reasonable and rational need for budget distributions that in the aggregate exceed the available budget, it is unlikely that any proposed distribution will be either perfect or satisfactory to all parties. As discussed previously in these Reply Comments and throughout this proceeding, the RBA respectfully submits that equitable distribution of the limited USF budget for rate-of-return carriers requires adherence to two principles:

> 1. Distribution of support to each carrier that reasonably approximates the support the carrier rationally anticipated when making investments and establishing just and reasonable expense levels under the Commission's prior rules; and
>
> 2. Clarity regarding the level of support available to a carrier for new investments and related expenses to provide universal service before the carrier makes financial commitments to incur additional investment and expenses that require support.

The adoption of the proposals set forth herein result in equitable and efficient support distribution in a manner consistent with these principles. A significant portion of the current annual budget would be utilized first to recover prior expenses. That portion of the annual budget available to support new investment and related expenses would be distributed to rate-of-return carriers on a proportionate basis to ensure that every carrier has an opportunity to utilize a portion of the available funding to extend the provision of universal service and high-speed broadband connectivity.[64] Once the budget has been utilized to recover prior investment, carriers would have access to an equitable portion of the annual budget determined by the model-based CAF for rate-of-return carriers (modified in accordance with the proposed "fail-safe" waiver process in those instances where the model-based support is demonstrably insufficient to support universal service in the carrier's territory).[65]

(c) ***<u>Distribute support based on forward-looking costs (rather than embedded costs)</u>***

Under the Commission's proposal regarding the utilization of ICLS and HCLS to recover prior investments, a portion of the rate-or-return carrier USF budget would continue to be distributed on the basis of embedded costs. As the past costs are recovered, however, that portion of the budget utilized to recover embedded costs will decline. Support for new investment and related expenses under the proposal set forth herein would be based on a forward-looking cost model for rate-of-return carriers (subject to the "fail-safe" waiver process to endure the provision and maintenance of universal service to consumers residing in territories served by rate-of-return carriers).

(d) ***<u>Ensure that no double recovery occurs by removing the costs associated with the provision of broadband Internet access service from the regulated rate base.</u>***

As discussed in Section III A. 1., above, the RBA recommended implementation of the Commission's proposed ICLS/HCLS rule regarding recovery of past expenses in conjunction with the proposed CAF for rate-of-return carriers to provide needed support

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[64] *See,* Section II B 2, *supra*, that further addresses how the proposals set forth herein equitably and efficiently distribute the current USF budget for rate-of-return carriers.

[65] *See,* Section II C 2, supra, that further addresses how the proposals set forth herein can be implemented within the current budget.

for new capital and operating expenses provides separate and distinct mechanisms for the support of past and future expenses. This separation addresses the Commission's concern regarding double recovery that may occur if the support mechanisms are not separated.

Under the proposals set forth herein, double recovery cannot occur. Existing investment is recovered only from the ICLS and HCLS. Irrespective of whether the consumer chooses to utilize an existing connection for broadband only service, the investment associated with the existing connection will not qualify for new CAF support. The carrier will, instead, continue to receive the support anticipated for the existing investment from ICLS and HCLS. Similarly, new investment would not be recovered after the date certain set by the Commission from ICLS and HCLS; the new investment would only qualify for potential CAF support.

B. The option to utilize ICLS and HCLS to recover past expenses in combination with the implementation of the recommended design for a new rate-of-return carrier CAF is consistent with the core principles for reform adopted by the Commission in 2011.

In its *NPRM* released on February 9, 2011, the Commission articulated four core principles that would guide its USF reform efforts. The proposals set forth herein are consistent with each of these principles:

1. Modernize USF for broadband
2. Fiscal Responsibility
3. Accountability
4. Market-driven policies

***<u>Modernize USF for Broadband</u>*:**

The proposals result in winding down the old USF mechanisms that focused on two-way voice services and transition to a new CAF support mechanism for rate-of-return carriers designed to target support to locations where it is needed to expand and maintain universal services and high-speed broadband connectivity.

Fiscal Responsibility:

The proposals ensure that the limited USF budget is utilized in a fiscally responsible manner by directing the available budget first to the recovery of existing investments. Support available for new investment and expenses required to expand and maintain universal service and broadband are directed on an equitable, proportionate basis to carriers from the new CAF mechanism for rate-of return carriers. As a result, the proposals constrain and eventually wind down the utilization of the old USF mechanisms and tie additional funding directly to the FCC's objective to expand and maintain the provision of broadband service.

Accountability:

The ICLS and HCLS funding remain subject to the Commission's audit processes and existing rules regarding recovery of just and reasonable expenses. Additional funding is provided subject to the additional accountability the FCC establishes.

Market-Driven Policies:

The proposed option to limit and wind down the utilization of the ICLS and HCLS mechanisms and transition to a rate-of-return carrier model-based CAF provides rate-of-return carriers with meaningful incentives to manage their business within the frozen interstate revenue requirement. Recognizing the reality of the limited USF budget for rate-of-return carriers, additional support is tied into the Commission's objective of targeting funding to the provision of broadband with accountability and fiscal responsibility as discussed above.

IV. CONCLUSION -The long-term USF objectives require immediate attention to long-term issues including reform of the contribution mechanism and budget sufficiency.

The RBA respectfully submits that the adoption of the recommendations set forth herein regarding the Commission's proposed ICLS/HCLS rule and the development of a CAF for rate-of-return carriers will provide an option that will facilitate the achievement of the Commission's universal service objectives. The RBA, however, urges the Commission to recognize that the achievement of long-term universal service objectives requires additional and immediate attention to two critical issues: reform of the universal service contribution mechanism and the sufficiency of the budget.[66]

Today's evolution of the broadband network results in both growing consumer needs for service and changes in the consumer's utilization of the network. As a result, there is a clear and imperative need to ensure that universal service mechanisms are structured in a manner that provides the required statutory result mandated by Section 254 of the Communications Act: a specific, sustainable and predictable mechanism that provides funding sufficient to ensure the provision of universal service to rural consumers at service levels and rates reasonably comparable to those available to urban consumers.

[66] The comments of other parties raise similar concerns. *See, e.g.*, NRIC at pp. ; Comments of the Rural Associations, p. 14; and Comments of the Concerned Rural LECs at pp. 11-12.

While the proposals under consideration in the *FNPRM* and the recommendations set forth herein address specificity and predictability, additional consideration must be afforded to sufficiency and sustainability in order to achieve and maintain universal service objectives.

As the RBA observed in comments filed on April 18, 2011, in response to the *NPRM*: "It is vital to rural America that the Commission expediently resolves the long-pending issues raised in this proceeding, and it is essential to rural economic development, job creation, and job preservation that the Commission gets it right." While the RBA recognizes the critical need to act on near-term and longer-term USF rule reforms for rate-of-return carriers within the currently established budget, as discussed herein, RBA continues to submit that it is essential to move the "horse" out in front of the "cart."

The RBA has respectfully noted previously in this proceeding that the reform of the universal service rules (the "cart") has been placed ahead of the determination of what ultimately drives universals service: a fact-based determination of the support levels required to establish and maintain universal service (the "horse").

Section 254 of the Communications Act does not suggest that the Commission fulfill its universal service obligations under the Act by first establishing a "budget." The Act clearly anticipates that the FCC, with the recommendation of the Joint Board, will first determine what constitutes universal service and reasonably comparable rates for reasonably comparable universal services. With that fundamental information as a basis, the Act provides that the Commission should establish "specific, sufficient and predictable" funding mechanisms to advance and preserve universal service. On this basis, the Commission can sustain a determination of the funding level that will be sufficient and establish equitable mechanisms to obtain contributions to the USF.

The Universal Service reform effort thus far has, perhaps as the result of political reality or perceived reality, turned this process around. Without basis in statute or policy, the process has proceeded with an assumed budget level for each USF program. Moreover, USF rule change efforts have gone forward without consideration of contribution mechanism reform. The RBA is appreciative that the FCC has recently initiated an inquiry into the contribution mechanism with a referral to the Joint Board, but urges action on contribution reform within a reasonably short timeframe.[67]

The RBA does not suggest that USF administration and policy should proceed in the absence of a budget. The RBA, however, does submit that universal service policy objectives cannot be fulfilled without first evaluating and quantifying universal support requirements.

When challenged by the reality of operating universal service support mechanisms within an established budget that is insufficient to do the job, rate-of-return carriers serving rural high-cost-to-serve communities react with the same logic, emotion, and concern that would be expected of anyone genuinely interested in fulfilling the universal service mandates of the Communications Act fairly and efficiently. Rate-of-return carriers will explain the shortcomings of the existing budget, and set forth the facts that support the capital and operating expenses that demonstrate the real world requirement for additional support to bring fully the benefits of universal service to the consumers they serve. Rate-

[67] The need for contribution mechanism reform in order to ensure sustainable universal service programs is further underscored and discussed by NRIC at pp. 6. The RBA notes that the current contribution mechanisms do not reflect the usage or value of nationwide interconnected voice and broadband networks. The contribution mechanism largely assesses interstate long distance usage; the increasing assessment factor reflects the shrinking base of interstate long distance revenues and ignores the increasing broadband usage of interconnected networks. Ironically, the current contribution mechanisms incorporate the additional absurdity that broadband consumers of rate-of-return carriers are the only consumer group whose broadband connectivity is assessed for USF contribution purposes.

of-return carriers, however, are not alone in identifying the need to establish a budget that is sufficient.

For example, the National Broadband Plan recognized the value of additional funding and stated, "Additional funding would allow the country to achieve the National Broadband Availability Target faster and ease the glide path for implementing other reforms in this plan by removing regulatory uncertainty over USF and ICC revenue streams potentially available for further broadband deployment."[68]

Even if the overall $ 4.5 billion USF budget were sufficient, there is no factual basis that demonstrates whether the portion of the budget dedicated to territories served by rate-of-return carriers is sufficient. As Commissioner Pai noted, "Over two paragraphs, the Order reiterates the determination in the Universal Service Transformation Order that the overall budget for the Connect America Fund is sufficient and that market trends support this conclusion. See Order at para. 123–24. For what it's worth, I agree that the $4.5 billion budget is sufficient (indeed, the Fund is running a surplus today). But that determination says nothing about the sufficiency of the legacy support offered to each individual carrier to meet the new broadband common-carriage obligations. On that question, the Order has no response."[69]

The RBA appreciates that the Commission previously recognized the need to review and modify the USF budget when it issued the *ICC/USF Transformation Order*, stating:

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[68] *See* Federal Communications Commission, *Connecting America: The National Broadband Plan* (rel. Mar. 16, 2010), at 152. (National Broadband Plan).

[69] **Report and Order, Declaratory Ruling, Order, Memorandum Opinion and Order, Seventh order on Reconsideration, and Further Notice of Proposed Rulemaking,** WC Docket No. 10-90 et al., released June 10, 2014 at fn. 1119.

"We anticipate that we may revisit and adjust accordingly the appropriate size of each of these programs by the end of the six-year period we budget for today, based on market developments, efficiencies realized, and further evaluation of the effect of these programs in achieving our goals."[70]

The RBA respectfully submits that as the Commission approaches the third anniversary of the six-year period, it is time to conduct the review and to make needed adjustments in order to better ensure that universal service objectives are achieved.

The undertaking of this endeavor will assist the Commission in its efforts to expand and maintain universal service. The results will better inform consumers, carriers and decision-makers with respect to: what support levels are required to fulfill the Congressional universal service mandates; what limitations on universal service deployment may result under proposed annual budgets; and how to evaluate the impact of the budget changes on the timeline for delivering expanded universal service and broadband capacity to consumers residing in high cost areas.

The RBA also appreciates the efforts of the Commission and Bureau reflected by the Seventh Report and Order and the *FNPRM*. The Commission has the opportunity to further serve the public interest and advance universal service objectives by its consideration of reform that recognizes the coexisting needs of rate-of-return carriers for universal service funding to support existing investments, ongoing operating expenses and new investment to expand and maintain universal services and high-speed broadband connectivity. For the reasons set forth above, the RBA urges the Commission to provide rate-of-return carriers

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[70] *ICC/USF Transformation Order* at para. 123.

with the option, as recommended herein, to utilize ICLS and HCLS to recover past expenses and transition to a new CAF for rate-of-return carriers that appropriately modifies the model established for price cap carriers and incorporates a "fail-safe" mechanism to ensure that support is sufficient to provide universal service to rural consumers in accordance with both the rules and regulations of the Commission and the universal service mandate established by Congress.

Respectfully submitted,

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