

**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**

ADDITIONAL UNIVERSAL SERVICE FUND ISSUES PRINCIPAL BRIEF

[Counsel for Petitioners Listed on Following Pages]

July 11, 2013

Rural Telephone Service Company, Inc., 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 Co. 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 hreiter@stinson.com

<p><i>Allband Communications Cooperative</i> By Its Counsel Don L. Keskey Public Law Resource Center PLLC 139 W. Lake Lansing Road, Suite 210 East Lansing, MI 48823 Tel: 517-999-7575 donkeskey@publiclawresourcecenter.com</p>	<p><i>Arizona Corporation Commission</i> 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</p>
<p><i>CenturyLink, Inc.</i> By Its Counsel Robert Allen Long, Jr. Gerard J. Waldron Yaron Dori Michael P. Beder Covington & Burling 1201 Pennsylvania Avenue, NW Washington, DC 20004 Tel: 202-662-6000 ydori@cov.com rlong@cov.com gwaldron@cov.com mmosier@cov.com</p>	<p><i>Consolidated Communications Holdings, Inc.</i> By Its 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</p>

<p><i>National Association of Regulatory Utility Commissioners</i> 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</p>	<p><i>Rural Independent Competitive Alliance</i> By Its Counsel David Cosson 2154 Wisconsin Avenue, NW Washington, DC 20007 Tel: 202-333-5275 dcosson@klctele.com</p> <p>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 hreiter@stinson.com</p>
<p><i>Vermont Public Service Board</i> 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</p> <p>Elisabeth H. Ross Birch, Horton, Bittner and Cherot 1155 Connecticut Ave. NW, Suite 1200 Washington, D.C. 20036 Tel: 202-659-5800 eross@dc.bhb.com</p>	

TABLE OF CONTENTS

TABLE OF AUTHORITIES	iii
GLOSSARY	vii
STATEMENT OF ISSUES	1
STANDARD OF REVIEW	2
SUMMARY OF ARGUMENT	3
I. THE COMMISSION’S DECISION LIMITING USF SUPPORT FOR BROADBAND DEPLOYMENT TO INCUMBENT PRICE CAP CARRIERS DISREGARDED BOTH ITS STATUTORY DUTY TO PROMOTE COMPETITION BETWEEN INCUMBENTS AND COMPETITIVE CARRIERS AND ITS OWN POLICY MANDATING “COMPETITIVE NEUTRALITY” BETWEEN INCUMBENTS AND CETCs IN THE DISBURSEMENT OF USF SUPPORT.	7
A. The Commission’s <i>Order</i> Results in Disparate Treatment of Price Cap ILECs and CETCs.	8
B. The Five Year Head Start Given Price Cap Carriers Under the <i>Order</i> Undermines the Act’s Goal of Promoting Competition for Incumbent Carriers.	9
C. The Commission’s Claim That It Is Proper To Favor Incumbent Carriers Because They Are Better Able To Expand Broadband Not Only Flouts Its Competitive Neutrality Principle, It Is Unsupported By Substantial Evidence.	10
II. THE FCC VIOLATED SECTION 410(c) BY CHANGING SEPARATIONS RULES WITHOUT REFERRING THOSE ELEMENTS OF ITS REFORM PROPOSALS TO A SEPARATIONS BOARD.....	14
A. Facts, Procedural History, and Regulatory Background.	14
B. The <i>Order</i> Ignores That There Are No Exceptions To The Requirement That “Any Proceeding Regarding The Jurisdictional Separation Of Common Carrier Property And Expenses Between Interstate And Intrastate Operations” Be Referred To A Joint Board.....	17
1. Standards for Determining Which Rule Changes “Regard” Separations.	18
2. Changes to the Part 36 Separations Rules Themselves.....	19
3. Changes to Other Rules that Affect Separations Rules.....	20

III. THE COMMISSION IRRATIONALLY REFUSED TO MODIFY SERVICE OBLIGATIONS FOR CARRIERS IT DENIED UNIVERSAL SERVICE SUPPORT	24
IV. THE <i>ORDER</i> , AS APPLIED TO CERTAIN SMALL RURAL CARRIERS, IS UNCONSTITUTIONAL UNDER DUE PROCESS PRINCIPLES AND AS A BILL OF ATTAINDER, AND ALSO VIOLATES THE ACT, AND PRINCIPLES OF ESTOPPEL AND CONTRACT LAW.	29
A. Statement Of Additional Facts.....	29
B. Allband’s Constitutional Rights Are Violated By the <i>Order</i>	31
CONCLUSION	38
CERTIFICATE OF COMPLIANCE.....	39
CERTIFICATE OF SERVICE	40

TABLE OF AUTHORITIES

	Page(s)
CASES	
<i>Alenco Communications, Inc. v. FCC</i> , 201 F.3d 608 (5 th Cir. 2000)	10
<i>Bluefield Waterworks & Improvement Co. v. Public Service Comm’n of West Virginia</i> , 262 U.S. 679 (1923).....	34
<i>Covington & Lexington Tpk. Rd. Co. v Sandford</i> , 164 U.S. 578 (1896).....	38
<i>Crockett Telephone Co. v. FCC</i> , 963 F.2d 1564 (D.C. Cir. 1992).....	18
<i>Federal Communications Commission, et al. v Fox Television Stations, Inc.</i> , 132 S. Ct. 2307 (2012).....	33
<i>Federal Power Commission v Hope Natural Gas Company</i> , 320 U.S. 591 (1944).....	34
<i>Idaho Power Co. v. FERC</i> , 312 F.3d 454 (D.C. Cir. 2002).....	11, 12
<i>Lucas v. South Carolina Coastal Council</i> , 505 U.S. 1003 (1992).....	38
<i>Maier v. EPA</i> , 114 F.3d 1032 (10th Cir. 1997)	28
<i>Maryland Peoples’ Counsel v. FERC</i> , 761 F.2d 768 (D.C. Cir. 1985).....	28
<i>Motor Vehicle Mfrs. Assn. of United States, Inc. v. State Farm Mut. Automobile Ins. Co.</i> , 463 U.S. 29 (1983).....	14
<i>Pennsylvania Coal Co. v Mahon</i> , 260 U.S. 393 (1922).....	38

<i>Sierra Club v. Gorsuch</i> , 715 F.2d 653 (D.C. Cir. 1983).....	28
<i>Smith v. Illinois Bell Tel. Co.</i> , 282 U.S. 133 (1930).....	16, 17
<i>Stone v. Farmers' Loan and Trust Co.</i> , 116 U.S. 307 (1886).....	38
<i>Texas Office of Pub. Util. Counsel. v. FCC</i> , 183 F.3d 393 (5th Cir. 1999)	18, 19, 20
<i>United States v Brown</i> , 381 U.S. 437 (1965).....	35
<i>United States v Lovett</i> , 328 U.S. 303 (1946).....	35
<i>United States v Winstar Corp.</i> , 518 U.S. 839 (1996).....	37

AGENCY DECISIONS

<i>Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers</i> , Seventh Report and Order, 16 F.C.C.R. 9923 (2001)	13
<i>Connect America Fund</i> , 26 F.C.C.R. 4554 (2011).....	9, 15
<i>Connect America Fund</i> , 26 F.C.C.R. 17663 (2011).....	<i>passim</i>
<i>Mescalero Apache Telecom, Inc.</i> , 16 F.C.C.R. 38136 (2001).....	14
<i>M&L Enterprises, Inc., d/b/a Skyline Telephone Co.</i> , 19 F.C.C.R. 6761 (2004).....	14
<i>Petition of Mid-Rivers Telephone Cooperative, Inc. for Order Declaring It to Be an Incumbent Local Exchange Carrier in Terry, Montana Pursuant to Section 251(h)(2)</i> , Report and Order, 21 F.C.C.R. 11506 (2006)	13

<i>Universal Service Order,</i> 12 F.C.C.R. 8776 (1997).....	8
---	---

<i>US West Communications, Inc. and Eagle Telecommunications,</i> 10 F.C.C.R. 1771 (1995).....	14
---	----

STATUTES

5 U.S.C. §706(2)	6
47 U.S.C. §160.....	27
47 U.S.C. §214(e)	5, 25, 29
47 U.S.C. §214(e)(1).....	9, 25
47 U.S.C. §214(e)(2).....	9
47 U.S.C. §214(e)(4).....	26, 27
47 U.S.C. §214(e)(5).....	24
47 U.S.C. §254(b)	31
47 U.S.C. §254(b)(5).....	31
47 U.S.C. §254(c)	25
47 U.S.C. §254(d)	31
47 U.S.C. §254(e)	5, 9, 25, 27, 31
47 U.S.C. §410(c)	1, 14, 15, 16, 17, 18, 19, 21

REGULATIONS

47 C.F.R. §54.5	24
47 C.F.R. §36.603	19
47 C.F.R. §36.605(a).....	19
47 C.F.R. §36.621(a)(4).....	19
47 C.F.R. §36.621(a)(5).....	19

LEGISLATIVE MATERIALS

S. Rep. No. 92-362	22
--------------------------	----

GLOSSARY

Act	Telecommunications Act of 1996
CAF	Connect America Fund
CETC	Competitive Eligible Telecommunications Carrier
CLEC	Competitive Local Exchange Carrier
ETC	Eligible Telecommunications Carrier
FCC or Commission	Federal Communications Commission
ILEC	Incumbent Local Exchange Carrier
RLEC	Rural Local Exchange Carrier
RUS	Rural Utilities Service
SA	Supplemental Joint Appendix
USF	Universal Service Fund

STATEMENT OF ISSUES

1. The Federal Communications Commission (FCC or Commission) is required (1) by the Telecommunications Act of 1996 (Act) to promote both universal service and local service competition and (2) by its own rules to ensure “competitive neutrality” between service providers in distributing USF support. Did the Commission arbitrarily disregard its statutory obligations and its own rules in granting price cap carriers USF support for expanding broadband and a right of first refusal to future universal service fund (USF) support, neither of which is available to competitive eligible telecommunications carriers (CETCs)?

2. The Commission is required by 47 U.S.C. § 410(c) to initially refer issues regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations (“separations”) that arise in a rulemaking proceeding to a Federal-State Joint Board (“Separations Joint Board”):

The Commission shall refer any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations, which it institutes pursuant to a notice of proposed rulemaking . . . to a Federal-State Joint Board. The Joint Board . . . shall prepare a recommended decision for prompt review and action by the Commission. . . . The Commission shall also afford the State members of the Joint Board an opportunity to participate in its deliberations, but not vote . . .

47 U.S.C. § 410(c). Did the Commission violate Section 410(c), or, in the alternative, act arbitrarily and capriciously, by failing to refer to a Separations Joint Board elements of its proposed reform rules that directly impacted its separations

rules and changed the level of common carrier property and expenses allocated to the interstate jurisdiction?

3. Was it arbitrary and capricious, unreasonable or otherwise contrary to law for the FCC to withhold USF support from any carrier serving a territory also served by an “unsubsidized competitor” without also relieving these carriers of their ongoing mandatory service obligations under the Act?

4. Is *Connect America Fund*, 26 F.C.C.R. 17663 (2011) (*Order*), as applied to Allband Communications Cooperative, unconstitutional under Due Process provisions, and as a Bill of Attainder, and is it also unlawful under principles of estoppel and contract law, and as being arbitrary and contrary to the Act?

STANDARD OF REVIEW

Sections I and III of the Brief are governed by the standard of review discussed at pp. 39-42 of the Joint Preliminary Brief. Section II of this brief is governed by the *Chevron* “step one” standard set out at pages 39-40 of the Preliminary Joint Brief. If any factual or discretionary determinations were involved in the failure to issue the referral – and there were none – the standard of review set out at pages 41-42 of that brief would apply. Section IV of this brief is governed by the *de novo* standard of review applicable to constitutional issues, as set out at pages 40-41 of that brief.

SUMMARY OF ARGUMENT

1. The Act requires the FCC *both* to advance universal service and to promote and protect competition between incumbent local exchange carriers (ILECs) and CETCs. In granting ILECs an exclusive five year right to Phase I Connect America Fund (CAF) funds for broadband deployment and an exclusive right of first refusal to obtain CAF funds in Phase II, the Commission arbitrarily gave no effect to the competition-promoting objectives of the Act. On the contrary, because USF support is essential to the viability of rural service, its *Order* gives ILECs a five year competitive head start, threatening the viability of rural competitive local exchange carriers (CLECs). This has the effect of erecting, not eliminating barriers to competition for ILECs in contravention of the Act.

The Commission's disparate treatment of ILECs and CLECs in distribution of USF support violates its own USF "competitive neutrality" principle that support mechanisms must "neither unfairly advantage nor disadvantage one provider over another." While competitive neutrality does not require identical treatment, the Commission's policy requires that disparities be "minimized." That policy is self-evidently violated by the *Order*'s provisions giving ILECs *exclusive* USF rights. The Commission's assertion that the interest in competitive neutrality is "outweighed" by its expectation that larger price cap carriers will be better able to expand broadband deployment fails on two grounds. First, granting ILECs

exclusive USF rights cannot be squared with the FCC's professed continued adherence to the "competitive neutrality" principle. Second, there is no record support for its conclusion even if it were free to abandon the competitive neutrality principle. On the contrary, the evidence (and the FCC's own prior findings) indicate that the favored price cap ILECs have a record of poor service to rural communities and are the least likely entities to expand broadband deployment.

2. Generally, the Telecommunications Act (the "Act") establishes a dual regulatory scheme, giving the FCC jurisdiction over interstate services, and the states jurisdiction over intrastate services. "Separations" is necessary to enable each sphere of governmental authority to carry out its responsibilities. The FCC has adopted formal separations rules to govern carriers' allocations of plant and expenses between the two jurisdictions.

The Act requires the FCC, when it initiates a rulemaking proceeding, to refer any issues regarding the jurisdictional separation of plant and expenses to a Separations Joint Board, and base its decision on those issues on a Joint Board Recommended Decision. In the proceeding below, the FCC changed separations rules and practices in two ways. In some cases, the FCC directly adopted new separations rules with new formal separations methodologies. In others, the FCC made decisions that had as much effect on separations as direct changes to the rules themselves, such as by ordering the reduction of intrastate access rates (and

thereby revenues) and replacing them in part with a new interstate charge, without also adjusting the allocation of the underlying costs between jurisdictions. It should have referred all elements of its proposed reform that impacted separations to a Separations Joint Board.

The FCC's referral duty is mandatory where it adopts formal changes to its separations methodologies in a rulemaking proceeding such as this one. Referral is also mandatory where the FCC adopts rule changes that have direct effects on separations methodologies. The FCC's decisions regarding separations methods should be reversed and remanded so that the FCC can submit those issues to a Separations Joint Board and adopt a new decision based on a Separations Joint Board Recommended Decision.

3. Sections 214(e) and 254(e) of the Act establish an explicit *quid pro quo* in which eligible telecommunications carriers assume obligations to provide and advertise basic services in exchange for the opportunity to receive USF support. The *Order* improperly thwarts Congressional intent by decreeing that ETCs may not receive any support for areas where an "unsubsidized competitor" offers service, but refusing to relieve these ETCs of their corresponding service obligations. Assuming *arguendo* the FCC can rely on the presence of an "unsubsidized competitor" as a reason to remove eligibility for support in particular areas at all, it cannot do so without also relieving carriers of their service

obligations for these areas. The decoupling of these two issues is inconsistent with the statutory scheme.

4. The *Order* as applied to Allband violates the Due Process Clause because (i) the *Order* is void for vagueness; (ii) the *Order* comprises an unfair and unconscionable retroactive reversal of Commission orders and federal loan contracts upon which Allband has relied; and (iii) effects an unconstitutional confiscation of Allband's (and its customer-members') property, in violation of Fifth Amendment Due Process.

The *Order* (arising from a legislative rulemaking process) also imposes a harsh and punitive result targeted at Allband, or a small identifiable class of rural companies which undertook actions after, and in reliance upon, the 1996 USF provisions, thus comprising an unconstitutional legislative action in the nature of a Bill of Attainder.

The *Order* is also contrary to the 1996 Act; is arbitrary and unlawful under Section 706(2) of the Administrative Procedures Act, 5 U.S.C. § 706(2); and is unlawful under estoppel and contract law principles.

I. THE COMMISSION’S DECISION LIMITING USF SUPPORT FOR BROADBAND DEPLOYMENT TO INCUMBENT PRICE CAP CARRIERS DISREGARDED BOTH ITS STATUTORY DUTY TO PROMOTE COMPETITION BETWEEN INCUMBENTS AND COMPETITIVE CARRIERS AND ITS OWN POLICY MANDATING “COMPETITIVE NEUTRALITY” BETWEEN INCUMBENTS AND CETCs IN THE DISBURSEMENT OF USF SUPPORT.

Of critical importance to competitive rural local exchange carriers is the impediment to their survival posed by the Commission’s discriminatory policy favoring incumbent price cap carriers over CETCs in the disbursement of USF funds targeted to support broadband. While RICA does not join the rural wireless carriers’ argument that elimination of the identical support rule was arbitrary,¹ we agree fully with those carriers that denying any USF support to competitive carriers for broadband and reserving it exclusively to price cap ILECs was arbitrary in two respects.

First, the FCC failed to explain how a USF policy reserving USF support for incumbents and excluding competitive rural carriers from USF support could be reconciled with the Act’s directive that local telecom markets be open to competition. *See* Wireless Carrier USF Br. at 32-35. As the wireless carriers aptly put it, “making CAF II support accessible only to the largest LECs will serve only to preserve and advance their dominance in the local telecom market.” *Id.* at 35.

¹ *See* Wireless Carriers USF Brief, Section IV.

Second, the FCC departed without reasoned explanation from its own USF competitive neutrality principle that “universal support mechanisms and rules neither unfairly advantage or disadvantage one provider over another.” *Universal Service Order*, 12 F.C.C.R. 8776, ¶¶ 46-48 (1997). As the wireless carriers explained, the Commission could not logically claim that admittedly disparate treatment is acceptable as long as it is not “unfair” without addressing how it could possibly be fair to exclude CETCs from USF support *entirely* and still preserve competitive neutrality. Wireless Carrier USF Br. at 34.

Accordingly, RICA adopts and incorporates by reference the argument contained at Section III of the Wireless Carrier USF Brief (pp. 32-35). This brief supplements that argument on two points. It explains that by giving incumbent carriers a five year head start, the FCC’s *Order* raises barriers to competition that the Act obliges it to reduce. And, with respect to the Commission’s USF competitive neutrality principle, it demonstrates the unsupported nature of the Commission’s claim that it is proper to favor incumbent carriers because they are better able to expand broadband. These points are discussed in more detail below.

A. The Commission’s *Order* Results in Disparate Treatment of Price Cap ILECs and CETCs.

As noted in the preliminary joint brief, the FCC allocated \$1.8 billion in CAF support to areas served by price-cap ILECs. Under CAF Phase I, existing high cost support to these carriers is frozen, but up to \$300 million of new funding

will be available to them, but not to CETCs, to promote broadband deployment.

Id. ¶¶22, 25 (JA at 400, 401). CETCs' existing support was capped effective

December 31, 2011, and will be phased-out over five years. *Id.* ¶519 (JA at 559).

CAF II will develop a cost model to estimate the support necessary to fund

broadband in high-cost areas. *Order*, ¶23 (JA at 400). Following adoption of the

cost model, the incumbent price-cap carrier "shall be the presumptive recipient of the model derived support amount for the five-year CAF Phase II period," *Order*,

¶171 (JA at 456), provided it accepts a state-level broadband deployment

commitment. *Id.* (JA at 456). Although the *Order* does not use the term, this right

of first refusal (RoFR) had its origins in the proposed rule, a proposal that would

have granted price cap carriers a RoFR for USF support in their service areas.

Connect America Fund, 26 F.C.C.R. 4554 (2011) (*NPRM*), ¶281 (SA at 95). Even

where the price cap carrier does not exercise its right of first refusal, it is still

permitted to bid in the auction for USF support against other carriers.

B. The Five Year Head Start Given Price Cap Carriers Under the *Order* Undermines the Act's Goal of Promoting Competition for Incumbent Carriers.

The Act requires both that only designated ETCs may receive universal

service support, 47 U.S.C. §§ 214(e)(1) and 254(e), and that additional qualified

carriers *shall* be designated ETCs in the areas of non-rural carriers. 47 U.S.C. §

214(e)(2). These provisions reflect the dual nature of the FCC's obligations under

the Act, namely that it “must see to it that *both* universal service and local competition are realized.” *Alenco Communications, Inc. v. FCC*, 201 F.3d 608, 615 (5th Cir. 2000) (emphasis in original). In determining, however, that only price cap carriers (the great majority of which are non-rural), but not their competitors, are eligible for additional USF support over the next five years -- while their competitors’ existing support is phased out during that same period - the Commission has rendered meaningless the competition-promoting aspect of its dual statutory obligations. Under the *Order*, incumbents are effectively given a five year head start on their CETC competitors. Since, by the Commission’s own account, USF support is essential to build out in rural areas, *Order*, ¶ 2 (JA at 394), such a head start gives incumbents a virtually insurmountable, and arbitrary advantage.

C. The Commission’s Claim That It Is Proper To Favor Incumbent Carriers Because They Are Better Able To Expand Broadband Not Only Flouts Its Competitive Neutrality Principle, It Is Unsupported By Substantial Evidence.

Conceding that its *Order* results in disparate treatment of incumbent price cap carriers and CETCs, the Commission asserts that the departure from “strict” competitive neutrality is “outweighed” by the access to advanced services to consumers it expects price cap ILECs will provide when given the “opportunity to commit to deploying broadband in their statewide service areas.” *Order*, ¶177 (JA at 458-59). It acknowledges that other providers might be able to commit to

serving small areas, but asserts that the price cap carriers' service area-wide facilities put them in a unique position to deploy broadband rapidly and efficiently in such large areas. *Id* (JA at 459). This explanation can neither be squared with the competitive neutrality principle with which the Commission claims to comply nor justified by the record.

The competitive neutrality principle is quite explicit. The reference in its text to support mechanisms that “neither unfairly advantage nor disadvantage one provider over another,” *Universal Service Order, supra*, ¶ 46-47, necessarily implies that competitive neutrality does not require *identical* treatment. But while perfect neutrality might not be achievable, the Commission explained that its goal was to “ensure that such disparities are *minimized* so that no entity receives an unfair competitive advantage that may skew the marketplace or inhibit competition.” *Id.*, ¶ 48 (emphasis added). The *Order*, however, makes no claim – nor could it – that in *excluding* CETCs it has “minimized disparities” in treatment. Nor does it claim that the exclusion will not “skew the marketplace.” To the contrary it expects exactly that result: it expects that incumbent price cap carriers, not their competitors, will be the exclusive broadband providers in their service areas and grants them USF support to further that end.

While agencies are generally given deference in the interpretation of their own orders and regulations, their interpretation must still be plausible. *Idaho*

Power Co. v. FERC, 312 F.3d 454, 461-62 (D.C. Cir. 2002). Having established the criteria for evaluation of the fit between its rules and its principles, the Commission is not free simply to ignore those criteria when they become inconvenient. That, however, is exactly what has happened here.

Instead of explaining how the exclusion of CETCs could be “fair” or addressing its original definition of the principle, the *Order* effectively abandons any pretense of adhering to competitive neutrality and turns to its real justification: the price cap carriers are big and rich (read AT&T, Verizon, CenturyLink) and can somehow leverage their existing infrastructure to more quickly bring broadband to more of the locations that they have previously ignored. *Order*, ¶ 177 (JA at 458-59). By contrast, competitors may be competent in small areas, but are believed to be singularly or collectively incapable of rapid expansion to state-wide areas. *Id.* (JA at 458-59).

Even if the Commission could lawfully depart from its competitive neutrality principle, this excuse for doing so is not supported by the record. Take first the Commission’s assertion that USF will go to areas where the ILEC is likely to have the only wireline facilities and that few other bidders will have the “financial and technological capabilities to deliver scalable broadband that will meet our requirements over time.” *Order*, ¶175 (JA at 457). No citation is provided for this conclusion, and the record is to the contrary. Rural CLECs have repeatedly

explained to the Commission that in rural areas, price cap carriers' facilities are often old and ill-maintained. RICA Comments, CC Docket 01-92, August 21, 2001, pp 1-2 (JA at 1201-02) ("...large ILECs...had for some time avoided upgrading or even maintaining the facilities in these communities...").² More than a decade ago the Commission itself observed:

CLECs often are more likely to deploy in rural areas the new facilities capable of supporting advanced calling features and advanced telecommunications services than are non-rural ILECs, which are more likely first to deploy such facilities in their more concentrated, urban markets.

Access Charge Reform, Reform of Access Charges Imposed by Competitive Local Exchange Carriers, Seventh Report and Order, 16 F.C.C.R. 9923, ¶ 65 (2001) ("CLEC Order").

Rural CLECs also explained that in rural areas with long local loops even where the price cap carriers have up-to-date voice capable facilities, they are not scalable to meet the new broadband requirement. Broadband provided over copper loops with DSL technology may be upgradable to meet the new 4/1 standard in small towns, but is not upgradeable to that standard on much longer loops serving

² *Petition of Mid-Rivers Telephone Cooperative, Inc. for Order Declaring It to Be an Incumbent Local Exchange Carrier in Terry, Montana Pursuant to Section 251(h)(2)*, Report and Order, 21 F.C.C.R. 11506 (2006), ¶ 12 ("Mid-Rivers serves between 85 and 93 percent of the access lines in the Terry exchange . . . The Mid-Rivers facilities in Terry appear to be technically superior to those of Qwest. Mid-Rivers also appears to provide maintenance and repair operations that are located much closer . . .")

rural residents. RICA Ex Parte, October 17, 2011, p. 5 (JA at 3924). The Commission ignores the contradictions between the record on this point and its “leverage” assumption.

The Commission also ignores the logical implication of its finding that by far the largest amount –both in absolute and percentage terms—of areas unserved by broadband are in the service areas of the price cap companies. *Order*, ¶ 127 (JA at 439) (83% of Americans without access to fixed broadband live in price cap study areas). Indeed, the Commission’s conclusion is inconsistent with its own recognition that large carriers have underperformed in rural communities. *CLEC Order, supra*.³ Where, as here, the agency has ignored evidence – as well as its own findings - contradicting its conclusions, its actions are arbitrary and capricious. *Motor Vehicle Mfrs. Assn. of United States, Inc. v. State Farm Mut. Automobile Ins. Co.*, 463 U.S. 29, 43 (1983).

II. THE FCC VIOLATED SECTION 410(c) BY CHANGING SEPARATIONS RULES WITHOUT REFERRING THOSE ELEMENTS OF ITS REFORM PROPOSALS TO A SEPARATIONS BOARD.

A. Facts, Procedural History, and Regulatory Background.

³ Over the last twenty years, many large companies have sold their rural exchanges rather than invest in network upgrades needed to improve and modernize rural service. See, e.g., *US West Communications, Inc. and Eagle Telecommunications*, 10 F.C.C.R. 1771, 1774 (1995); *M&L Enterprises, Inc., d/b/a Skyline Telephone Co.*, 19 F.C.C.R. 6761 (2004); *Mescalero Apache Telecom, Inc.*, 16 F.C.C.R. 38136 (APD 2001) (order by Chief, Accounting Policy Division).

The FCC adopted the November 18, 2011 *Order* under review as a rule, preceded by a Notice of Proposed Rulemaking.

The FCC recognized from the outset that its proposed comprehensive reforms might very well impact separations. In its *NPRM*, the FCC asked parties to comment on how its proposed reforms might affect or be affected by the existing separations process and future reform.⁴ The FCC specifically noted that it has already created a Separations Joint Board to study separations issues in another docket. However, the FCC did not refer the separations issues in this proceeding to that Separations Joint Board (or any new Separations Joint Board) for preparation of a Recommended Decision pursuant to Section 410(c), even while acknowledging that the proposed rule changes would likely alter existing separations policies.

In their comments, parties reminded the FCC that it had to comply with its statutory duty to refer separations issues to a Separations Joint Board. For example, the Rural Broadband Alliance (“RBA”) cautioned the FCC not to “overlook the statutorily required Joint Board processes that jurisdictionally separate network costs used to provide both interstate and intrastate services.”⁵ RBA reminded the FCC that it had to refer separations issues initially to a Joint Board under Section

⁴ *NPRM*, ¶ 396 (SA at 123).

⁵ Comments of the RBA, submitted Aug. 22, 2011, at 18 (“RBA Aug. Comments”) (JA at 3186).

410(c)⁶ and pointed out a number of separations rules and policy changes implicated by the FCC's proposals.⁷

The Section 410(c) referral requirement fortifies the dual regulatory scheme that the Act establishes for carriers' provision of telecommunications services.

The Act generally gives the FCC jurisdiction over carriers' provision of interstate services⁸ and the states jurisdiction over carriers' provision of intrastate services.⁹

Because most property and expenses relate both to interstate and intrastate service, *e.g.*, the cost of a switch that handles both interstate and intrastate calls, separation of common carrier property and expenses is fundamental to preserving each regulator's sphere of authority. Indeed, in *Smith v. Illinois Bell Telephone Company*, the U.S. Supreme Court held that it was essential for carriers to "separate" their property, revenues and expenses between the two jurisdictions to recognize "the competent governmental authority in each field of regulation

⁶ Attachment to RBA Aug. Comments at 26 (JA at 3194).

⁷ *Id.* See also, *e.g. id.* at 18 (cap on the High Cost Loop Fund), 26, 28-29 (reductions in intrastate access charges) (JA at 3186, 3194, 3196-97); Comments of the RBA, Apr. 18, 2011, 25 (other matters require referral to the Joint Board) (JA at 2607); see generally, Letter from AT&T to FCC (Dec. 6, 2010), 1 (JA at 1764)(in the letter that prompted the FCC to seek comments on separations impacts of its proposals in its *NPRM*, referenced at ¶ 396 (SA at 123) n.569, AT&T said the FCC should "treat loops used to provide broadband as exclusively interstate.").

⁸ Section 152(a).

⁹ Section 152(b).

appropriately.”¹⁰ The FCC adopted Part 36 of its rules to govern the allocation of carriers’ revenues, costs and expenses between the two jurisdictions.

B. The *Order* Ignores That There Are No Exceptions To The Requirement That “Any Proceeding Regarding The Jurisdictional Separation Of Common Carrier Property And Expenses Between Interstate And Intrastate Operations” Be Referred To A Joint Board.

There are no exceptions to the requirement that “any proceeding regarding the jurisdictional separation of common carrier property and expenses between interstate and intrastate operations” be referred to a Joint Board. 47 U.S.C. § 410(c). This rulemaking “regard[ed]” jurisdictional separations, so the FCC was required to refer the elements of its proposed comprehensive reform that changed separations to a Separations Joint Board.

The FCC made a number of key changes to separations rules and policies in the rulemaking order it finally adopted. As discussed further below, the FCC changed Part 36 separations rules expressly in some parts of its order, and in others, it used phraseology not explicitly cast in separations terms that had just as much direct impact on the separations rules as the changes it made to the Part 36 rules themselves. The FCC also directly affected separations policies by ordering the reduction of intrastate rates (and thereby revenues), and replacing them in part

¹⁰ *Smith v. Illinois Bell Tel. Co.*, 282 U.S. 133, 148 (1930).

with a new interstate charge, without also making corollary changes to adjust the allocation of the underlying costs between jurisdictions.

1. Standards for Determining Which Rule Changes “Regard” Separations.

As the D.C. Circuit held in *Crockett Telephone Company v. FCC*, the FCC must make a Separations Joint Board referral under Section 410(c) when elements of its proposed rules will result in separations methodology changes.¹¹ Further, even where the proposed rule changes do not explicitly change the separations rules, but nevertheless *effect* allocations between jurisdictions, Joint Board referral is required. As the Fifth Circuit stated in *Texas Office of Public Utility Counsel v. FCC*: “[The FCC] must show that the Joint Board was aware of the *effects* on the jurisdictional separations rules of replacing the existing high-cost support system. The plain language of the statute shows that *any* shift in the allocation of

¹¹ *Crockett Telephone Co. v. FCC*, 963 F.2d 1564, 1571 (D.C. Cir. 1992) (“Crockett”). In *Crockett*, the FCC and the state public utility commissions were both using an informal “average schedule” method to approximate the result achieved by formal separations rules. There was no rule change as the FCC had simply informally consented to the States’ use of the same “average schedule” method the FCC used. *Id.* In denying a petition for review by private company petitioners seeking to overturn this FCC/state consensus, the Court held that Section 410(c) by its terms applies only to rulemaking proceedings begun to alter the separations rules, and so did not apply. *Id.*; see 47 U.S.C. § 410(c) (duty to refer applies to proceedings the FCC “institutes pursuant to a notice of proposed rulemaking”). By contrast, the FCC here has proceeded by issuing a rulemaking notice. Further, there is no consensus between the state petitioners and the FCC. The Section 410(c) referral requirement applies to achieve mandatory involvement by states in FCC deliberations on separations rule changes.

jurisdictional responsibility lies at the heart of § 410(c)'s consultation requirement.”¹²

2. Changes to the Part 36 Separations Rules Themselves.

In its decision, the FCC made numerous and substantial changes directly to its Part 36 rules to accomplish its universal service/intercarrier compensation reform. The FCC limited the portion of nationwide loop cost expense that certain carriers could allocate to the interstate jurisdiction.¹³ It also significantly curtailed carriers’ ability to receive “Safety net additive support” for new Telecommunications Plant in Service;¹⁴ so that carriers would no longer be able to recover these costs from the interstate jurisdiction. Moreover, it limited the amount of Corporate Operations Expenses carriers could allocate to the interstate jurisdiction.¹⁵

In one of its most glaring failures to respect the jurisdictional division of authority, the FCC adopted a new Part 36.621(a)(5) rule giving its *staff* discretion to publish a schedule each year establishing new limits on unseparated loop cost allocated to the interstate jurisdiction.¹⁶ Loop costs below those actually incurred by the carrier are then fed into the separations algorithms and reduce the amount of

¹² *Texas Office of Pub. Util. Counsel. v. FCC*, 183 F.3d 393, 416 (5th Cir. 1999) (emphasis added).

¹³ 47 C.F.R. § 36.603, *Order* at App. A, 496-97 (JA at 886-87).

¹⁴ 47 C.F.R. § 36.605(a), *Order* at App. A, 497 (JA at 887).

¹⁵ 47 C.F.R. 36.621(a)(4), *Order* at App. A, 498-99 (JA at 888).

¹⁶ *Order*, ¶ 218 (JA at 471).

cost allocated to the interstate jurisdiction. As a result, a carrier may have included a level of investment in its “rate base” without objection in one year pursuant to the FCC’s rule, but in the next year, the FCC Staff could issue a new “schedule” that unilaterally and materially reduced the level of the previously permitted investment or expense. The FCC would essentially move previously allowable interstate expenses to the intrastate jurisdiction to reduce universal service support for loop costs each time its Staff decided to reduce the allowable total unseparated costs of a carrier.

In each of these instances, the FCC made actual changes to Part 36 separations rules in its *Order* without first consulting a Separations Joint Board.

3. Changes to Other Rules that Affect Separations Rules.

The FCC’s changes to its universal service rules affected its separations rules, thereby requiring referral under the *Texas Office of Public Utility Counsel* precedent from the Fifth Circuit reviewed above. A number of its changes were designed to limit the amount of universal service support carriers would receive. The FCC capped the level of the High Cost Loop (“HCL”) Fund to limit the support carriers would receive for various expenses, including capital and operating expenses.¹⁷ It reduced HCL support for carriers whose intrastate end user

¹⁷ *Order*, ¶¶ 214-217 (JA at 470-71).

local rates were below a local rate floor.¹⁸ If a carrier does not raise its intrastate rates at least to that level, its support levels are reduced.

Each of these changes directly impacted the separation of property and expenses between the jurisdictions. Costs that were assigned to the interstate jurisdiction for recovery from the Universal Service Fund were essentially reassigned to the intrastate jurisdiction for possible recovery from other sources.¹⁹ These costs and expenses had previously been allocated to the interstate jurisdiction to be supported by the USF and now would no longer be covered by the Fund.

These changes impact separations as much as changes to the rules themselves. In fact, in enacting Section 410(c), Congress was specifically concerned that FCC separations rule changes would leave costs to the states for recovery by default in intrastate rates:

Thus, if the Commission declares its rate base to include certain costs, these costs are not used in determining a State's rate base; conversely,

¹⁸ *Order*, ¶ 235 (JA at 476-77).

¹⁹ The RBA highlighted the separations' impact of this proposed High Cost Loop Fund cap rule change: "There is, however, a growing cost recovery problem that results from the imposition of a cap on the High Cost Loop fund. Costs that are assigned to the interstate jurisdiction for recovery from the HCL fund pursuant to separations rules are essentially reassigned to the intrastate jurisdiction because of the insufficiency of the Fund. Consideration of the impact of this result on a rural incumbent rate-of-return carrier may properly be addressed by the Commission in conjunction with the Federal State Joint Board; the state members of the Joint Board are best placed to address the issues set forth above . . ." Attachment to the RBA Aug. Comments at 18 (JA at 3222).

if the Federal Communications Commission does not use certain costs, the State may be left with these costs in determining its rate base---and correspondingly higher rates for local services to the local consumer. The determination of the rate base at the Federal level then, has a strong relation to the rates which are charged at the local level. Accordingly, the procedures for establishing the separations of plant and expenses at the Federal level have invoked great concern among the States as manifested by the interest expressed by the National Association of Regulatory Utility Commissioners (NARUC).²⁰

Universal service changes that have the effect of changing the state cost allocation must be reviewed by a Separations Joint Board.

The FCC's changes to intercarrier compensation rules also directly affected separations rules, and required referral to a Separations Joint Board. Through its intercarrier compensation reform, the FCC reduced and eliminated certain intrastate access charges over a transition period.²¹ For many carriers, the intrastate access revenues can represent a substantial portion of their existing intrastate revenues. The FCC allowed carriers to charge a new interstate-approved rate, the Access Recovery Charge, and receive some limited support from the Connect America Fund as a partial and limited means of addressing substantial lost revenue.²²

²⁰ S. Rep. No. 92-362, reprinted in 1971 U.S.C.C.A.N. 1511, 1513.

²¹ *Order*, ¶ 801, Figure 9 (JA at 661-62). "Access charges" are rates that local carriers charge interexchange carriers to provide access to their local networks for originating and completing long distance calls.

²² *Order*, ¶ 905 (JA at 714).

The FCC failed to reclassify carrier access costs between jurisdictions as a corollary to these actions, however. Thus, states were still officially “left” with them in their intrastate allocations used for ratemaking.²³ The FCC never asked a Separations Joint Board to review the impacts of the proposal on existing separations rules and methodologies, or make recommendations on what shift in recovery, if any, in both revenues and expenses, was appropriate. The change had as much of an impact on separations as direct changes to the Part 36 rules themselves.

For these reasons, the Court should reverse and remand the FCC’s decision on issues impacting jurisdictional separations, and direct the FCC to refer the issues to a Separations Joint Board. The Court should direct the FCC to issue a new decision, based on the Separations Joint Board’s Recommended Decision.

²³ RBA notified the FCC that whatever means it adopted to reduce intrastate access charges would have separations implications that should be reviewed first by a Joint Board. Attachment to RBA Aug. 2011 Comments, at 26: “Under Section 410 of the Act, the appropriate initial process is the referral of this matter to the Federal-State Joint Board. Irrespective of whether the Commission is determined to achieve reductions in intrastate access charges through state preemption or alternatively pursues the provision of cooperative incentives to the states, the result will impact the jurisdictional separation of common carrier property and expenses between the state and federal jurisdiction.” (JA at 3230).

III. THE COMMISSION IRRATIONALLY REFUSED TO MODIFY SERVICE OBLIGATIONS FOR CARRIERS IT DENIED UNIVERSAL SERVICE SUPPORT.

As part of its overhaul of its USF regulations, the FCC decided it will no longer provide USF support to carriers serving any territory, regardless of cost, where voice and broadband service are available to customers from an “unsubsidized competitor.”²⁴ *Order*, ¶170 (JA at 456) (price cap territories), ¶283 (JA at 494-95) (RLEC territories).²⁵ Petitioners have argued that this was arbitrary and capricious because “unsubsidized competitors” have no obligation to provide service to all customers on demand. *See* Joint Universal Service Fund Principal Brief at 54-56. Assuming *arguendo*, however, that the FCC could properly eliminate support in these “overlap” territories, it committed further error by refusing to relieve Eligible Telecommunications Carriers (ETCs) of their ongoing duty to serve all comers without USF support.

²⁴ The FCC defined an “unsubsidized competitor” as “a facilities-based provider of residential terrestrial fixed voice and broadband service.” *Order*, ¶103 (JA at 428). Newly-adopted 47 C.F.R. §54.5 provides that “An ‘unsubsidized competitor’ is a facilities-based provider of residential fixed voice and broadband service that does not receive high-cost support.” Thus, the definition does not require qualification as an ETC, and does not exclude benefitting from other types of subsidies.

²⁵ In price cap territories, an ETC will be ineligible to receive support in CAF Phase II for any *census block* in which an “unsubsidized competitor” offers services. In RLEC territories, an ETC will be denied support, after a three-year transition period, only if one or more “unsubsidized competitors” serve an entire service area as designated under §214(e)(5).

Under the Act, the receipt of USF support comes with corresponding obligations. Any ETC designated under Section 214(e) must, throughout the service area for which the designation is received:

- (A) offer the services that are supported by Federal universal service support mechanisms under section 254(c) of this title ...; and
- (B) advertise the availability of such services and the charges therefor using media of general distribution.

47 U.S.C. §214(e)(1). Thus, an ETC must hold out its supported services indifferently to all potential customers. Conversely, only a carrier that is designated as an ETC, and thus accepts these obligations, may receive USF support. 47 U.S.C. §254(e). The service obligation is inextricably tied to the support.

The *Order* is contrary to Section 214 because it requires ETCs to provide services for which the carrier is not receiving, and cannot receive, support. The service obligation imposed by Section 214(e) does not apply to services that merely are authorized to receive support under Section 254(c); rather, it applies to services that actually “are supported by Federal universal service support mechanisms.” Contrary to this limitation, the *Order* maintains ETCs’ service obligations even in areas where they no longer will receive federal universal service support.

Further, the statute permits an ETC to relinquish its right to USF support, and its corresponding duty to serve, only if the state commission (or where

applicable the FCC) designates more than one ETC within the same service area. 47 U.S.C. §214(e)(4). In that case, the state commission must ensure that all customers served by the relinquishing carrier will continue to be served by one of the other ETCs. *Id.* This statutory structure leaves no room for doubt that Congress intended eligibility for support and the duty to serve to be two sides of the same coin.

The FCC arbitrarily and unlawfully severed this linkage by declaring that ETCs will no longer be eligible for support in any service area in which an “unsubsidized competitor” is operating, but will continue to be subject to the duties of an ETC. Significantly, the FCC does not require that the “unsubsidized competitor” be an ETC. This omission has two critical consequences. First, if the “unsubsidized competitor” were required to be an ETC, existing ETCs would have an opportunity to relinquish their status under Section 214(e)(4). If, however, an ETC loses support because of the presence of a non-ETC competitor, it is no longer “eligible” to receive support, but remains unable to relinquish the corresponding duty to serve.

Second, eliminating support in any service area in which an “unsubsidized competitor” is operating virtually ensures that ETCs will face escalating, and ultimately unsustainable, financial burdens. By definition, ETCs are subject to more costly obligations than their competitors. Under the *Order*, ETCs facing an

“unsubsidized competitor” in their service area are still required to advertise and offer basic voice services as a carrier of last resort throughout the entire area. In contrast, competitors who are not ETCs are free to engage in “cream-skimming,” serving only the low-cost parts of a service area. ETCs will not be able to cover the cost of their more comprehensive service obligations with increased rates, given both competitive and regulatory limits on end-user charges. *See* Joint Universal Service Fund Principal Brief at 43-44; *cf. Order*, ¶¶9-10 (JA at 396-97). Yet the *Order* removes universal service support while maintaining these obligations. This amounts to an unfunded mandate, which violates Section 254’s requirement that ETCs receive support that is sufficient. *See* 47 U.S.C. §254(e).

The FCC recognized this issue, but refused to deal with it. Instead, it sought comment in the Further NPRM section of the *Order* on suggestions that “the Commission should relax or eliminate ETCs’ voice service obligations” as it removes eligibility for support. *Order*, ¶1095 (JA at 790-91); *see also* ¶¶1096-1101 (JA at 791-93) (proposing to address these issues on a case-by-case basis through §214(e)(4) relinquishment process and forbearance under §10 of the Act, 47 U.S.C. §160).

It was arbitrary, capricious, unreasonable and contrary to law for the Commission to maintain the service obligations while eliminating support. Congress clearly intended these obligations and benefits to be complementary.

When the FCC decides that a carrier can no longer receive USF support for serving a particular area, that carrier is no longer “eligible” for support and can no longer be treated as an “eligible telecommunications carrier” subject to a duty to serve.

The Commission has created unnecessary tension and confusion for the states and providers by seeking comment on this issue rather than logically resolving an obvious paradox it has created through its misapplication of the law. Although an administrative agency has discretion as to how it manages its docket and the order in which it addresses issues, it abuses that discretion when it separates consideration of issues that logically must be decided together. “While there may well be circumstances where a particular objection is more properly deferred to a later proceeding, that is assuredly not the case where the objection goes to the heart of the public interest determination immediately to be made.”

Maryland Peoples’ Counsel v. FERC, 761 F.2d 768, 778 (D.C. Cir. 1985) (internal citation omitted). *See also Maier v. EPA*, 114 F. 3d 1032, 1039-1040 (10th Cir. 1997) (Court may review an agency’s refusal to initiate rulemaking if the decision rests on an insufficient legal predicate); *Sierra Club v. Gorsuch*, 715 F.2d 653, 658-59 (D.C. Cir. 1983) (Court’s review of agency decision to defer action on a particular issue should be deferential, but “must not be frustrated by *blind* acceptance” of agency’s claim that decision is still under study) (emphasis in original).

The ultimate effect of the *Order* is that ETCs facing an “unsubsidized competitor” in their service area will remain subject to costly unsupported service obligations, at least unless and until the Commission acts at some unspecified future time, in either its further rulemaking or some other proceeding, to relieve them of those obligations. Of course, there is no assurance that the outcome of the future proceedings will be to lift these obligations, so ETCs may remain subject to them indefinitely. This state of affairs is contrary to the intent of Congress as expressed in §214(e), and the Commission’s refusal to remedy it was arbitrary, capricious, unreasonable and contrary to law. Accordingly, the Court should vacate and remand the rules reducing support in areas served by an “unsubsidized competitor.”

IV. THE *ORDER*, AS APPLIED TO CERTAIN SMALL RURAL CARRIERS, IS UNCONSTITUTIONAL UNDER DUE PROCESS PRINCIPLES AND AS A BILL OF ATTAINDER, AND ALSO VIOLATES THE ACT, AND PRINCIPLES OF ESTOPPEL AND CONTRACT LAW.

A. Statement Of Additional Facts.

Allband Communications Cooperative (Allband) was created in 2003 by local residents seeking to obtain communications services in their heavily forested rural area located in four contiguous counties in northern Michigan, which never before had such services.

Upon adoption of the 1996 USF amendments to the Act, the local residents pursued their only option to obtain service, by creating a communications cooperative, and by obtaining a grant from Michigan State University (MSU) to further the project. Commencing in 2004, the Michigan Public Service Commission (MPSC) issued several orders granting Allband necessary licenses and ETC status. In 2005, the FCC approved Allband as an ILEC, an important step to obtain USF funding. Allband thereby assumed the responsibilities of an ILEC and ETC to provide a range of emergency and interconnection services essential to the public interest. Allband then received approval of an \$8 million loan from the USDA Rural Utility Service (RUS), premised upon receipt of USF revenues as security. Allband then constructed an advanced communications network, commencing partial service in late 2005. By 2010, Allband had constructed an efficient modern communications network that, for the first time, provided service to the residents in its large rural exchange area.

The annual USF funds provided to Allband comprise the bulk of the revenues necessary to make payments on Allband's RUS loans. Allband, its creditors, and the RUS, all relied upon the USF revenues as the financial security for payment of the RUS loans.

Allband made extensive filings in the subject FCC dockets establishing that the continuation of the existing level of USF funding (without imposition of the

Order's per-line reductions and expense limitations) are critical to Allband's survival. Without such USF support, Allband will be forced to close down, cease services, and default on its RUS loans, which inevitably would result in bankruptcy and the stranding of Allband's modern network providing service to the public.²⁶

B. Allband's Constitutional Rights Are Violated By the *Order*.

The *Order* is unlawful and beyond the jurisdiction of the Commission because it is contrary to the plain language of, and objectives and purposes of Congress underlying, the 1996 Act. The 1996 Act established the USF fund and program to promote the establishment of service in rural areas having no service, such as the area Allband now serves. Allband fully meets all of the provisions and purposes of the 1996 Act, such as the USF provisions of Section 254(b).

The *Order*, as it adversely impacts Allband, also contravenes the provisions, and the goals and objectives of Congress under Section 254(b)(5) and 254(d) of the Act, requiring "specific, predictable and sufficient... mechanisms to preserve and advance universal service"; and under Section 254(e) which requires that universal service support provided to ETC Providers "should be explicit and sufficient to achieve the purposes of this section."

²⁶ The FCC's Wireline Bureau (WLB), pursuant to delegated authority, issued an order dated July 25, 2012, granting Allband a 3-year waiver of the Order; on August 24, 2012, Allband filed an Application for Review of the WLB order, seeking a waiver of the Order for the duration of the RUS loans.

The *Order* imposes a drastic reduction in the per-line USF funding support to be provided some small rural companies such as Allband, and also established a “benchmark regression rule” which purports to impose limitations on capital and operations costs reimbursable from the USF. This rule operates pursuant to an economic model utilizing national variables, which are subject to change on a yearly basis. The model does not adequately consider the individual circumstances of each small rural company, or their service areas. The benchmark regression rule is thus hopelessly vague, unascertainable, uncertain, and arbitrary as applied to small companies such as Allband. The *Order* undermines confidence in the viability of Allband by local residents, employees, vendors, interconnecting carriers, and the financial community. This in turn degrades Allband’s opportunities to provide and expand services in its rural area, which thus contravenes the purposes of the 1996 Act and the USF program.

The *Order*, as applied to Allband, is also unconstitutional under the Due Process clause because (i) it imposes a retroactive reversal of Commission orders and USF program commitments upon which Allband (and the RUS) have relied in establishing Allband and in incurring capital costs, funded by the RUS loan, to construct its network, and (ii) because the expense reimbursement limitations under the ever-changeable “benchmark regression rule,” on a going-forward basis, are hopelessly vague and unascertainable. The *Order* thus fails to meet the

holdings and reasoning stated in *Federal Communications Commission, et al. v. Fox Television Stations, Inc.*, 132 S. Ct. 2307 (2012), wherein the Court held that Due Process is violated when FCC regulations are vague, and holding that “... clarity in regulation is essential to the protections provided by the Due Process Clause of the Fifth Amendment . . .” requiring . . . “the invalidation of laws that are impermissibly vague. . . .” The Court in *Fox* also ruled that a waiver option (or “policy of forbearance”) in the regulatory scheme does not absolve the constitutional defect.

A similar Due Process defect as found in *Fox* (vague and unascertainable regulatory standards and requirements) has been imposed by the *Order*, as applied to Allband. An even more egregious violation of Due Process has occurred here, however, because the *Order* goes beyond lack of advance notice and vagueness by effecting a retroactive reversal of prior orders and policies upon which there has been substantial reliance, coupled with the substitution of detrimental rules and policies on an unforeseen retroactive basis.

The *Order* is also unconstitutional as applied to Allband under the Fifth Amendment Due Process clause, as it would effect a confiscation of Allband’s (and its customer-members’ property), and will financially destroy commitments made by Allband to its employees, vendors, and entities providing credit and loans. The *Order* limits USF reimbursements relied upon by Allband to undertake long-

term capital investments and service obligations, and to cover expenses and to repay RUS loans. By ignoring these circumstances, the Commission as a ratemaking agency has acted contrary to the venerable precedent of the United States Supreme Court in *Bluefield Waterworks & Improvement Co. v. Public Service Comm'n of West Virginia*, 262 U.S. 679, 692-693; 42 S. Ct. 675 (1923), requiring regulatory action to provide a return ... “to assure confidence in the financial soundness of the utility and... to maintain and support its credit and enable it to raise the money necessary for the proper discharge of its public duties...” The *Order* is likewise contrary to *Federal Power Commission v. Hope Natural Gas Company*, 320 U.S. 591 (1944), wherein the Court held that the “return ... should be sufficient to assure confidence in the financial integrity of the enterprise, so as to maintain its credit and to attract capital.”

The *Order*, as applied to Allband, also constitutes an unconstitutional Bill of Attainder. The *Order*, including the April 25, 2012 “delegated” WLB Order limiting USF expense reimbursements under the “benchmark regression rule” threatens to reduce reimbursement funding from the USF, crippling Allband and a small class of similar rural carriers which relied on the 1996 Act’s USF. The *Order* punishes Allband for pursuing the Act’s opportunities and violates Allband’s Fifth Amendment and other Due Process protections. The *Order* effectively targets a small class of companies for differential treatment as being outside of the so-called

“market-based” economic model favored by the Commission. Such treatment and similar punishments have been reversed by the U. S. Supreme Court in *United States v Lovett*, 328 U.S. 303, 315 (1946) and more recently in *United States v Brown*, 381 U.S. 437 (1965). In *Lovett* and *Brown*, the Court did not hesitate to reverse as Bills of Attainders governmental orders which selectively denied petitioners their fundamental constitutional rights.

The *Order*, as applied to Allband, is also unlawful and arbitrary because it is irrational to the extreme. The *Order’s* imposition of per-line reductions and expense limitation reimbursements under the USF program (i) are not supported by the plain language of the Act; (ii) retroactively reverses purposes and objectives of Congress in the 1996 Act as noted, and (iii) ignores the direct reliance on the USF by Allband, the RUS, the MPSC, and agencies administering the USF program. The *Order* should be reversed as applied to Allband based upon estoppel principles.

The *Order* is also arbitrary because it fails to recognize that the destructive impacts upon Allband (or similar small rural carriers) are wholly unnecessary to achieve the stated goals or objectives of the *Order*. The *Order’s* suggestion that it seeks to curtail the unchecked growth of the USF is not accomplished by reducing

Allband's USF funding, and by destroying Allband and its services.²⁷ The *Order's* stated goal to reduce waste and inefficiency, or to conserve the USF budget, also is *not* accomplished by punishing Allband. There exists no evidence of waste or inefficiency attributable to Allband. The July 25, 2012, WLB order granting Allband a 3-year waiver from the *Order* expressly found the opposite—acknowledging that Allband was a lean and efficient operation, providing reliable service in a rural area in accordance with the public interest.

The *Order* also arbitrarily failed to consider Allband's assertions that the USF funding should not be reduced as applied to already invested capital and expenses incurred in reliance on the USF, and at most, should apply only to *prospective* investment incurred after the *Order*. Allband cannot retroactively pull out already constructed plant, or cancel maintenance, depreciation, taxes, and related expenses on such plant, or alter decisions made in the past. A rational, non-arbitrary order would recognize that a lawful and constitutional order can and should only apply to investment and expense decisions made on a prospective basis, on and after the *Order* is effective.

²⁷ Allband's USF funding of about \$1.3 million constitutes an imperceptible portion of the multi-billion USF annual budget. The combined amount saved from imposing the Order's \$3,000 per line cap, on *all* companies in the United States, also constitutes a *negligible* portion of the annual USF budget (as documented by calculations in Allband filings using Exhibit B of the April 25, 2012 WLB Order).

The *Order* is also unlawful and arbitrary because, besides destroying Allband and its services, and stranding its recently constructed network, the *Order* will cause a prompt default by Allband of its RUS loan contracts and obligations. The *Order* wholly ignores that the pre-*Order* USF revenue stream was relied upon by both Allband and the RUS to pay back the RUS loans. The *Order* would thus undercut the loan programs of a sister agency of the federal government. This retroactive reversal of policy, and resulting impacts, has been ruled unlawful in an analogous context in *United States v Winstar Corp*, 518 U.S. 839 (1996). In that case, the plaintiffs were awarded substantial damages against the United States in a similar situation. In Allband's situation, however, the pursuit of damages on a post-loan default basis, after cessation of operations to the public, would be clearly inadequate. In order for Allband to continue service and to uphold its loan obligations to the RUS, Allband asserts that reversal of the FCC *Order* as applied to Allband is necessary and far more appropriate.

The *Order* is also unlawful and beyond the jurisdiction of the FCC because it intrudes much too far into the economic market place. The *Order* serves to pick “winners and losers” among companies—to force Allband and perhaps other small carriers established under the USF out of business and into bankruptcy, perhaps with an unwarranted windfall to the same large powerful companies which refused for decades to provide service in the subject rural service areas. Allband asserts

that the FCC's jurisdiction does not go this far, and that the attempted unilateral assumption of such power is neither lawful nor necessary. Regulation does not entail the power to destroy.²⁸

CONCLUSION

For the reasons stated above, this Court should reverse and/or remand the *Order* and vacate it in its entirety.

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

July 11, 2013

On behalf of the Joint Petitioners
listed on the cover of this filing²⁹

²⁸ The Court in *Pennsylvania Coal Co v. Mahon*, 260 U.S. 393, 415 (1922), held the government may effect a taking without physical occupation or appropriation if it “goes too far . . .” The “power to regulate is not a power to destroy . . .” *Stone v. Farmers’ Loan and Trust Co*, 116 U.S. 307, 331 (1886); *see also*, *Covington & Lexington Tpk. Rd. Co. v. Sandford*, 164 U.S. 578, 597 (1896). The Court in *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1015 (1992), held a non-possessory regulation may constitute a per se taking if it deprives the owner of “all economically beneficial or productive use of land.”

²⁹ Rural Independent Competitive Alliance joins only in Section I; the National Association of Regulatory Commissioners, Arizona Corporation Commission, Vermont Public Service Board and Rural Telephone Service Co. *et al.* join only in Section II; Consolidated Communications Holdings, Inc. and CenturyLink, Inc. join only in Section III; and Allband Communications Cooperative joins only in Section IV of this brief.

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 Amended First Briefing Order because it contains 7,785 words exclusive of any citations to the Joint Appendix or Supplemental Joint Appendix and 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 July 11, 2013, and according to the program is free of viruses.

/s/ Harvey L. Reiter

July 11, 2013

CERTIFICATE OF SERVICE

I hereby certify that, on November 6, 2012, per the Court's order of July 11, 2013, 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

July 11, 2013