IN THE UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

NO. 11-9900

IN RE: FCC 11-161

ON PETITIONS FOR REVIEW OF AN ORDER OF THE FEDERAL COMMUNICATIONS COMMISSION

UNCITED JOINT UNIVERSAL SERVICE FUND REPLY BRIEF (DEFERRED APPENDIX APPEAL)

[Counsel for Petitioners Listed on Following Pages]

June 5, 2013

Adak Eagle Enterprises LLC, Adams Telephone Cooperative, Alenco Communications, Inc., Arlington Telephone Company, Bay Springs Telephone Company, Inc., Big Bend Telephone Company, Inc., The Blair Telephone Company, Blountsville Telephone LLC, Blue Valley Telecommunications, Inc., Bluffton Telephone Company, Inc., BPM, Inc., Brantley Telephone Company, Inc., Brazoria Telephone Company, Brindlee Mountain Telephone LLC, Bruce Telephone Company, Bugs Island Telephone Cooperative, Cameron Telephone Company, LLC, Chariton Valley Telephone Corporation, Chequamegon Communications Cooperative, Inc., Chickamauga Telephone Corporation, Chickasaw Telephone Company, Chippewa County Telephone Company, Clear Lake Independent Telephone Company, Comsouth Telecommunications, Inc., Copper Valley Telephone Cooperative, Cordova Telephone Cooperative, Crockett Telephone Company, Inc., Darien Telephone Company, Deerfield Farmers' Telephone Company, Delta Telephone Company, Inc., East Ascension Telephone Company, LLC, Eastern Nebraska Telephone Company, Eastex Telephone Coop., Inc., Egyptian Telephone Cooperative Association, Elizabeth Telephone Company, LLC, Ellijay Telephone Company, Farmers Telephone Cooperative, Inc., Flatrock Telephone Coop., Inc., Franklin Telephone Company, Inc., Fulton Telephone Company, Inc., Glenwood Telephone Company, Granby Telephone LLC, Hart Telephone Company, Hiawatha Telephone Company, Holway Telephone Company, Home Telephone Company (St. Jacob, Ill.), Home Telephone Company (Moncks Corner, SC), Hopper Telecommunications Company, Inc., Horry Telephone Cooperative, Inc., Interior Telephone Company, Kaplan Telephone Company, Inc., KLM Telephone Company, City Of Ketchikan, Alaska, Lackawaxen Telecommunications Services, Inc., Lafourche Telephone Company, LLC, La Harpe Telephone Company, Inc., Lakeside Telephone Company, Lincolnville Telephone Company, Loretto Telephone Company, Inc., Madison Telephone Company, Matanuska Telephone Association, Inc., McDonough Telephone Coop., Inc., MGW Telephone Company, Inc., Mid Century Telephone Coop., Inc., Midway Telephone Company, Mid-Maine Telecom LLC, Mound Bayou Telephone & Communications, Inc., Moundville Telephone Company, Inc., Mukluk Telephone Company, Inc., National Telephone of Alabama, Inc., Ontonagon County Telephone Company, Otelco Mid-Missouri LLC, Otelco Telephone LLC, Panhandle Telephone Cooperative, Inc., Pembroke Telephone Company, Inc., People's Telephone Company, Peoples Telephone Company, Piedmont Rural Telephone Cooperative, Inc., Pine Belt Telephone Company, Pine Tree Telephone LLC, Pioneer Telephone Cooperative, Inc., Poka Lambro Telephone Cooperative, Inc., Public Service Telephone Company, Ringgold Telephone Company, Roanoke Telephone Company, Inc., Rock County Telephone Company, Saco River Telephone LLC, Sandhill Telephone Cooperative, Inc., Shoreham Telephone LLC, *The Siskiyou Telephone Company, Sledge Telephone Company, South Canaan Telephone Company, South Central Telephone Association, Star Telephone Company, Inc., Stayton Cooperative Telephone Company, The North-Eastern Pennsylvania Telephone Company, Tidewater Telecom, Inc., Tohono O'Odham Utility Authority, SD, Unitel, Inc., War Telephone LLC, West Carolina Rural Telephone Cooperative, Inc., West Tennessee Telephone Company, Inc., West Wisconsin Telcom Cooperative, Inc., Wiggins Telephone Association, Winnebago Cooperative Telecom Association, and Yukon Telephone Co., Inc. (Rural Telephone Service Company et al.)*

By Their Counsel	
David Cosson 2154 Wisconsin Avenue, NW Washington, DC 20007 Tel: 202-333-5275 dcosson@klctele.com	**H. Russell Frisby, Jr.** **Harvey L. Reiter** Stinson Morrison Hecker LLP 1775 Pennsylvania Avenue, NW Suite 800 Washington, DC 20006 Tel: 202-785-9100 rfrisby@stinson.com dlane@stinson.com hreiter@stinson.com * Adak Eagle Enterprises LLC, *et al*. join in Sections I – VIII of this brief.

Allband Communications Cooperative By Its Counsel **Don L. Keskey** Public Law Resource Center PLLC 139 W. Lake Lansing Rd, Suite 210 East Lansing, MI 48823 Tel: 517-999-7572 donkeskey@publiclawresourcecenter.com	*Arizona Corporation Commission* By Its Counsel **Maureen A. Scott** **Wesley Van Cleve** **Janet F. Wagner** Arizona Corporation Commission Legal Division 1200 West Washington Phoenix, AZ 85007 Tel: 602-542-3402 mscott@azcc.gov wvancleve@azcc.gov jwagner@azcc.gov
Cellular South, Inc. *d/b/a C Spire Wireless* By Its Counsel **Michael B.Wallace** **Rebecca Hawkins** 401 E. Capitol Street Heritage Bldg., Suite 600 Jackson, MS 39201 Tel: 601-968-5500 mbw@wisecarter.com rwh@wisecarter.com	*Choctaw Telephone Company* By Its Counsel **Benjamin H. Dickens, Jr.** **Mary J. Sisak** Blooston, Mordkofsky, Dickens, Duffy & Prendergast, LLP 2120 L Street, NW, Suite 300 Washington, DC 20037-0000 Tel: 202-659-0830 bhd@bloostonlaw.com mjs@bloostonlaw.com **Craig S. Johnson** Johnson & Sporleder, LLP 304 E High St. Suite 200 P.O. Box 1670 Jefferson City, MO 65102 Tel: 573-659-8734 cj@cjaslaw.com

Direct Communications Cedar Valley, LLC, Totah Communications, Inc., H & B Communications, Inc., The Moundridge Telephone Company of Moundridge, Pioneer Telephone Association, Inc., Twin Valley Telephone, Inc., and Pine Telephone Company By Their Counsel **David R. Irvine** 747 East South Temple, Suite 130 Salt Lake City, UT 84102 Tel: 801-579-0802 drirvine@aol.com **Alan Lange Smith** 1169 East 4020 South Salt Lake City, UT 84124 Tel: 801-262-0555 alanakaed@aol.com	*Gila River Indian Community and Gila River Telecommunications, Inc.** By Their Counsel **Michael C. Small** Akin Gump Strauss Hauer & Feld LLP 2029 Century Park E. Suite 2400 Los Angeles, CA 90067 Telephone: 310-229-1000 Facsimile: 310-229-1002 msmall@akingump.com **Sean T. Conway** Akin Gump Strauss Hauer & Feld LLP 1333 New Hampshire Avenue, N.W. Washington, DC 20036 Telephone: 202-887-4000 Facsimile: 202-887-4288 sconway@akingump.com * Gila River Indian Community and Gila River Telecommunications, Inc. join in Sections III, V, VI, VII.B, VIII, and IX of this brief.

National Association of Regulatory Utility Commissioners By Its Counsel **James Bradford Ramsay** National Association of Regulatory Utility Commissioners 1101 Vermont Avenue, NW Suite 200 Washington, DC 20005 Tel: 202-898-2200 jramsay@naruc.org	*National Association of State Utility Consumer Advocates** By Its Counsel **David Bergmann** 3293 Noreen Drive Columbus, OH 43221-4586 Tel: 614-771-5979 david.c.bergmann@gmail.com **Paula Marie Carmody** Maryland Office of People's Counsel 6 St. Paul Street, Suite 2102 Baltimore, MD 21202 Tel: 410-767-8150 paulac@opc.state.md.us **Christopher J. White** New Jersey Division of Rate Counsel 140 E. Front Street, 4th Floor Trenton, NJ 08625 Tel: 609-633-9141 cwhite@rpa.state.nj.us *****NASUCA joins in Sections I.A., II.A., II.B., IV, VII.A., VIII., and IX of this brief.

*National Telecommunications Cooperative Association and Consolidated Communications Holdings, Inc.** By Their Counsel **Russell Blau** **Tamar Finn** Bingham McCutchen LLP 2020 K Street, NW Washington, DC 20006 Tel: 202-373-6000 russell.blau@bingham.com tamar.finn@bingham.com *NTCA and Consolidated Communications join in Sections I – VIII of this brief.	*Pennsylvania Public Utility Commission* By Its Counsel **Bohdan R. Pankiw** **Kathryn G. Sophy** **Joseph K.Witmer** **Shaun A. Sparks** Pennsylvania Public Utility Commission 400 North Street, 3rd Floor Harrisburg, PA 17120 Tel: 717-783-3190 bpankiw@state.pa.us ksophy@pa.gov joswitmer@pa.gov shsparks@pa.gov
*Rural Independent Competitive Alliance, Rural Telephone Service Company, Inc.** By Their Counsel **David Cosson** 2154 Wisconsin Avenue, NW Washington, DC 20007 Tel: 202-333-5275 dcosson@klctele.com **H. Russell Frisby, Jr.** **Dennis Lane** **Harvey L. Reiter** Stinson Morrison Hecker LLP 1775 Pennsylvania Avenue, NW #800 Washington, DC 20006 Tel: 202-785-9100 rfrisby@stinson.com dlane@stinson.com hreiter@stinson.com *RICA and Rural Telephone join in Sections I – VIII of this brief.	*Vermont Public Service Board* By Its Counsel **Bridget Asay** Office of the Attorney General for the State of Vermont 109 State Street Montpelier, VT 05609-1001 Tel: 802-828-3181 basay@atg.state.vt.us

TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES **Page(s)**

AGENCY DECISIONS

STATUTES

REGULATIONS

I. THE BROADBAND INTERNET ACCESS CONDITION UNLAWFULLY COERCES ETCS TO USE USF FOR UNSUPPORTED SERVICES.

A. The Commission's Contradictory Claims That It Is Not Requiring USF Recipients To Provide Broadband Internet Access And That The Condition Is Voluntary Are Both Unsupported.

In return for USF support, ETCs must offer broadband internet access, an "information service," on reasonable request. *Order*, ¶26. Because §254 authorizes USF support only for telecommunications services, and because information services are not telecommunications services, Petitioners have challenged this condition as unlawful. USF Br., 12-17. [1] Respondents concede that broadband internet access is an information service and therefore cannot be a supported service under §254, FCC Br., 20, but offer a threefold response.

Their first response is to deny the condition's existence altogether. They claim the *Order* "merely conditioned the receipt of support on a carrier's deployment of a broadband-capable network" and that Petitioners "fail to show" that the FCC has "authorized federal universal service support for broadband Internet access service itself." FCC Br., 20. But their brief directly contradicts itself, conceding that the *Order*, in fact, "required USF recipients to provide broadband Internet access." *Id.*, 18. *See* also, *Order*, ¶¶26, 86.

[1] Petitioners' Uncited Joint Universal Service Fund Principal Brief is cited herein as "USF Br.", and the Federal Respondents' Uncited Response to the Joint Universal Service Fund Principal Brief as "FCC Br."

Respondents also assert that the broadband internet access condition is an acceptable means of ensuring that those benefiting "from public investment in their networks" accept "clearly defined obligations associated with the use of such funding." FCC Br., 21. Citing *U.S.* v. *Am. Libraries Ass'n*, 539 U.S. 194, 211-13 (2003), *Tex. Office of Pub. Util. Counsel v. FCC*, 183 F.3d 393, 444 (5th Cir. 1999) and *Qwest Commc'ns Int'l., Inc. v. FCC*, 398 F.3d 1222, 1238 (10th Cir. 2005) (*Qwest II*), they maintain that the courts have denied "similar challenges to conditions on federal subsidies." *Id*. None of these cases, however, involved a condition requiring recipients to use USF for unsupported services.

The first two cases involve conditions on the use of funds to support services to schools, hospitals and libraries – the sole express §254 exception to the requirement that USF go only to telecommunication services. *See* USF Brief, 15-16. And the *Qwest II* case involves a condition – a state finding of rate comparability – consistent with, rather than contradictory to, the statutory language.[2] Likewise, the *Am. Libraries* condition *barred* funds intended for education from being diverted to pornography; here, the FCC *mandates* that funds intended for telecommunications services be diverted to information services.

[2] 47 U.S.C. § 254(b) (consumers in "rural, insular, and high cost areas" should have access to services that are "reasonably comparable" to those provided in urban areas at "reasonably comparable" rates)

Implicitly acknowledging some limitation on the FCC's conditioning authority, Respondents' last argument is that "providers voluntarily assume the conditions in the first instance," so the condition "does not amount to 'regulation' of any sort." FCC Br., 23. But the condition is not voluntary *and* it requires recipients to use USF support for unlawful purposes.

An administrative agency may have express authority to impose conditions appropriate to "*promote* the policies of the [a]ct" it administers, but the conditions it adopts "may not *contravene* the Act." *Richmond Power & Light Co. v. FERC*, 574 F.2d 610, 620 (D.C. Cir. 1978) (emphasis added). As Respondents implicitly concede, the Commission cannot use its conditioning power to compel action it has no independent authority to require. "What the Commission is prohibited from doing directly it may not achieve by indirection." *Id.*; *see also, National Fuel Gas Supply Corp. v. FERC*, 909 F.2d 1519, 1522 (D.C. Cir. 1990). Analogously, Congress may provide financial inducements for states or individuals to act in lawful ways that Congress could not compel directly, *South Dakota v. Dole*, 483 U.S. 203, 206 (1987), but Congress cannot cross the line "distinguishing encouragement from coercion." *New York v. U.S.* 505 U.S. 144, 175 (1992). The Commission's constraints are no less stringent.

Even a voluntary condition must be lawful. Because broadband internet access is concededly not a supported service under §254, FCC Br., 20, requiring USF recipients to provide it forces them to use USF unlawfully.

The condition, moreover, is not truly voluntary. The Act requires that support be provided to make service affordable for "the most expensive to serve, most rural, and insular communities," *Order*, ¶2, and requires carriers to continue providing those services. Under the *Order*, providers declining to provide broadband internet access lose not only USF funds to support broadband investment, they lose *all* USF support. But both §214(e)(1) and State law compel these carriers to continue providing essential telecommunications service whether they accept support or not. A condition that would deprive them and the communities they serve of USF support they have relied on "[f]or decades," *Order*, ¶2, is not voluntary.

In this respect, the Commission's broadband access condition is like the Medicaid eligibility condition struck down in *National Federation of Independent Business, et al., v. Sebelius*, 567 U.S. ___, 132 S. Ct. 2566 (2012). There, states long dependent on federal funds to support their Medicaid programs were required under the Affordable Care Act either to expand their Medicaid programs or lose all Medicaid support. *Id.*, Slip. Op. at 10. While the government argued that accepting Medicaid dollars was voluntary, the Court concluded that the states' longstanding reliance on existing Medicaid support made it impossible to decline the funding. *Id*. at 51. As with the Medicaid eligibility condition, "the financial 'inducement' [the FCC] has chosen is much more than a 'relatively mild encouragement'— it is a gun to the head." *Id*. "[W]hen a condemned man is given the choice between the noose and the firing squad, we do not ordinarily say that he has 'voluntarily' chosen to be hanged." *Associated Gas Distributors v. FERC*, 824 F.2d. 981, 1024 (D.C. Cir. 1987). The decision to decline USF support would be no less fatal to rural carriers and no more voluntary.

B. Respondents' Claim that the Broadband Internet Service Obligation Placed On ETCs is Not Common Carriage Is Neither Entitled To Deference Nor Reasonable.

Respondents concede that requiring ETCs to offer information service as common carriage service would be unlawful, but maintain that it *is* lawful to impose "some" conditions applicable to common carriers on non-common carriers without thereby regulating them as common carriers. FCC Br., 22-23. The latter proposition, though unremarkable, is inconsistent with the *Order*, which indeed attaches common carriage obligations to non-telecommunications services.

Respondents characterize the broadband condition as "modest:" "it simply requires" USF applicants "to offer broadband service that meets certain basic performance requirements and to report regularly on associated performance measures." *Id*., 23 (citing *Order*, ¶86). But the *Order*'s actual requirements go much farther: "[All] ETCs must make this broadband service available at rates that are reasonably comparable to the offerings of comparable broadband services in urban areas," *Order*, ¶86, "upon their customers' reasonable request." *Id.*, ¶26.

The FCC lacks authority either to impose common carriage obligations on entities that are not common carriers, *FCC v. Midwest Video Corp. (Midwest Video II),* 440 U.S. 689, 700-01(1979), or to require common carriers for a particular service to assume common carriage obligations for other services. 47 U.S.C. §153(51).

To be sure, the D.C. Circuit has held that "common carriage" is an ambiguous term and that the Commission's definition will be entitled to deference. *U.S. Telecom Association v. FCC,* 295 F.3d 1326, 1331-32 (D.C. Cir. 2002). But the FCC's discretion to determine whether its requirements impose common carriage is limited to the "gray area" – "the space between *per se* common carriage and *per se* private carriage." *Cellco Partnership v. FCC*, 700 F.3d 534, 547 (D.C. Cir. 2012). And what distinguishes *per se* common carriage is this: "If a carrier is forced to offer service indiscriminately and on general terms, then that carrier is relegated to common carrier status." *Id*. "The primary *sine qua non* of common carrier status is a quasi-public character, which arises out of the undertaking 'to carry for all people indifferently...'" *Id*. at 546 (quoting *Nat'l Ass'n of Regulatory Utility Commissioners v. FCC*, 533 F.2d 601, 608 (D.C. Cir. 1976). A private carrier for a "particular service," by contrast, "chooses its clients on an individual basis and determines in each particular case 'whether and on what terms to serve' and there is no specific regulatory compulsion to serve all indifferently." *Southwestern Bell Telephone Co. v. FCC*, 19 F.3d 1475, 1481 (D.C. Cir. 1994).

The *Order* requires that broadband services be offered to all upon reasonable requests, at prices meeting the FCC's standards, and nowhere suggests that ETCs may negotiate individualized end user arrangements or otherwise treat customers differently from one another. This is the essence of a common carriage requirement. The FCC itself acknowledges that "[t]he broadband deployment obligation we adopt is similar to the [common carrier] voice deployment obligations many of these carriers are subject to today." *Order*, ¶206. Respondents' contrary assertion on brief should be rejected.

C. The FCC Cannot Use Its Conditioning Authority to Impose Common Carrier Obligations on Information Service Providers.

Respondents' additional argument (FCC Br., 22-23) that the FCC has power to impose funding conditions "commensurate with the requirements imposed on common carriers," relies on this court's decision in *WWC Holdings v. Sopkin*, 488 F.3d 1262, 1274 (10th Cir. 2009). But the issue in *WWC Holdings* was not whether states could impose common carrier regulations on non-common carriers: "[W]e do not pass on the questions of whether the nature and extent of the conditions at issue here are beyond the bounds of a state's Section 214(e) authority, or whether they impermissibly burden the federal universal service program under Section 254(f)." *Id*. at 1276.

The court's observation, moreover, that the wireless carrier in that case "retains the ability to opt out of [the conditions] entirely by declining any federal universal service subsidies" (*Id*. at 1274) does not and cannot establish that the broadband condition in *this* case is voluntary. In *Sopkin*, the wireless carrier had already decided that it needed no state subsidies, *id*. at 1268.

II. THE FCC'S BROADBAND FACILITIES CONDITION IS UNLAWFUL.

A. The FCC Conflates Permissible *Inducements* to Deploy Broadband-Capable Facilities With Its *Requirement* That USF Recipients Deploy Broadband Facilities.

Respondents acknowledge that the FCC's §706-based "no barriers" policy "*permitted* (but did not require) recipients of federal high-cost universal service support to invest in 'dual-use' facilities that provide voice as well as broadband Internet access services" and that the *Order* "go[es] beyond the 'no barriers' policy" to "*require* carriers receiving federal universal service support to invest in modern broadband-capable networks." FCC Br., 12-13 (emphasis added). Citing this Court's decision in *Qwest Corp. v. FCC*, 258 F.3d 1191, 1200, 1204 (10th Cir. 2001) (*Qwest I*), Respondents claim that the agency's "mandatory duty" under §254(e) to "create some inducement" to advance broadband gives it this power. *Id*.

Respondents conflate the FCC's power (and duty) to *induce* broadband deployment by telecommunications carriers with the authority to *compel* it. An inducement is an incentive. There is, by definition, no need for an inducement to act where a party can be required to do so.

Respondents argue that "nothing in section 254 … requires [the agency] simply to provide federal funds to carriers and hope that they will use such support to deploy broadband facilities." *Id.*, quoting *Order* ¶65. This is true, but irrelevant. There are many ways to induce broadband investment without mandating it, with the Commission's "no barriers" policy being one. *Federal-State Joint Board on Universal Service*, 16 FCC Rcd 11244, 11322, ¶¶200-01 (2001). Its classification of broadband internet access as an information, not a telecommunications service, was likewise aimed to "encourage the ubiquitous availability of broadband" by creating a "minimal regulatory environment" for broadband services. *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, *Notice of Proposed Rulemaking*, 17 F.C.C.R. 3019, ¶¶3, 5 (2002). And it has "refused to classify" VoIP at all for much the same reason.[3] But the FCC cannot treat the perceived shortcomings of these policies in inducing broadband deployment as an excuse to *mandate* the use of USF funds for that purpose and then call its actions a mere "inducement."

---

[3] *Nuvio Corp. v. FCC*, 473 F.3d 302, 304, 308 (D.C. Cir. 2006).

B. The Argument That Petitioners' Interpretation of §254 Would Render The "No Barriers" Policy Unlawful is a Strawman that Misstates Petitioners' Position.

Respondents erroneously attribute to Petitioners the contention that under §254, USF "may support facilities only to the extent that they are used to provide telecommunications services." FCC Br., 17. This interpretation, they say, implies that "allowing ETCs to expend universal service subsidies to deploy facilities used to provide broadband Internet access, even on a permissive basis [its existing "no barriers" policy], would have violated the Act." *Id*. Petitioners' position, however, is not that USF-supported facilities may *only* be used for telecommunications services, but that under §254(c)(1), USF-funded facilities built for dual use must be used, at least in part, for telecommunications services.

The FCC itself says that "facilities" eligible for USF support under Section 254 are those "physical components of the telecommunications network *that are used* in the transmission or routing of *services that are designated for support*." *Order*, ¶64 n. 69. (emphasis added). The problem is not that USF recipients may not use USF funds for facilities *dually* capable of providing supported and unsupported services. They may. USF Br., 22. Instead, the problem is that the FCC's interpretation of §254 would allow USF to fund broadband-capable facilities capable *solely* of providing VoIP, an as-yet unclassified service. *Id*., 17-

18. Permitting the installation of pet doors so that humans and animals might live together would not support a mandate that all homes include doghouses.

III. RESPONDENTS CONCEDE THAT NON-TELECOMMUNICATIONS CARRIERS CANNOT BE ELIGIBLE TO RECEIVE USF SUPPORT.

Petitioners argued that by adding "voice telephony service" to the list of supported services under section 254(c)(1), without limiting the definition of that service to "telecommunications services," the *Order* violates §254(c)(1). USF Br. 17-18. Respondents denounce this argument as "wrong," FCC Br. 24, but then concede virtually all its premises. They agree that "only 'eligible telecommunications carriers' are eligible for subsidies under section 254," and that an ETC must be "a 'common carrier'" that offers supported services. FCC Br. 26, *citing* 47 U.S.C. §214(e)(1)(A). They also agree that an entity can be designated as an ETC under the statute only if it "complies with appropriate federal and state requirements" applicable to telecommunications carriers under Title II of the Act. *Id.*, *quoting IP-Enabled Services*, 20 FCC Rcd 10245, 10268 (2005) (subsequent history omitted).

This concession was not apparent on the face of the *Order*, as the FCC specifically included VoIP in the definition of "voice telephony service" without classifying VoIP as a telecommunications service. *Order*, ¶63; FCC Br. 26. However, based on Respondents' acknowledgement that only an entity providing telecommunications services as a Title II common carrier can become an ETC, Petitioners no longer believe there is any issue of the FCC authorizing USF support for ineligible carriers or unsupported VoIP services for the Court presently to resolve.[4]

IV. BY DISCLAIMING RELIANCE ON SECTION 706 AS SUPPORT FOR ITS REQUIREMENT THAT USF RECIPIENTS OFFER BROADBAND SERVICES, THE FCC HAS RENDERED ITS CLAIM OF SECTION 706 AUTHORITY TO IMPOSE THE CONDITION IRRELEVANT.

Respondents assert on brief – indeed on the same page of their brief -- both that the Commission "has not authorized support for VoIP service under section 706" (p.27 n. 6) *and* that it "*has* authority under section 706" to require USF recipients "to deploy broadband networks *and* services." *Id*., Section D (heading). (emphasis added). Petitioners' opening brief explained why §706 does not give the FCC power to impose its broadband condition. But because the agency has disclaimed reliance on §706 as a basis to sustain its broadband service condition, this Court need not reach the question whether §706 gives the FCC power, independent of §254, to require that USF recipients offer customers VoIP or other broadband internet services.

[4] To be clear, Petitioners base this statement on the understanding that a claim by an entity seeking support that it qualifies as a Title II common carrier can be challenged in subsequent regulatory proceedings and, if necessary, on judicial review.

V. THE FCC'S REDUCTIONS OF RLEC SUPPORT VIOLATE STATUTORY CRITERIA AND ARE ARBITRARY AND CAPRICIOUS.

A. The FCC Failed To Perform A Meaningful Analysis Of Sufficiency Of Support.

The Communications Act directs the FCC to establish "specific, predictable, and sufficient" universal service support mechanisms. 47 U.S.C. §254(e). Responding to Petitioners' argument, USF Br. 30-33, that the *Order* arbitrarily focused exclusively on preventing allegedly excessive support, and failed to guard against inadequate support, Respondents maintain that the FCC found support would not be insufficient. FCC Br. 33-34. The passages cited (*Order*, ¶¶125, 285-92), however, are naked assertions that support would remain sufficient, lacking any rational or factual analysis. Even if reductions in USF support to RLECs were designed to eliminate "inefficiencies and wasteful spending," *Order,* ¶125, that does not establish whether the remaining support would be adequate for the future needs of rural communities, particularly because the support reductions do not require or follow from any finding of inefficiency or waste in particular cases.

Respondents also argue that the *Order*'s reforms were designed to minimize impacts on RLECs, and contain a waiver process. FCC Br. 34-35. Again, the fact that the FCC took steps to reduce some burdens does not necessarily mean support will be adequate to meet remaining burdens; nor does the fact that carriers may seek waivers in extreme situations (facing a "threat[] [to] their financial viability," *Order*, ¶539) imply support to carriers in less dire circumstances will be sufficient.

Respondents complain that Petitioners did not quantify the additional costs imposed on RLECs to comply with the new broadband condition. FCC Br. 36-37. Taken at face value, this argument concedes that the FCC did not know what it might cost to fulfill the condition (or otherwise fulfill the mandates of universal service), which undermines its position that it had a reasonable basis for expecting support to be sufficient. Yet the FCC found that "one of the most significant barriers to investment in broadband infrastructure is the lack of a business case for operating a broadband network in high-cost areas in the absence of programs that provide additional support." *Order*, ¶67. It at least knew the costs were enough to deter private investment, which contradicts counsel's *post hoc* rationalization that the "FCC had little reason to think that the additional cost (if any) would be substantial …." FCC Br. 36.

Nonetheless, Respondents argue, the FCC did estimate the impact of funding changes on RLECs by determining that "34 percent of rate-of-return carriers would see no change in universal service support *receipts*, and 12 percent would see an increase …." FCC Br. 36 (emphasis supplied). This is a *non sequitur*. The fact that "receipts" (for some) are unchanged, or even increased, says nothing about whether support will be sufficient to meet future costs (including the additional cost of satisfying the broadband condition), especially for consumers served by the majority (54%) of carriers who will experience reductions. *See* USF Br. 29-30.

Respondents ask the Court to defer to the FCC's "reasonable predictive judgment" that support will be sufficient. FCC Br. 33, 37. But where, as here, the agency's judgment about sufficiency has not in fact evaluated the specific costs of universal service, that judgment has "ignored a critical aspect of the problem" and is not entitled to deference. *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). Instead, its "opinion contains much talk but no demonstration of expertise." *Schurz Commc'ns, Inc. v. FCC*, 982 F.2d 1043, 1050 (7^{th} Cir. 1992).

B. Respondents' "Takings" Argument Is Misplaced.

Respondents maintain that Petitioners' have mounted a takings claim and that this claim is not ripe, because the FCC will consider waivers where RLECs can demonstrate confiscation. FCC Br. 38-39. This misstates Petitioners' argument. Petitioners contend the *Order* was arbitrary and inconsistent with the statutory requirement of "sufficient support" because it will not provide them a reasonable opportunity to recover prudently incurred costs, USF Br. 42-44, not that it violated the constitutional prohibition on takings, a separate argument raised by Allband (Add'tl USF Br., 33-34). The waiver provision is inadequate, first because the exceptions that justify a lawful waiver swallow the rule, and second because the FCC imposed conditions on the grant of waivers that would deprive carriers of prudent cost recovery. USF Br. 44-45. Respondents' brief never responds to the latter point, that the *Order* precludes waivers even in the many instances in which support is demonstrably inadequate for carriers to recover their prudently incurred costs, irrespective of whether consumers are at risk of losing voice services.

C. The FCC Acted Arbitrarily By Reducing Support Without Requiring Evidence Of Imprudent Or Inefficient Costs.

Respondents argue the FCC acted reasonably to "eliminate waste and inefficiency" in the high-cost support system, and that the Court should defer to its judgment regarding the necessity of these changes. FCC Br. 37-38, 39-40. Unquestionably, if the FCC identifies actual wasteful spending, it should correct it. But that is not what the *Order* did. Rather, the FCC reduced support to *all* carriers whose costs (in total, or in specific categories such as corporate overhead) exceeded arbitrary levels, without even considering whether a specific carrier's costs were prudent and justified in its particular circumstances.[5] Respondents reject Petitioners' argument that these cuts are "untethered to evidence" of inefficiency, USF Br. 32, as "demonstrably incorrect," claiming that the revised

[5] The FCC does permit a carrier to present evidence of the prudence of its expenditures in support of a petition for waiver, but the shortcomings with the FCC's reliance on its waiver process are discussed elsewhere in this brief.

support formulas "are based on carrier-specific analyses of costs and rates." FCC Br. 38. This statement is misleading. The support formulas compare a carrier's specific costs and rates to benchmark levels, but the benchmarks themselves are arbitrary (USF Br. 41-42) and there is no identified causal relationship between exceeding those levels and imprudent spending. Even though carriers' costs are inputs to the formulas, as Respondents assert, the formulas are still untethered to evidence of inefficiency.

D. The FCC's Regression-Based Benchmarks Violate The Statute's Predictability Standard.

Petitioners argued that the use of regression formulas to "benchmark" high-cost support renders support irrationally unpredictable. The regression rule limits some carriers' ability to provide supported services, not because the carrier is overspending, but because it is spending at a rate allegedly higher than other companies based upon opaque benchmarks. The FCC examined no facts to determine whether carriers facing reduced support actually had spent imprudently, or whether instead the support was needed to provide voice or broadband services.

The rule is unpredictable because the actual "regression" limitation is not itself published in the rules, and can be changed annually through a methodology announced in a public notice. The rule merely delegates authority to FCC staff "to finalize a methodology." *Order*, ¶226. This open-ended, changeable formulation is not a predictable rule, and thus cannot be a fair implementation of the statute's predictability factor, even if balanced against other statutory factors.

Although Respondents argue the FCC "imposed meaningful 'substantive limitation[s]'" on the Bureau's implementation of the rule, FCC Br. 44, they do not identify those substantive limitations. The directives to employ "statistical techniques," using a *non-binding* list of variables, and to publish results annually, are neither substantive, nor meaningful guidance to the Bureau. Respondents never address Petitioners' arguments that the text of the rule itself is hopelessly vague, can be changed at will without any further proceedings, and thus is not a "predictable" rule as required by §254(b). USF Br. 36-39.[6]

Respondents suggest the new rule is no more unpredictable than previous rules. FCC Br. 45. This is incorrect because the prior rule's published formula permitted a carrier at least to approximate its support, s*ee, e.g.*, 47 C.F.R. § 36.631, while the new rule does not permit even a rough estimate -- an argument that Respondents do not answer. USF Br. 37. Further, an agency cannot justify an arbitrary rule on the grounds that it is similar to a past practice that was itself arbitrary. At a minimum, the agency must engage in a reasonable quantification of

6 Although the substantive application of the regression analysis has changed significantly since adoption, the text of the rule has not been changed. *Connect America Fund*, WC Docket No. 10-90, et seq., DA 12-646 (Wir. Comp. Bur., rel. Apr. 25, 2012) ("Benchmark Order"), *application for rev. granted in part,* FCC 13-16 (rel. Feb. 27, 2013) ("Sixth R&O").

the results of its rules to demonstrate that its balancing of competing interests achieves the statutory purpose. *Qwest II*, 398 F.3d at 1237. Had the Commission undertaken such an examination, it would have confirmed that its new rules are significantly more unpredictable than prior rules, enough to violate the "predictability" requirement of §254(b).

Respondents wrongly claim that Petitioners are seeking guaranteed outcomes rather than predictable rules. FCC Br. 44-45.[7] Petitioners never argued in this proceeding that the precise level of support must be certain under the statute. Rather, Petitioners seek a clear rule that enables companies to evaluate whether support will be sufficient in general to support planned network investments, which is a rational business pre-requisite and a stated FCC policy. *Order*, ¶858. The current rule does not even come close to providing a reasonable basis for investment decisions, thus violating §254's predictability mandate.

By delegating unfettered authority to the Bureau to adjust support amounts, the Commission also violated its own rules prohibiting rulemaking by subordinate agency entities.[8] While Respondents are correct that §155(c) of the Act *permits*

---

[7] Respondents' Brief (at 45) presents a quotation from the Fifth Circuit's *Alenco* decision concerning "predictable market outcomes" in a confusing manner that suggests it could be quoting from Petitioners' Brief, which contains no such language.

[8] Respondents argue that this issue was not raised below and is therefore barred by §405(a). FCC Br. 42. The illegality of this rule's delegation was in fact

delegation "by published rule or order," FCC Br. 43-44, the FCC chose to deny the Bureau delegated rulemaking authority in 47 C.F.R. §0.291(e). Having done so, it is bound by its choice. *FCC v. Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009); *City of Colorado Springs v. Solis*, 589 F.3d 1121, 1132 (10th Cir. 2009).

E. The Retroactive Effects of the Rules are Unreasonable.

Respondents erroneously attribute to Petitioners the argument that the regression benchmarking and SNA rules "preclude[] [carriers] from recovering expenses they incurred based on the 'reasonable expectation[]' that they would receive universal service support." FCC Br. 47, quoting USF Br. 46. That is not, however, what Petitioners argued. Respondents truncated the quote from Petitioners' brief. As the full quote shows, Petitioners' actual claim was that the rule "retroactively precludes carriers from recovering reasonable and prudent capital and operating expenses they previously made *to comply with* the ETC provisions of Section 214(e) of the Act, Rural Utilities Service (RUS) loan

---

raised in Petition For Reconsideration and Clarification of the National Exchange Carrier Association, Inc., et al., 10 (filed Dec. 29, 2011) (*citing* Letter from Michael R. Romano, NTCA, to Marlene H. Dortch, FCC, WC Docket No. 10-90, *et al*., 2 (filed Oct. 21, 2011)). The argument need not have been raised by petitioners themselves to avoid the §405(a) bar. *Amer. Elec. Power Serv. Corp. v. FCC*, 708 F.3d 183, 190 (D.C. Cir. 2013). The agency had the "opportunity" to respond to this issue, which is all that §405(a) requires. *See, e.g., AT&T v. FCC*, 974 F.2d 1351, 1354 (D.C. Cir. 1992).

covenants and/or state COLR requirements." USF Br. 46 (emphasis added). The claim is not merely about upset expectations, but denial of recovery of costs carriers were *obligated* to incur. The FCC's contention that the rules are not retroactive "merely because they upset expectations based on prior law," FCC Br. 47, fails to address that fundamental point.

Respondents' answer to the retroactivity argument is, in essence, that carriers were on notice that the high-cost support rules might change, and were not entitled to make expenditures in reliance on receiving future reimbursement from the fund. FCC Br. 50. As regulated common carriers under Title II of the Act and under comparable State laws, however, RLECs lack the freedom of unregulated businesses to respond to uncertainty about future revenues by reducing spending and output. They are required to maintain sufficient facilities to serve all potential customers on demand, and to maintain specified levels of service quality.[9] The FCC's after-the-fact decision to prevent recovery of these mandatory expenditures, by eliminating SNA support and limiting high-cost loop support through the benchmarking rule and other caps, was unreasonable, and thus prohibited under the "secondary retroactivity" standard Respondents themselves cite. FCC Br. 48.

---

[9] *See*, *e.g.*, 47 U.S.C. §201(a) (duty to furnish service upon reasonable request), §214(d) (FCC may order a carrier "to provide itself with adequate facilities").

VI. THE FCC'S CHANGES TO SUPPORT FOR PRICE CAP CARRIERS WERE ARBITRARY AND CAPRICIOUS.

Petitioners challenge several discrete aspects of the FCC's reforms to high-cost support for price cap carriers.

First, in deciding to make "interim" Phase I support available only in "unserved" areas and to deny support for upgrades of existing broadband facilities, the FCC failed to address arguments that this approach would penalize States that had already promoted broadband deployment. USF Br. 57. The FCC's response paints this as a mere "disagree[ment] with [a] policy judgment[,]" which it claims it adequately explained. FCC Br. 52. However, ¶137 of the *Order*, on which the FCC relies, simply states that the agency "expects" carriers that have already deployed broadband capacity to continue doing so; it does not even mention, let alone respond meaningfully to, arguments that this approach is irrational and discriminatory. The Court is only required to defer to the FCC's judgment when it is supported by a rational explanation that acknowledges and responds to the issues presented by parties.[10] As to this issue, it did neither.

Second, the FCC failed to engage arguments against using an auction mechanism to distribute "Phase II" support. USF Br. 49. The FCC argues that this issue is not ripe for review, because the FCC did not "adopt" an auction

---

[10] *PSEG Energy Res. & Trade LLC v. FERC*, 665 F.3d 203 (D.C. Cir. 2011); *NorAm Gas Transmission Co. v. FERC*, 148 F.3d 1158, 1165 (D.C. Cir. 1990).

mechanism. FCC Br. 53. In fact, however, the FCC determined that "[i]n areas where the incumbent declines a state-level commitment, we *will* use a competitive bidding mechanism to distribute support." *Order*, ¶179 (emphasis added). This is plainly a decision, not a tentative conclusion. Although the details of the competitive bidding mechanism are yet to be determined, the decision to conduct an auction (as distinct from the particular method of conducting it) is ripe for review. Petitioners argued below that *any* auction would inherently conflict with statutory principles, and the FCC did not address these concerns at all, as discussed at USF Br. 48-50.

The FCC criticizes Petitioners for citing sections of the *Order* dealing with the separate Mobility Fund auction in the argument concerning competitive bidding for price cap Phase II support. FCC Br. 53. By doing so, Petitioners were giving the FCC the benefit of the doubt, because that was the only section of the *Order* that addressed, albeit inadequately, issues raised in the comments concerning potential harms of competitive bidding. If the Court were to ignore that section of the *Order* when reviewing this issue, the agency's failure to confront the issues presented to it would be even more evident.

Third, Respondents misapprehend Petitioners' argument that the denial of Phase II support in price cap service areas where costs exceed an "alternative technology" threshold, was arbitrary. USF Br. 52-53. Respondents brief the issue as if Petitioners were arguing that these high cost areas were not receiving any support at all, FCC Br. 62-63, but that is not the case. Rather, the FCC's rule provides that if a census block in a price cap service area exceeds the alternative technology threshold by even one dollar, the area is removed from Phase II support entirely and instead relegated to a separate remote areas fund. (For example, if the subsidy benchmark is $80 and the upper threshold is $250, a carrier with costs of $249 per line would receive $169 per line in support; but a carrier with costs of $251 per line would receive $0 in Phase II support.) Commenters offered an alternative in which the alternative technology threshold would serve as a cap on support instead of an absolute limit; under this approach, a carrier with costs of $251 or $2,500 per line would still be eligible for $170 in support. Comments of Consolidated Communications Holdings, WC Docket No. 10-90 *et al*., at 15-16 (filed Aug. 24, 2011). The FCC never responded to this alternative in the *Order*, and still has not done so on brief.

VII. OTHER ASPECTS OF THE *ORDER* ARE ARBITRARY, CAPRICIOUS, AND UNLAWFUL.

A. The Local Rate Floor is Unlawful and Inadequately Supported.

Respondents defend the FCC's denial of support to carriers whose local rates are below a minimum level, claiming that the agency can use "carrots" and "sticks" to "encourage" states to adjust local rates as long as it does not directly regulate them. FCC Br. 55-56. Here, however, the FCC crossed the jurisdictional line because the practical effect of its action is to regulate rates; any carrier that does not adjust its local rates is penalized by the exact dollar amount of the variation from the FCC's desired result.

Respondents dismiss the alternative argument that the rate floor is irrational because the FCC did not consider whether some "low" local rates may reflect smaller service areas, USF Br. 41-42, claiming that it was not adequately supported by data. FCC Br. 56-57. Yet the FCC itself had no data about *why* any particular carrier's rates were lower than another's, instead simply adopting an absolute rule that any rate below a particular level was "too low." It is hypocritical for the FCC to refuse to address a commenter's concerns for failure to meet a standard of proof that the FCC itself cavalierly ignores.

Respondents contend that the conflict between the rate floor and state universal service policies was never presented to the FCC, FCC Br. 57-58, but then admit the FCC was urged to modify its rate floor rule to take account of state laws mandating specific rates, and that the FCC did not address this issue. *Id*. Respondents argue, nonetheless, that the Petitioners' brief did not present the issue precisely the same way as below. But §405(a) only requires that the FCC have an opportunity to address the substance of an issue, not that it be given an advance look at every specific contention on appeal.[11] Respondents' substantive response

[11] *See* note 8, above.

to this issue, moreover, is a *non sequitur*. They argue that if states are subsidizing local rates, there is no need for a further federal subsidy, FCC Br. 58, but the "low" rates in question result from *both* federal and state subsidies, and there is no logical reason to assume that rates will continue to be affordable if one of the two is removed.

B. The Elimination of Support in Areas Served by an "Unsubsidized Competitor" Violates the Statute.

Respondents defend the FCC's rule denying support to incumbent carriers for any service area where an "unsubsidized" competitor operates as a reasonable "predictive judgment" that unsubsidized competitors will have an incentive to continue serving these areas. FCC Br. 58-60. This misses the point. The statute declares that "[q]uality services should be available [to all consumers] at … affordable rates[.]" 47 U.S.C. §254(b)(1), (3). It further creates a balanced system in which the ability of "eligible telecommunications carriers" to receive universal service support is offset by their obligation to continue providing service. 47 U.S.C. §214(e). The Commission cannot logically assume that *quality* service at *affordable* prices will remain available to *all customers* if there is no ETC obligated to provide it.

Respondents erroneously suggest that Petitioners are challenging State-imposed carrier-of-last-resort obligations. FCC Br. 60-61. Petitioners pointed to the existence of these obligations as a reason why the FCC's elimination of support is irrational, but did not ask either the FCC or the Court to modify State laws. Respondents' argument is a red herring that does not address the irrationality of the *Order*.

VIII. THE FCC'S FAILURE TO ADDRESS THE CONTRIBUTION BASE WAS ARBITRARY AND CAPRICIOUS.

Respondents' arguments why the FCC was justified in deferring the issue of how to generate sufficient revenues for the USF, FCC Br. 66-69, depend on the same inadequate theory of administrative discretion already addressed in Petitioners' initial brief. USF Br. 34-36. We therefore will not reply further to these points, except to note that Respondents' assertion that the FCC dealt with the growth of the contribution rate by setting a fixed budget for the high-cost fund, FCC Br. 68, is a *non sequitur*. Limiting outflows from the fund merely limits the potential magnitude of the problem, but does not address the underlying issue that the contribution *base* continues to shrink, putting an ever-growing burden on those consumers who have to bear the costs of supporting universal service.

IX. THE ORDER VIOLATED APA NOTICE AND COMMENT REQUIREMENTS.

A. The Notice Issue Is Properly Before This Court.

Citing *Globalstar, Inc. v. FCC*, 564 F.3d 476 (D.C. Cir. 2009), Respondents maintain that by failing to seek reconsideration of the Order, under section 405(a) Petitioners have waived the right to pursue the APA notice issue. FCC Br. 64. But *Globestar* is not binding on this Court, *see North American Coal Corporation v.*

OWCP, US Dept Labor, 854 F.2d 386, 388 (10th Cir. 1988) and Respondents' red herring argument amounts to a claim of ignorance of the APA. Regardless, this Court has denied the FCC's request to stay proceedings while reconsideration petitions are pending. Denials of reconsideration requests, moreover, are not appealable, *AT&T v. FCC*, 363 F.3d 504, 511 (D.C. Cir. 2004), and the FCC's history of sitting on pending reconsideration petitions would have made a reconsideration request futile anyway.

B. The Notices Respondents Reference Did Not Alert Petitioners To the Scope of the Order.

Respondents inaccurately assert that the various notices they cite alerted Petitioners to the scope of the ARC, ROFR, Dual Process and EAM provisions of the Order. NPRM ¶ ¶ 235-36, for example, read as a whole, expressed the FCC's expectation that the IAS transition would *trigger*, not remove an exogenous adjustment. The *Order* created an exemption but no such exemption appears in the final rules. Permitting EAM would eliminate the need for an ARC.

Respondents' claim that still other notices adequately alerted Petitioners to the Residential Rate Ceiling, Dual Process and ARC final rules similarly fails. These provisions were adopted as part of, and integral to, the FCC's determination to require the bill and keep regime that was first announced only in the *Order*. Thus, neither the scope and complexity of the ARC rules, the Residential Rate

Ceiling nor the dual process mechanism, as finalized, was reasonably foreshadowed by the FCC's cited notices.

Finally, the *Order* (¶¶173-175) differs in fully seven substantive ways from the ABC Plan referenced by Respondents. These were substantial changes and new approaches that required notice and opportunity for comment to comply with the APA. *BASF Wyandotte Corp*., *v. Costle*, 598 F.2d 637, 642 (1st Cir. 1979); *Prometheus Radio Project v FCC*, 652 F.3d 431, 449, 450, 453 (3rd Cir. 2011).

Respectfully submitted,

/s/ *Harvey L. Reiter*
Harvey L. Reiter
H. Russell Frisby, Jr.

Stinson Morrison Hecker LLP
1775 Pennsylvania Avenue, NW#800
Washington, DC 20006
202-728-3016
hreiter@stinson.com

On behalf of the Joint Petitioners
listed on the cover of this filing

CERTIFICATE OF COMPLIANCE

Certificate of Compliance With Type-Volume Limitations, Typeface Requirements, Type Style Requirements, Privacy Redaction Requirements, and Virus Scan

1. This filing complies with the type-volume limitation of the Third Briefing Order and Summary of Deadlines for Uncited Briefing because it contains 6,614 words, excluding the parts of the filing exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This filing complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and 10th Cir. R. 32(a) and the type style requirements of Fed. R. App. P. 32(a)(6) because this filing has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in 14-point Times New Roman font.

3. All required privacy redactions have been made.

4. This filing was scanned for viruses with Sophos Anti-Virus Program, last updated on June 5, 2013, and according to the program is free of viruses.

/s/ Harvey L. Reiter

June 5, 2013

CERTIFICATE OF SERVICE

I hereby certify that, on June 5, 2013, per the Court's order of October 18, 2012, I caused the foregoing document to be electronically filed with the Court via e-mail. I also certify this document was furnished through ECF electronic service to all parties in this case through a registered CM/ECF user. This document is available for viewing and downloading on the CM/ECF system.

/s/ Harvey L. Reiter

June 5, 2013