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IN THE UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

NO. 11-9900

IN RE: FCC 11-161

ON PETITION FOR REVIEW OF ORDERS OF THE
FEDERAL COMMUNICATIONS COMMISSION

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GLOSSARY

1996 Act	The Telecommunications Act of 1996
Act	The Communications Act of 1934
APA	The Administrative Procedure Act
ARC	Access Recovery Charge
COLR	Carrier of Last Resort
ETC	Eligible Telecommunications Carrier
FCC	Federal Communications Commission
FNPRM	Further Notice of Proposed Rulemaking
HCLS	High-Cost Loop Support
LEC	Local Exchange Carrier
NPRM	Notice of Proposed Rulemaking
SNA	Safety Net Additive
USF	Universal Service Fund
VoIP	Voice over Internet Protocol
WCB	Wireline Competition Bureau

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ON PETITIONS FOR REVIEW OF ORDERS OF THE
FEDERAL COMMUNICATIONS COMMISSION

FEDERAL RESPONDENTS FINAL RESPONSE TO THE
JOINT UNIVERSAL SERVICE FUND
PRINCIPAL BRIEF OF PETITIONERS

ISSUE PRESENTED

Whether the Federal Communications Commission ("FCC") lawfully reformed its universal service rules to efficiently enhance access to broadband in rural America.

INTRODUCTION AND SUMMARY OF ARGUMENT

The FCC, in the *Order* on review, took the necessary steps to modernize its universal service program. *See Connect America Fund*, 26 FCC Rcd 17663 (2001) ("*Order*") (JA at 390-1141). Finding that "[n]etworks that provide only voice service … are no longer adequate for the country's communication needs," *Order* ¶2 (JA at 394), the FCC reoriented

the federal high-cost universal service program to support dual-use networks capable of providing voice as well as broadband service to all Americans. *See* FCC Preliminary Br. 21-22.

Seeking to preserve the *status quo*, petitioners raise at least twelve issues. Br. 1-3. They claim that the FCC lacked authority to reform its universal service rules, violated various provisions of the Communications Act of 1934 ("Act"), engaged in unreasoned decision-making in violation of the Administrative Procedure Act ("APA"), and failed to follow proper procedures. As explained below, these claims are baseless, and many are not properly presented.

I. Petitioners broadly assert that the FCC lacked statutory authority to enact universal service reform. Petitioners' various challenges rest on the assertion that Congress fenced off "information services" (*see* FCC Preliminary Br. 8 n.6) – notably, broadband Internet access – from the universal service program. Petitioners are wrong.

A. The FCC reasonably determined that section 254 of the Act, 47 U.S.C. §254, authorized the agency to provide federal universal service support for broadband-capable networks.

The FCC has a "mandatory duty" to "base its universal [service] policies on the principles listed in §254(b)" of the Act. *Qwest Corp. v. FCC*,

258 F.3d 1191, 1200 (10th Cir. 2001) ("*Qwest I*"). Among those principles are that "[a]ccess to advanced telecommunications and information services should be provided in all regions of the Nation," and that "[c]onsumers in all regions of the Nation … should have access to telecommunications and information services … that are reasonably comparable to those services provided in urban areas" and at reasonably comparable rates. 47 U.S.C. §254(b)(2), (3).

After evaluating the record evidence, the FCC found that the achievement of the section 254(b) principles requires carriers to deploy networks capable of providing consumers with access to both voice and broadband services. The FCC concluded that it was authorized to advance those principles by 47 U.S.C. §254(e), which requires recipients of support from the federal universal service fund ("USF") to "use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended." Because "facilities" and "services" are distinct terms, the FCC reasoned that, through section 254, Congress granted the agency authority to support the "telecommunications services" designated under 47 U.S.C. §254(c)(1) *and* the facilities necessary to achieve the principles in section 254(b). In fact, in the decade prior to the *Order*, the FCC permitted (but did not require) the recipients of high-cost universal

service support to invest in "dual-use" facilities that provide voice as well as broadband services. Consistent with that long-standing policy, the FCC in the *Order* conditioned a carrier's receipt of federal universal service support under section 254 on the deployment of a broadband-capable network. To ensure that USF recipients use support for that purpose, the FCC further required them to offer broadband service that meets certain basic performance requirements.

1. Petitioners claim that the FCC lacks authority to fund broadband facilities because, in their view, section 254(e)'s use of the phrase "for which the support is intended" must be construed as referring to the "telecommunications services" deemed eligible for support under section 254(c)(1). But the FCC reasonably interpreted that clause to refer to the universal service principles in section 254(b) of the Act. This reading gives full effect to section 254. Indeed, under petitioners' reading, the FCC could not achieve the mandatory principles in section 254(b)(2) and (3) – which include "[a]ccess to advanced telecommunications and *information services* … in all regions of the Nation." 47 U.S.C. §254(b)(2) (emphasis added). The FCC was not required to adopt an interpretation of the statute that disabled the agency from achieving the purposes Congress assigned to it. Such a reading is not reasonable, much less mandated.

2. To ensure that universal service support is being used to deploy broadband facilities, the FCC further required USF recipients to provide broadband Internet access service – a public interest obligation that was a valid and necessary exercise of the agency's judicially affirmed authority to impose conditions on federal subsidies. Further, because the public interest obligation is conditional (*i.e.*, carriers need only provide broadband if they voluntarily seek federal universal service support), it does not amount to common carrier "regulation" under Title II of the Act, 47 U.S.C. §201 *et seq*., as petitioners allege.

3. While petitioners assert that the *Order* distributes universal service support to entities that are not "telecommunications carriers" and provide no "telecommunications services," that claim will not be ripe for judicial review unless and until a state commission (or the FCC) designates such an entity an "eligible telecommunications carrier" ("ETC"). *See* 47 U.S.C. §214(e)(2), (6). But even under petitioners' theory, a provider of Voice over Internet Protocol ("VoIP"), an "unclassified" service, could be eligible for such support if it voluntarily offers VoIP as a "telecommunications service" – a practice that the FCC has sanctioned in prior orders and that occurs in the marketplace today.

B. The FCC concluded that it has independent authority under section 706 of the Telecommunications Act of 1996 ("1996 Act"), 47 U.S.C. §1302, to support broadband networks and services. That provision empowers the FCC to "take immediate action to accelerate deployment of such capability by removing barriers to infrastructure investment and by promoting competition in the telecommunications market." 47 U.S.C. §1302(b). Evidence in the record showed that support for broadband helps achieve both those statutory objectives. The FCC separately found that its exercise of authority under section 706 helps fulfill the objectives in section 254(b), notably the principle that "[a]ccess to advanced telecommunications and information services should be provided in all regions of the Nation." 47 U.S.C. §254(b)(2).

II. The FCC, for the first time, established an annual funding target for the high-cost component of the USF. Relying on its predictive judgment, the FCC found that setting the target at $4.5 billion annually would provide sufficient support to ensure affordable and reasonably comparable voice and broadband service.

Contrary to petitioners' claims, the FCC carefully calibrated the impact of universal service reform on incumbent local exchange carriers ("LECs") subject to rate-of-return regulation. It maintained high-cost support for those

carriers at existing levels (about $2 billion annually), and required them to extend facilities to customers only upon a reasonable request for service. The FCC estimated that almost one-half of all rate-of-return carriers would see no change or an increase in federal support, and of those expected to experience a reduction, the majority would see reductions of fewer than 10 percent of their annual subsidies. The FCC also provided a waiver process under which carriers may receive exemptions from these reductions if they are able to demonstrate that support reductions would imperil their financial viability and threaten service to consumers. The availability of that waiver process undercuts petitioners' arguments that the *Order* (1) provides insufficient support for purposes of sections 254(b)(5) and (e) of the Act, *see Rural Cellular Ass'n v. FCC*, 588 F.3d 1099, 1104 (D.C. Cir. 2009) ("*RCA I*"); and (2) effects an unconstitutional taking of property, *see Williamson County Reg'l Planning Comm'n v. Hamilton Bank*, 473 U.S. 172, 194 (1985).

III. To eliminate waste and inefficiency in universal service support to rate-of-return carriers, the FCC limited those carriers' recovery of certain capital and operating expenses. Petitioners have waived their various challenges to this rule because they never presented them to the FCC. *See* 47 U.S.C. §405(a). The challenges lack merit in any event. Petitioners' primary complaint is that the new rule will produce unpredictable funding amounts,

allegedly in violation of 47 U.S.C. §254(b)(5). But that provision of the Act only requires predictable rules, not outcomes. *See Alenco Commc'ns, Inc. v. FCC*, 201 F.3d 608, 622 (5th Cir. 2000). Moreover, it has always been the case that carriers will not know how much support they will receive in future periods, so the new rule adds no uncertainty to USF disbursements.

Separately, petitioners argue that the FCC engaged in impermissible retroactive rulemaking. Not so. There is no "primary retroactivity" because the *Order* only reduces universal service support prospectively. Even if the *Order* were retroactive in effect (which it is not), there is no "secondary retroactivity" because the FCC's decision to amend its rules was reasonable and thus lawful.

IV. The FCC also overhauled the support mechanisms for incumbent LECs subject to price cap regulation. To spur broadband deployment, over and above what price cap carriers had already planned, the FCC offered additional high-cost support, on a one-time basis, to areas currently lacking broadband service. Having adequately explained its decision to jump-start broadband deployment in previously unserved areas rather than subsidize service upgrades in areas that already have access to broadband, the FCC was not required to separately respond to petitioners' objections to that limitation.

Nor was the FCC required to address petitioners' arguments that using an auction mechanism to eventually distribute subsidies to price cap carriers will degrade service and disadvantage small telecommunications carriers. The *Order* merely stated the FCC's intention to use an auction mechanism. In an attached Further Notice of Proposed Rulemaking ("FNPRM"), the FCC sought comment on how best to design and implement it – including comment on the issues of concern to petitioners. Until the FCC acts on the FNPRM, petitioners' claims that the mechanism will degrade service or harm small carriers are not ripe.

V. Petitioners launch a scattershot attack on various other reforms designed to more efficiently and cost-effectively support voice and broadband with federal universal service funding. Many of these perfunctory and often underdeveloped claims are waived or unripe; they all lack merit.

A. In response to record evidence showing that a number of USF recipients charge artificially low rates, the FCC adopted a rule that reduces federal subsidies to carriers with rates below a specified floor so as not to burden consumers who ultimately make universal service contributions. While petitioners complain that the new rule has the *de facto* effect of setting local rates in violation of 47 U.S.C. §152(b), courts have made clear that an incidental effect on rates does not mean that the FCC is "regulating" rates.

See Cable & Wireless PLC v. FCC, 166 F.3d 1224, 1230 (D.C. Cir. 1999). Moreover, FCC adoption of measures that encourage states to adjust local rates is not only permissible, it is sometimes required to ensure that states assist in implementing the universal service goals in section 254 of the Act. *See Qwest I*, 258 F.3d at 1203-04; *Qwest Commc'ns Int'l., Inc. v. FCC*, 398 F.3d 1222, 1238 (10th Cir. 2005) ("*Qwest II*").

B. The FCC also eliminated support in areas served by an unsubsidized competitor. Petitioners predict that this will threaten customers, because an unsubsidized competitor (unlike the incumbent LEC) has no legal obligation to provide voice and broadband service. But the FCC reasonably predicted that unsubsidized competitors would have business incentives to maintain service in areas they serve today, and thus declined to fund duplicative networks where market forces are already sufficient to ensure consumer access to voice and broadband services. That sensible determination is entitled to substantial deference.

C. To spur the deployment of mobile wireless services, the FCC decided to use competitive bidding to distribute $300 million in one-time high-cost support to wireless carriers in certain designated areas. Petitioners argue that this mechanism usurps state commission authority under 47 U.S.C. §214(e), but they conflate eligibility for subsidies with the right to receive

subsidies. Nothing in the *Order* limited the states' authority under section 214(e) to determine who is eligible for support, and where they are eligible for support. Such state eligibility determinations are still a precondition to receiving support, but no carrier is entitled to receive federal universal service support simply by virtue of these state determinations.

D. The FCC decided to transition support for the most remote areas of the nation to a newly created fund. The *Order* set aside $100 million annually for that effort but sought comment on how to distribute support in the attached FNPRM. Contrary to petitioners' suggestion, until those distribution rules are in place, extremely high-cost areas will continue to receive support under existing mechanisms for price cap and rate-of-return carriers. When the FCC creates the new Remote Areas Fund, petitioners may, if they are aggrieved, challenge that new mechanism. Until then, their claim is not ripe and, in any event, meritless.

VI. Petitioners complain that certain key provisions of the *Order* did not comply with the notice-and-comment requirements of the APA. That argument is not properly before the Court, because it was not first presented to the FCC through a petition for reconsideration. It also lacks merit, because the FCC sought comment on all of the challenged provisions.

VII. Finally, the FCC reasonably decided to address in a separate proceeding the issue of universal service contributions. This action was well within the agency's discretion to define the scope of its own proceedings and to proceed incrementally.

ARGUMENT

I. THE FCC REASONABLY DETERMINED THAT THE STATUTE AUTHORIZES THE UNIVERSAL SERVICE REFORMS IN THE ORDER.

A. The FCC Reasonably Concluded That It Has Authority Under Section 254 Of The Act To Condition Receipt Of Federal Universal Service Subsidies On Deployment Of Broadband-Capable Networks.

"'The public switched telephone network is not a single-use network.'" *Order* n.70 (JA at 412-413) (quoting *Federal-State Joint Board on Universal Service*, 16 FCC Rcd 11244, 11322 (¶200) (2001) ("*Rural Task Force Order*")). Rather, "'[m]odern network infrastructure can provide access not only to voice services, but also to data, graphics, video, and other services.'" *Id*. Thus, in the *Rural Task Force Order*, the FCC established the "no barriers" policy. *Order* ¶¶64, 308 (JA at 412-413, 502-503). For more than a decade, this 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. *Id*.

The FCC, in the *Order*, found that section 254(e) of the Act allowed it to "go beyond the 'no barriers' policy" to "require carriers receiving federal universal service support to invest in modern broadband-capable networks." *Id*. ¶65 (JA at 413-414); *see also* ¶308 (JA at 502-503). Petitioners now contend that the FCC lacked authority to make that once-permissive policy mandatory. Br. 21-22.

The FCC properly rejected petitioners' view in the *Order*, explaining 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" as occurred under the "no barriers" policy. *Order* ¶65 (JA at 413-414). "To the contrary, [the FCC] ha[s] a 'mandatory duty' to adopt universal service policies that advance the principles … in section 254(b), and … the authority to 'create some inducement' to ensure that those principles are achieved." *Id*. (quoting *Qwest I*, 258 F.3d at 1200, 1204). Two of those principles identify access to information services as an integral component of universal service. *See* 47 U.S.C. §254(b)(2), (3). By conditioning support on the deployment of a broadband-capable network, the *Order* lawfully sought to "induce" the recipients of federal universal service subsidies to "advance" the principles in section 254(b). In this regard, petitioners' argument that the section 254(b) principles are merely

"aspirational language" (Br. 16) is squarely foreclosed by *Qwest I*, 258 F.3d at 1200 (explaining that "[t]he plain text of the statute mandates that the FCC 'shall' base its universal policies on the principles listed in § 254(b)," which "indicates a mandatory duty on the FCC"); *see also* FCC Response to Wireless Carrier USF Principal Br. 11.

Despite the FCC's precedent authorizing support for broadband facilities, petitioners contend that because the phrase "facilities and services" in section 254(e) is modified by the clause "for which the support is intended," the FCC may only require USF recipients to deploy facilities that are used to provide the "telecommunications services" deemed eligible for support pursuant to section 254(c)(1). Br. 22-23. According to petitioners, this prohibits the FCC from conditioning federal universal service support on the deployment of broadband-capable networks.

As the FCC explained, however, "[b]y referring to 'facilities' and 'services' as distinct items for which federal universal service funds may be used, … Congress granted [the FCC] the flexibility not only to designate the types of telecommunications services for which support would be provided, but also to encourage the deployment of the types of facilities that will best achieve the principles set forth in section 254(b)." *Order* ¶64 (JA at 412-413); *see id.* ¶308 (JA at 502-503). Limiting support to the facilities used to

provide the section 254(c)(1) services, as petitioners argue the FCC must, would conflate "services" with "facilities," rendering the latter term "superfluous." *See Nutraceutical Corp. v. Von Eschenbach*, 459 F.3d 1033, 1040 (10th Cir. 2006) (holding that because "[t]he rule against surplusage encourages courts to give meaning to every word used in a statute to realize congressional intent," the district court erred by conflating "significant risk" with "unreasonable risk" – "a distinct term"); *see also Bowoto v. Chevron Corp.*, 621 F.3d 1116, 1127 (9th Cir. 2010) (when a statute uses distinct terms, a court "must … presume those terms have different meanings").[1]

The FCC thus reasonably interpreted the phrase "for which the support is intended" in section 254(e) to reference the universal service principles in section 254(b). *Order* ¶¶64, 308 (JA at 412-413, 502-503). This reading properly gives full effect to both section 254(b) and section 254(c)(1) of the Act. *See In re Dawes*, 652 F.3d 1236, 1242 (10th Cir. 2011) (statutes should be construed so that no part will be inoperative or superfluous). Petitioners'

[1] Petitioners incorrectly read the *Order* to define the "facilities" supported by section 254(e) as limited to those used to provide only the "telecommunications services" designated under section 254(c)(1). *See* Br. 22-23 (citing *Order* n.69 (JA at 412)). As the FCC explained, "Section 254(e) … contemplates that carriers may receive federal support to enable the deployment of broadband facilities used to provide supported telecommunications services *as well as* other services." *Order* ¶64 (JA at 412-413) (emphasis added).

narrow and exclusive focus on "telecommunications services" ignores the FCC's obligation to achieve the section 254(b)(2) and (3) principles, which include "[a]ccess to advanced telecommunications and *information services* … in all regions of the Nation." 47 U.S.C. §254(b)(2) (emphasis added). The agency cannot satisfy that obligation if section 254(c)(1) prohibits the FCC from conditioning a recipient's use of federal subsidies on the deployment of a single network capable of supporting both telecommunications services and information services. Indeed, the prior, permissive "no barriers" policy failed to sufficiently achieve those objectives. *See* FCC Preliminary Br. 15. It follows that petitioners' interpretation of the statute is not reasonable – much less mandated – because it would disable the FCC from achieving the explicit statutory goals regarding information services.

Petitioners' interpretation also ignores the FCC's duty to "advance" universal service. *See* 47 U.S.C. §254(b); *Qwest II*, 398 F.3d at 1236. Their proposal to "limit[] federal support based on the regulatory classification of the services offered … would exclude from the universal service program providers who would otherwise be able to deploy broadband infrastructure to consumers." *Order* ¶72 (JA at 417-418). That infrastructure is used to provide new services, such as VoIP, which are "viewed by consumers as substitutes for traditional voice telephone services." *Id.* ¶63 (JA at 412).

Thus, requiring USF recipients to deploy networks capable of providing voice *and* broadband services "advances" universal service, whereas merely requiring recipients to deploy networks capable of providing traditional circuit-switched voice services would only "preserve" the *status quo*.

If, as petitioners claim (Br. 22-23), the FCC may support facilities only to the extent that they are used to provide telecommunications services, then allowing ETCs to expend universal service subsidies to deploy facilities used to provide broadband Internet access, even on a permissive basis, would have violated the Act. Hence, under petitioners' reading, the long-standing, permissive "no barriers" policy, which petitioners themselves supported in proceedings before the agency, would be unlawful.[2] In conflict with their legal position here, however, it is clear that petitioners do not oppose federal

[2] *See, e.g.*, Comments of the National Exchange Carrier Association, Inc.; National Telecommunications Cooperative Association; Organization for the Promotion and Advancement of Small Telecommunications Companies; and Western Telecommunications Alliance, WC Docket 10-90 *et al.* at 64-65 (filed Apr. 18, 2011) (JA at 2214-2215) (encouraging the FCC to "recognize that the current high-cost support mechanisms have enabled great success in broadband deployment and adoption in R[ural] LEC study areas" and specifically that "the 'no barriers to advanced services' policy … has allowed R[ural] LECs to use USF support in a forward-looking manner to construct multi-use networks that support both quality voice *and* broadband offerings"); *see also id.* n.135 (JA at 2215) (explaining that "there is no question that support can be distributed for mixed-use plant that supports both Title I broadband Internet access and Title II regulated telecommunications services").

universal service support that may be *used* for broadband deployment; rather, they oppose federal support *conditioned* on broadband deployment. In other words, petitioners want subsidies without the obligation. But this Court has already held that the FCC is not required to provide petitioners' hoped for "blank check." *See Qwest I*, 258 F.3d at 1204.[3]

B. The FCC Reasonably Concluded That It May Condition Federal Universal Service Subsidies On A Recipient's Compliance With Clearly Defined Public Interest Obligations.

Section 254(c)(1) of the Act defines "[u]niversal service" as "an evolving level of telecommunications services that the Commission shall establish periodically under this section, taking into account advances in telecommunications and information technologies and services." Petitioners argue that "the Commission [wa]s not … empowered to include" VoIP and broadband Internet access "on the list of supported services" designated under section 254(c)(1) because they are not "telecommunications services." Br. 14. Petitioners, however, mischaracterize the *Order*, which provides universal service support for (1) "voice telephony service" and (2) broadband-capable networks. To ensure that support is being used for the

[3] We address in section I.C., below, petitioners' separate claim that the FCC lacks authority to fund broadband-capable networks on the ground that the *Order* does not require USF recipients to provide telecommunications services. Br. 21-22.

latter, the FCC further required USF recipients to provide broadband Internet access service – a public interest obligation that was a valid and necessary exercise of the agency's judicially affirmed authority to impose funding conditions.

1. The *Order* Does Not Fund Information Services Under Section 254 Of The Act.

Pursuant to the *Order*, "voice telephony service" is the only supported service for purposes of section 254(c)(1).[4] *Order* ¶¶62, 80, 309 (JA at 411, 420, 503). "To the extent [ETCs] offer traditional voice telephony services as telecommunications services over traditional circuit-switched networks, [the FCC's] authority to provide support for such services is well-established." *Id*. ¶62 (JA at 411); *see also* 47 U.S.C. §254(c)(1).

Petitioners attack the *Order*'s inclusion of VoIP – an "unclassified service" (*i.e*., a service that the FCC has not classified either as a "telecommunications service" or an "information service") – in the definition of "voice telephony service." Br. 13-15. As the FCC explained, however,

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[4] Petitioners claim that "the Order fails to discuss how its new 'voice telephony service' definition takes … into account" any of the four factors listed in section 254(c)(1). Br. 56. This claim is barred because petitioners failed to raise it in the proceeding below or in a subsequent petition for reconsideration of the *Order*. *See Sorenson Commc'ns, Inc. v. FCC*, 659 F.3d 1035, 1044 (10th Cir. 2011) ("*Sorenson II*"); 47 U.S.C. §405(a). In any event, the *Order* did discuss these factors at length. *See Order* ¶¶61-65, 68-69, 71-72, 76-81 (JA at 411-414, 415-416, 417-418, 418-420).

"[i]f interconnected VoIP services are telecommunications services," the agency can designate them as eligible for support pursuant to section 254(c)(1). *Order* ¶63 n.67 (JA at 412). Alternatively, if "interconnected VoIP services are information services, [the FCC] ha[s] authority to support the deployment of broadband networks used to provide such services" under sections 254(b)(2)-(3) and (e). *Id.* In the latter circumstance, VoIP is not a "telecommunications service" supported by section 254(c)(1); it is one of the "other services" offered across "broadband facilities used to provide supported telecommunications services." *Id.* ¶64 (JA at 412-413).

2. The Broadband Public Interest Obligation Is A Lawful Condition On Federal Universal Service Support.

Petitioners likewise fail to show that the FCC, acting under section 254, authorized federal universal service support for broadband Internet access service itself. Br. 11-16. Indeed, the FCC expressly declined to "add broadband to the list of supported services" under section 254(c)(1). *Order* ¶¶65, 309 & n.514 (JA at 413-414, 503). Instead, it merely conditioned the receipt of support on a carrier's deployment of a broadband-capable network pursuant to sections 254(b) and (e). *Id.* ¶65 (JA at 413-414).

Petitioners counter that the *Order* (at ¶86 (JA at 422)) had that effect when, "[a]s a condition of receiving federal high-cost universal service support," it required funding recipients "to offer broadband service … that

meets certain basic performance requirements and to report regularly on associated performance measures." Br. 23-24. Petitioners' argument ignores the fact that "[n]othing in section 254 prohibits the Commission from *conditioning* the receipt of [universal service] support, and the Commission has imposed conditions in the past." *Connect America Fund*, 26 FCC Rcd 4554, 4581 (¶71 & n.103) (2011) (emphasis added) ("NPRM") (citing 47 C.F.R. §§54.313(a)-(b), 54.314(a)-(b) (SJA at 28); *see also United States v. Am. Libraries Ass'n, Inc.*, 539 U.S. 194, 211 (2003).

As the FCC explained, "[u]niversal service support is a public-private partnership," and carriers "that benefit from public investment in their networks must be subject to clearly defined obligations associated with the use of such funding." *Order* ¶74 (JA at 418). Courts have recognized this proposition in denying similar challenges to conditions on federal subsidies. *See Am. Libraries Ass'n*, 539 U.S. at 211-13 (upholding the requirement that public libraries use Internet filters as a condition on receipt of federal universal service subsidies); *Qwest II*, 398 F.3d at 1238 (affirming the FCC's authority to condition universal service support on state commission certification that local telephone rates are "reasonably comparable"); *Tex. Office of Pub. Util. Counsel v. FCC*, 183 F.3d 393, 444 (5th Cir. 1999) ("*TOPUC*") (affirming the FCC's authority to condition federal universal

service support on state-established discount rates for intrastate services provided to schools, libraries, and rural health care providers). Absent the performance metrics and rate comparisons set forth in paragraphs 90-114 of the *Order* (JA at 423-436), the FCC would have no means to ensure that federal universal service subsidies are being used, as required by section 254(b)(1)-(3) of the Act, to deploy "in all regions of the Nation" networks capable of providing affordable voice and broadband services that are reasonably comparable – in terms of quality and rates – to voice and broadband services in urban areas, *see Order* ¶¶87, 91, 106, 113 (JA at 422, 423, 430, 435).[5]

3. The Broadband Public Interest Obligation Does Not Constitute Title II Common Carrier Regulation.

Petitioners separately argue that the broadband public interest obligation "essentially forc[es]" USF recipients "to offer … information service[s] as a common carrier service." Br. 23. That claim is contrary to

[5] Petitioners contend that the agency cannot confirm that the *Order* will produce "reasonably comparable" broadband Internet access service because the agency has never compared broadband rates and service quality between urban and rural areas. Br. 33-34. The FCC directed its staff to gather the data needed to make this determination. *See Order* ¶¶113, 1018 (JA at 435, 773). Because agencies may proceed incrementally, the FCC was not required to complete this effort before adopting the *Order*. *See, e.g.*, *Sorenson Commc'ns, Inc. v. FCC*, 567 F.3d 1215, 1222 (10th Cir. 2009) ("*Sorenson I*").

this Court's precedent in *WWC Holding Co. v. Sopkin*, 488 F.3d 1262, 1268, 1274 (10th Cir. 2007), which held that a state commission could condition a wireless carrier's ETC designation on compliance with some of the "consumer protection and operational standards" imposed on incumbent LECs. As the Court explained, funding conditions commensurate with the requirements imposed on common carriers do not amount to common carrier "regulation," because providers voluntarily assume the conditions in the first instance and "retain[] the ability to opt out of [them] entirely by declining … federal universal service subsidies." *Id*. at 1274. Because the broadband public interest obligation is conditional (*i.e*., carriers only have to provide broadband service to a customer if they request federal subsidies), it does not amount to "regulation" of any sort.

Moreover, the *Order* does "not extend[] the gamut of telephone regulations" under Title II of the Act to broadband Internet access service; it simply requires providers that "approach[] the [FCC] to receive federal universal service subsidies" (*id*.) "to offer broadband service … that meets certain basic performance requirements and to report regularly on associated performance measures," *Order* ¶86 (JA at 422). Petitioners have failed to demonstrate that those modest requirements correspond to any, let alone all,

of the requirements that Title II imposes on common carriers. Br. 23. They do not.

But even if that were not the case, "common carriage is not all or nothing – there is a gray area in which although a given regulation might be applied to common carriers, the obligations imposed are not common carriage *per se*." *Cellco P'ship v. FCC*, 700 F.3d 534, 547 (D.C. Cir. 2012). Accordingly, "the Commission's determination" that the broadband public interest obligation "does not confer common carrier status warrants deference" from the Court. *Id*.

C. Petitioners' Claim That The *Order* Violates Sections 254(e) And 214(e) Of The Act Is Not Ripe And Lacks Merit.

Petitioners further argue that the *Order* violates sections 254(e) and 214(e) of the Act because "it distributes USF support to entities that are not telecommunications carriers and provide no telecommunications services." Br. 5, 17-18, 22. Petitioners' claim should be dismissed because it is not ripe. In any event, it is wrong.

1. Pursuant to section 254(e), only "eligible telecommunications carriers," *i.e.*, those entities designated under section 214(e), "shall be eligible to receive specific Federal universal service support." 47 U.S.C. §254(e). Section 214(e)(1), in turn, provides that "a common carrier designated as an

eligible telecommunications carrier … shall be eligible to receive universal service support in accordance with section 254." *Id.* §214(e)(1). "[T]he states designate common carriers over which they have jurisdiction as ETCs, and th[e] [FCC] designates common carriers as ETCs in those instances where the state lacks jurisdiction." *Order* ¶570 (JA at 576); *see* 47 U.S.C. §214(e)(2), (6).

The FCC, in the *Order*, reformed the larger framework for distributing federal universal service subsidies; it did not find that any particular service provider, or category of providers, would be eligible for support under this new framework. Br. 18. ETC designation under sections 214(e)(2) and (6), which is a pre-requisite for the receipt of federal subsidies, is an "inherently local and fact-specific" process. *WWC Holding Co*., 488 F.3d at 1278; *Federal-State Joint Board on Universal Service*, 20 FCC Rcd 6371, 6397 (¶61) (2005). For a "non-telecommunications carrier to use USF support for unregulated information services" (Br. 18), a state commission (or, in limited circumstances, the FCC) would first have to decide that the provider satisfies the requirements of section 214(e)(1). Consequently, petitioners' claim is not ripe for judicial review, because it is contingent upon such future, fact-specific decisions. *See Los Alamos Study Grp. v. U.S. Dept. of Energy*, 692 F.3d 1057, 1065 (10th Cir. 2012) (a claim is ripe where "the issues involved

are purely legal, … the agency's action is final," and the "action has or will have an immediate impact on the petitioner" (internal quotation marks and citation omitted)); *see also Qwest Commc'ns Int'l, Inc. v. FCC*, 240 F.3d 886, 894 (10th Cir. 2001).

2. Petitioners' claim also lacks merit. Petitioners mistakenly assert that the *Order* "does not limit support to telecommunications carriers or require that USF [support] be used for telecommunications services." Br. 17. Only "eligible telecommunications carriers" are eligible for subsidies under section 254, however, and an ETC, by definition, is a "common carrier" that "offer[s] the services that are supported by the Federal universal service support mechanisms under section 254(c)." 47 U.S.C. §214(e)(1)(A). Nowhere does the *Order* hold that an entity not designated as an ETC could receive federal universal service support.

Further, the only service that the FCC has designated under section 254(c)(1) is "voice telephony service." *See, e.g.*, *Order* ¶¶62-63, 79 (JA at 411-412, 420). Petitioners assert that providing "voice telephony service" as VoIP would violate the Act, because unlike circuit-switched voice service, VoIP has not yet been designated a "telecommunications service." Br. 17-18. While VoIP service is unclassified, the FCC has acknowledged that a VoIP provider can obtain the rights available to "telecommunications carriers"

under Title II of the Act if it voluntarily "holds itself out as a telecommunications carrier and complies with appropriate federal and state requirements." *IP-Enabled Services*, 20 FCC Rcd 10245, 10268 (¶38 n.128) (2005), *aff'd sub nom. Nuvio Corp. v. FCC*, 473 F.3d 302 (D.C. Cir. 2006). And in this proceeding, "some providers of facilities-based retail VoIP services state[d] that they are providing those services on a common carrier basis." *Order* ¶1389 & n.2537 (JA at 870). Thus, at a minimum, a provider could be eligible for ETC status under section 214(e)(1)(A) and universal service support under section 254(e) if it voluntarily offered VoIP as a "telecommunications service."

Consequently, a "set of circumstances exists in which [the *Order*] can be lawfully applied," so petitioners' facial challenge fails. *Cellco P'ship*, 700 F.3d at 549 (internal quotation marks and citations omitted).[6]

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[6] The *Order* "rel[ied] on section 706(b) as an alternative basis to section 254 to the extent necessary to ensure that the federal universal service program covers services and networks that could be used to offer information services as well as telecommunications services." *Order* ¶73 (JA at 418). While the FCC noted that section 706 would also permit the agency to provide universal service support to VoIP providers irrespective of the regulatory classification of that service, *id.* ¶71 (JA at 417), the *Order* further provides that "[c]arriers seeking federal support" under section 706(b) "must still comply with the same universal service rules and obligations set forth in section 254 and 214." *Id.* ¶73 (JA at 418). Hence, any funding recipient must still be an ETC. In any event, because the FCC has not authorized support for VoIP service under section 706, that issue is not presented here.

D. The FCC Reasonably Ruled That It Also Has Authority Under Section 706 Of The 1996 Act To Require Recipients Of Federal Universal Service Support To Deploy Broadband Networks And Services.

In section 706(b) of the 1996 Act, 47 U.S.C. §1302(b), Congress instructed the FCC to "determine whether advanced telecommunications capability is being deployed to all Americans in a reasonable and timely fashion," and if the agency concludes that it is not, to "take immediate action to accelerate deployment of such capability by removing barriers to infrastructure investment and by promoting competition in the telecommunications market." Having found that broadband deployment lagged, *Order* ¶70 (JA at 416), the FCC reasonably concluded that section 706(b) empowered it to support broadband-capable networks, *see id*. ¶¶67-70 (JA at 415-416).

Petitioners argue that the FCC lacked authority under section 706(b) because "[t]here is no mention of expanding the USF to include support for broadband information services" in that provision. Br. 26. While Congress could have created an exhaustive and highly specific list of the authorities the FCC could exercise to further the statutory goal set forth in section 706(b), it instead delegated to the FCC broad authority to "take immediate action to accelerate deployment of such capability by removing barriers to infrastructure investment and by promoting competition in the

telecommunications market." 47 U.S.C. §1302(b); *see also Ad Hoc Telecomms. User Comm. v. FCC*, 572 F.3d 903, 906-07 (D.C. Cir. 2009) (explaining that "[t]he general and generous phrasing of §706 means that the FCC possesses significant, albeit not unfettered, authority and discretion to settle on the best regulatory or deregulatory approach to broadband").

The FCC, in the *Order* (at ¶67 (JA at 415)), reasonably found that "[p]roviding support for broadband networks helps achieve section 706(b)'s objectives." Support for broadband "promot[es] competition in the telecommunications market" where "interconnected VoIP service is increasingly used to replace [traditional] voice service." *Id.* ¶68 (JA at 415-416) (internal quotation marks omitted). Support for broadband also "eliminate[s] a significant barrier to infrastructure investment." *Id.* ¶67 (JA at 415). This is because "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." *Id.* (internal quotation marks omitted). Those findings by the expert agency as to a matter within its competence satisfy the requirements of section 706(b).

Petitioners find no support in *Comcast Corp. v. FCC*, 600 F.3d 642 (D.C. Cir. 2010). *See* Br. 24. The D.C. Circuit in that decision found that a

prior FCC order stating that section 706(a) did not "constitute an independent grant of authority" was "still binding" at that time because the agency "never questioned [it], let alone overruled [it]." *Comcast*, 600 F.3d at 658-59. In a subsequent order, however, the FCC did just that. It held that if the prior order could be interpreted as having declined to read section 706(a) as a grant of authority, the FCC "reject[ed] that reading of the statute." *See Preserving the Open Internet*, 25 FCC Rcd 17905, 17969 n.370 (2010), *pet. for review pending*, *Verizon v. FCC*, D.C. Cir. No. 11-1355.

Petitioners also attempt to manufacture a conflict between sections 254 and 706. Br. 27-28. As the FCC explained, "section 254(b)(2)'s principle that '[a]ccess to advanced telecommunications *and information services* should be provided in all regions of the Nation' dovetails comfortably with section 706(b)'s policy that 'advanced telecommunications capability [be] deployed to all Americans in a reasonable and timely fashion.'" *Order* ¶72 (JA at 417-418) (quoting 47 U.S.C. §254(b)(2)). It follows that the FCC's "decision to exercise authority under Section 706 does not undermine section 254's universal service principles"; rather, it "ensures their fulfillment." *Id.* For the same reason, petitioners' argument that the "specific" section 254 controls the more "general" section 706(b) is unpersuasive. Br. 27. There is no point in "quibbl[ing] over which section is more specific," where, as here,

the agency's "interpretation … is reasonable" and "gives effect to both provisions." *Nat'l Ass'n of Home Health Agencies v. Schweiker*, 690 F.2d 932, 943 n.70 (D.C. Cir. 1982).

* * *

As this Court has recognized, "the 1996 Act is not a model of clarity." *Qwest II*, 398 F.3d at 1235 (quoting *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 397 (1999)). Section 254, in particular, is ambiguous, *RCA I*, 588 F.3d at 1101-02, and the FCC reasonably construed it to authorize the agency to modernize universal service support so that it enhances the broadband access that is critical to rural America. But "even if the agency's reading differs from what the court believes is the best statutory interpretation," it is clearly not precluded by the statute's language or structure and therefore must be affirmed under well-established principles of deference to agencies that interpret the statutes they are entrusted to administer. *Nat'l Cable & Telecomms. Ass'n v. Brand X Internet Servs.*, 545 U.S. 967, 980 (2005); *see Mainstream Mktg. Servs., Inc. v. FTC*, 358 F.3d 1228, 1250 (10th Cir. 2004).

II. THE FCC REASONABLY ADOPTED A $4.5 BILLION ANNUAL FUNDING TARGET.

The FCC "[f]or the first time … establish[ed] a defined budget for the high-cost component of the universal service fund." *Order* ¶123 (JA at 437-438). It did so to "ensure[] that individual consumers will not pay more in

[universal service] contributions due to the reforms" in the *Order*. *Id*. ¶124 (JA at 438). If those reforms were "to significantly raise the end-user cost of services," they "could undermine" the agency's larger efforts "to promote broadband and mobile deployment and adoption." *Id*.

The FCC set the annual funding target at $4.5 billion – the estimated amount of funding collected for the high-cost program in Fiscal Year 2011. *Order* ¶125 (JA at 438). By "setting the budget at this year's support levels," the FCC hoped to "minimize disruption and provide the greatest certainty and predictability to all stakeholders." *Id*. Of the $4.5 billion, the FCC allocated $500 million for the Mobility Fund, $1.8 billion for areas served by price cap carriers, and $2 billion for rate-of-return carriers. *Id*. ¶126 (JA at 438-439).

Although the FCC established a fixed budget, it adopted "a number of safeguards … to ensure that carriers that warrant additional funding have the opportunity to petition for such relief." *Order* ¶126 (JA at 438-439); *see also id*. ¶¶539-44 (JA at 566-569) (establishing express waiver procedures). The FCC also committed to "closely monitor" the budget going forward to "ensur[e] [it] remains at appropriate levels to satisfy [the FCC's] statutory mandates." *Id*. ¶126 (JA at 438-439).

"[A] broad cross-section of interested stakeholders, including consumer groups, state regulators, current recipients of funding, and those

that do not currently receive funding" supported the $4.5 billion annual budget. *Order* ¶122 & n.192 (JA at 437).

A. The FCC's Reasonable Predictive Judgment That The *Order* Will Provide Sufficient Support Is Entitled To Substantial Deference.

Sections 254(b)(5) and (e) of the Act require "sufficient" universal service support. *See* 47 U.S.C. § 254(b)(5) and (e). "[W]hat constitutes 'sufficient' support" is inherently "ambiguous." *TOPUC*, 183 F.3d at 425. So long as "the FCC … offer[s] reasonable explanations of why it thinks the funds will still be 'sufficient' to support high-cost areas," the Court should "defer to the agency's judgment of what is 'sufficient.'" *Id.*; *see also id.* at 426, 436-37; *Alenco*, 201 F.3d at 620-21; *RCA I*, 588 F.3d at 1103-04; *Rural Cellular Ass'n v. FCC*, 685 F.3d 1083, 1094 (D.C. Cir. 2012) ("*RCA II*").

Petitioners nevertheless contend that the FCC erred when it found that "maintaining total funding for rate-of-return companies at approximately $2 billion per year" would ensure that support is "sufficient" to "sustain service to consumers" and expand broadband. *Order* ¶195 (JA at 465). Petitioners' overarching complaint is that the FCC "improperly limited its analysis to whether, without reform, USF support would be excessive" without "also consider[ing] whether too little support is being provided." Br. 31.

Contrary to petitioners' assertion, the *Order* expressly considered the possibility of too little support, and it found that subsidies would not be "insufficient" given its efforts to eliminate "long-standing inefficiencies and wasteful spending" in the FCC's legacy funding mechanisms. *Order* ¶125 (JA at 438). The FCC expected that those cost savings would offset any increased support to individual carriers to make additional investments to deploy broadband. *See id*. ¶¶125, 285-92 (JA at 438, 495-497).

Particularly relevant to petitioners' objections, the FCC structured reform to mitigate the financial impact on rate-of-return carriers. Under the *Order*, "rate-of-return carriers will not necessarily be required to build out to and serve the most expensive locations within their service area." *Order* ¶207 (JA at 468). Instead, they are only obligated to offer broadband upon "reasonable request." *Id*. ¶¶206-07 (JA at 467-468). This "flexible approach" (*id*. ¶206 (JA at 467-468)) was specifically designed to protect rate-of-return carriers from extending facilities where high-cost support was insufficient to make deployment economically reasonable, *see also id*. ¶26 (JA at 401). The *Order* also "exempted the most remote areas" from the new broadband service obligations. *Id*. ¶533 (JA at 564-565). And the *Order* "provide[d] rate-of-return carriers … access to a new explicit recovery mechanism," which guarantees "stable and certain revenues that the current

intercarrier system can no longer provide." *Id*. ¶291 (JA at 496-497). In light of these factors, the FCC reasonably predicted that its "incremental reforms will not endanger existing service to consumers" and will "minimally affect[]" rate-of-return carriers "that invest and operate in a prudent manner." *Id*. ¶289 (JA at 496).

Further, as a backstop to ensure sufficient support in individual cases of hardship, the *Order* provides a waiver process for those carriers that can demonstrate that "reductions in current support levels would threaten their financial viability, imperiling service to consumers in the areas they serve." *Order* ¶¶539-44 (JA at 566-569). The agency has already granted two such waivers. *See Accipiter Communications, Inc*., 28 FCC Rcd 391 (WCB 2013); *Allband Communications*, 27 FCC Rcd 8310 (WCB 2012). Courts have

repeatedly held that it is reasonable for the agency to rely on a waiver process to address any unforeseen shortfalls that might arise in specific instances.[7]

Petitioners nonetheless allege that the FCC "disregard[ed] the substantial additional costs" to satisfy the broadband service condition in the *Order*. Br. 32. Their only support for that claim is a 2010 study estimating that many rate-of-return carriers provided broadband service at slower speeds than those required by the *Order*. *See id.* Petitioners, however, make no attempt to quantify the cost to upgrade their networks. The FCC had little reason to think that the additional cost (if any) would be substantial given that the *Order*'s "flexible approach" to broadband deployment "does not require rate-of-return companies to extend service to customers absent … a

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[7] *See Vt. Pub. Serv. Bd. v. FCC*, 661 F.3d 54, 65 (D.C. Cir. 2011) (finding a waiver process provided a reasonable means to update stale line count data used in a model for determining universal service support); *RCA I*, 588 F.3d at 1104 (discussing, with approval, a waiver process used to provide certain wireless carriers additional support should an interim cap render support insufficient); *RCA II*, 685 F.3d at 1095 (same); *Alenco*, 201 F.3d at 622 (finding a single carrier's reduced rate of return under an operating expenses cap "at most … presents an anomaly that can be addressed by a request for a waiver"). Petitioners never mention these cases, and instead rely on *FPC v. Texaco*, 417 U.S. 380, 399 (1974) and *Home Box Office, Inc. v. FCC*, 567 F.2d 9, 50-51 (D.C. Cir. 1977) – neither of which concern the FCC's universal service program – to argue that "a waiver" cannot "justify an otherwise unreasonable rule." Br. 32-33. Those cases are easily distinguished on the ground that the FCC is not relying on the waiver process to save an otherwise irrational rule; to the contrary, the rule is rational and the waiver process addresses potential outlier cases.

[reasonable] request." *Order* ¶26 (JA at 401). Moreover, the *Order* provides rate-of-return carriers, which serve "less than five percent of access lines in the U.S.," *id*., annual funding that totals nearly one-half of annual high-cost support (*i.e*., approximately $2 billion of the $4.5 billion budget), *id*. ¶126 (JA at 438-439).

Nor is it true that the *Order* "ma[de] no effort to quantify whether the resulting USF support can cover the [rate-of-return carriers'] 'efficient' cost of providing voice service plus the added cost of satisfying the broadband mandate." Br. 32. The FCC's analysis showed that 34 percent of rate-of-return carriers would see no change in federal universal service support receipts, and 12 percent would see an increase in support. *Order* ¶290 (JA at 496). Of those rate-of-return carriers expected to experience a reduction, most would see a reduction of fewer than 10 percent of their federal subsidies annually. *Id*.

Qwest II, 398 F.3d 1222 (Br. 32), is not to the contrary. In that decision, the Court directed the FCC, on remand, to provide "empirical findings supporting [its] conclusion" that rates then in effect were "reasonably comparable" for purposes of section 254(b)(3). *Id*. at 1237. The FCC, in the *Order* at issue here, necessarily could not provide "empirical support" that funding is currently "sufficient" to satisfy sections 254(b)(5)

and (e) because the reforms in the *Order* had not yet been implemented. Thus, the agency appropriately relied on evidence in the record to support a reasonable predictive judgment. *See Order* ¶123 (JA at 437-438). And "[w]here, as here, the FCC must make predictive judgments about the effects of increasing [or decreasing] subsidies, certainty is impossible." *RCA I*, 588 F.3d at 1105; *see also FCC v. Nat'l Citizens Comm. for Broad.*, 436 U.S. 775, 813-14 (1978); *Qwest Corp. v. FCC*, 689 F.3d 1214, 1230 n.7 (10th Cir. 2012); *Franklin Savings Ass'n v. Dir., Office of Thrift Supervision*, 934 F.2d 1127, 1146-47 (10th Cir. 1991).

Finally, petitioners complain that funding "cuts fall indiscriminately on most high-cost carriers, untethered to evidence that any particular company's support level was actually due to inefficiency rather than the intrinsically high cost of serving particular areas." Br. 32. That claim is demonstrably incorrect. The reforms in the *Order* are "targeted at eliminating inefficiencies and closing gaps in [the] system, not at making indiscriminate industry-wide reductions." *Order* ¶287 (JA at 496). For example, limitations on reimbursable capital and operating costs (*id.* ¶¶215-20 (JA at 470-472)) and high-cost loop support (*id.* ¶¶234-47 (JA at 476-483)), which are designed to encourage rate-of-return carriers to operate more efficiently, are based on carrier-specific analyses of costs and rates. In any event, "the agency [i]s

well within its discretion to impose" purely prophylactic cost controls "rather than to undertake the more costly alternative of intensive auditing." *Alenco*, 201 F.3d at 621.

B. Petitioners' Takings Claim Is Not Ripe And Lacks Merit.

Petitioners speculate that the *Order* is an unconstitutional taking of property. Br 42-45. At this point, however, petitioners' unsubstantiated takings claim is not ripe. The agency has made clear that if "*any* rate-of-return carrier can effectively demonstrate that it needs additional support to avoid constitutionally confiscatory rates, the Commission will consider a waiver request for additional support." *Order* ¶294 (JA at 498) (emphasis added); *see id.* ¶¶539-44 (JA at 566-569). No takings claim is ripe until a party has invoked that process and been denied. *See Williamson County*, 473 U.S. at 194; *Alto Eldorado P'ship v. County of Santa Fe*, 634 F.3d 1170, 1175-77 (10th Cir. 2011); *TOPUC*, 183 F.3d at 428-29; *Alenco*, 201 F.3d at 624.

A takings claim would fail, in any event. Carriers face a "heavy burden" in proving confiscation as a result of rate regulation. *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944). To be confiscatory, government-regulated rates must be so low that they threaten a regulated entity's "financial integrity," *Ill. Bell Tel. Co. v. FCC*, 988 F.2d 1254, 1263 (D.C. Cir.

1993), or "destroy the value" of the company's property, *Duquesne Light Co. v. Barasch*, 488 U.S. 299, 307 (1989). Petitioners made no such showing in the record below (*see Order* ¶294 (JA at 498)) or in their brief. Thus, "[t]he mere fact that, for many rural carriers, universal service support provides a large share of the carriers' revenues … is not enough to establish that the [*Order*] constitute[s] a taking. The Fifth Amendment protects against takings; it does not confer a constitutional right to government-subsidized profits." *Alenco*, 201 F.3d at 624 (internal quotation marks and citation omitted).

III. THE FCC REASONABLY REFORMED SUPPORT MECHANISMS FOR RATE-OF-RETURN CARRIERS TO ELIMINATE WASTE AND INEFFICIENCY IN THE PRIOR SYSTEM.

The FCC, in the *Order*, "implement[ed] a number of reforms to eliminate waste and inefficiency and improve incentives for rational investment and operation by rate-of-return LECs." *Order* ¶195 (JA at 465). These reforms were long overdue. As the FCC explained, "[b]y providing an opportunity for a stable 11.25 percent interstate return for rate-of-return companies, regardless of the necessity or prudence of any given investment, our current system imposes no practical limits on the type or extent of network upgrades or investment." *Id.* ¶287 (JA at 496). The consequence was that the FCC "provide[d] universal service support to both a well-run

company operating as efficiently as possible, and a company with high costs due to imprudent investment decisions, unwarranted corporate overhead, or an inefficient operating structure." *Id*. The FCC predicted that the reforms in the *Order* "will help ensure rate-of-return carriers retain the incentive and ability to invest and operate modern networks capable of delivering broadband as well as voice services, while eliminating unnecessary spending." *Id*. ¶288 (JA at 496); *see id*. ¶195 (JA at 465).

A. The "Benchmarking Rule" Is Consistent With Section 254(b)(5) Of The Act And The FCC's Other Rules.

The *Order* adopted a new rule (the "benchmarking rule") that uses regression analysis to establish "benchmarks," or caps, to limit the reimbursable capital and operating expenses in the formula used to determine high-cost loop support ("HCLS") for rate-of-return carriers. *Order* ¶¶214, 219 (JA at 470, 471-472).[8] The FCC's prior rules did not provide rate-of-return carriers an incentive to restrain costs. *Id*. ¶¶211, 219 (JA at 469, 471-472). The new rule addresses that problem by reducing subsidies to carriers with costs greater than similarly situated companies and redistributing that

[8] A local loop is the wire between a telephone company's switch (*i.e.*, a device that routes telephone calls) and the subscriber's home or office. HCLS "helps offset the non-usage based costs associated with the local loop in areas where the cost to provide voice service is relatively high compared to the national average cost per line." *Order* ¶216 n.347 (JA at 470-471).

support to other carriers to promote broadband deployment. *Id*. ¶220 (JA at 472).

The FCC also sought additional public comment on a methodology to implement this rule (the "benchmarking methodology") in an attached FNPRM. *See Order* ¶¶¶216, 1079-88 (JA at 470-471, 786-789), App. H (JA at 1012-1021). The FCC directed its staff (the Wireline Competition Bureau, or "WCB") to finalize the benchmarking methodology after considering the record compiled in response to the FNPRM. *Id*. ¶217 (JA at 471). WCB completed that task in an April 25, 2012, Order. *See Connect America Fund*, 27 FCC Rcd 4235 (WCB 2012) ("*Benchmarking Order*"), *aff'd in part and modified in part, Connect America Fund*, 28 FCC Rcd 2572 (Feb. 27, 2013) ("*Sixth Order on Reconsideration*").[9]

Petitioners contend that the FCC: (1) violated its own rules when it delegated implementation of the benchmarking rule to WCB; (2) provided WCB "unbounded discretion" to devise the benchmarking methodology, resulting in unpredictable support amounts in violation of section 254(b)(5) of the Act; and (3) authorized WCB "to revise [that methodology] without

[9] Petitioner NTCA asked this Court to stay implementation of the *Benchmarking Order*, or in the alternative to issue a writ of mandamus directing the FCC to rule on NTCA's application for review of the *Order*. This Court denied that request on August 13, 2012.

abiding by APA notice and comment procedures." Br. 36-37. Petitioners did not raise these contentions before the agency in a petition for reconsideration, and so they are waived. *See* 47 U.S.C. §405(a).

"The filing of a reconsideration petition" with the FCC "is 'a condition precedent to judicial review … where the party seeking such review … relies on questions of fact or law upon which the Commission … has been afforded no opportunity to pass.'" *Sorenson II*, 659 F.3d at 1044 (quoting 47 U.S.C. §405(a)). "[E]ven when a petitioner has no reason to raise an argument until the FCC issues an order that makes the issue relevant, the petitioner must file a petition for reconsideration with the Commission before it may seek judicial review." *Qwest Corp. v. FCC*, 482 F.3d 471, 474 (D.C. Cir. 2007) (internal quotation marks and citation omitted). Petitioners did not do this. Consequently, section 405 of the Act bars judicial review of petitioners' claims. *See Sorenson II*, 659 F.3d at 1044, 1048 n.8; *Sorenson I*, 567 F.3d at 1227-28.

These arguments in any event lack merit because the delegation was proper. Petitioners contend that the *Order* (at ¶217 (JA at 471)) violated 47 C.F.R. §0.291(e), which prohibits rulemaking by WCB, when it "delegate[d] authority to [WCB] to adopt the initial [benchmarking] methodology, to update it as it gains more experience and additional information, and to

update its regression analysis annually with new cost data." Br. 37. But the FCC, pursuant to the relevant statutory provision may "delegate any of its functions" to staff by rule or order. *See* 47 U.S.C. §155(c)(1). The FCC lawfully exercised that statutory power by explicitly delegating rulemaking authority to WCB in this narrow context, notwithstanding any prior limitations imposed on WCB's general authority under the pre-existing agency rules.

The delegation was also fully consistent with Rule 0.291. Pursuant to that rule "[t]he Chief, Wireline Competition Bureau, is … delegated authority to perform all functions of the Bureau" subject to certain "exceptions and limitations." 47 C.F.R. §0.291. One of those limitations is that WCB generally "shall not have authority to issue notices of proposed rulemaking, notices of inquiry, or reports and orders arising from either of the foregoing." *Id.* §0.291(e). Subsection (e), by its terms, only limits WCB's general authority under the rule; it in no way limits the full Commission's authority under the Act to "delegate any of its functions" to staff. 47 U.S.C. §155(c)(1).

Nor does the delegation breach any statutory provisions. Specifically, petitioners have not demonstrated that the benchmarking rule violates section 254(b)(5), which requires "predictable" universal service support

mechanisms. The *Order* imposed meaningful "substantive limitation[s]" on WCB's authority to develop and revise the benchmarking methodology, undercutting petitioners' claim that the "vague rule" will result in "unpredictable changes" in HCLS. Br. 38; *see Order* ¶¶217-18 (JA at 471) (directing WCB to use "statistical techniques," setting forth a non-exhaustive list of variables for WCB to consider, and directing WCB to publish an updated list of "capped" values annually).

Moreover, contrary to the premise of petitioners' argument, the FCC is not required to guarantee carriers substantially the same universal service support amounts "from year to year." Br. 38. Petitioners have made clear (Br. 38, 46) that what they seek "is not merely predictable funding mechanisms, but predictable market outcomes" – something to which the Act does not entitle USF recipients, *see Alenco*, 201 F.3d at 622.

Beyond that, petitioners' argument, even on its own terms, fails to demonstrate that the rule adds uncertainty into HCLS disbursements. It has always been the case that carriers do not know how much support they will receive in future periods. As the *Order* (at ¶220 (JA at 472)) explained, "the fact that an individual company will not know how the benchmark affects its support levels until after investments are made is no different from the current operation of high-cost loop support, in which a carrier receives support based

on where its own cost per loop falls relative to a national average that changes from year to year." The only difference is that under the prior rules, "carriers that t[ook] prudent measures to cut costs" often "los[t] HCLS support to carriers that significantly increase[d] their costs in a given year" (*id*. ¶219) (JA at 471-472), whereas after the *Order*, rate-of-return carriers have an incentive to avoid over-spending by "manag[ing] their costs to be in alignment with their similarly situated peers." *Id*. ¶221 (JA at 472).

Petitioners further claim that the *Order* "exacerbates unpredictability" by allowing WCB "to change the [benchmarking] rule … without following the notice and comment procedures required for proposed rule changes under the APA." Br. 39. In fact, WCB followed the APA's procedural requirements in implementing the benchmarking rule. *See* 77 Fed. Reg. 30,411-01 (May 23, 2012). To the extent that a later WCB order does not follow those rules, petitioners may challenge it then. Until then, their claim is

not ripe. *See Qwest*, 240 F.3d at 894; *Los Alamos Study Grp*., 692 F.3d at 1064-65; *Sw. Bell Tel. Co. v. FCC*, 153 F.3d 523, 556 (8th Cir. 1998).[10]

B. The FCC Did Not Engage In Impermissible Retroactive Rulemaking.

Petitioners argue that adoption of the benchmarking rule and elimination of the safety net additive (or "SNA") rule, which reduce their federal universal service subsidies, constitute improper retroactive rulemaking. *See* Br. 46-48. Their argument lacks merit.

The FCC's actions are far removed from the classic (or "primary") retroactivity that occurs when governmental conduct "would impair rights a party possessed when he acted, increase a party's liability for past conduct, or impose new duties with respect to transactions already completed." *Landgraf v. USI Film Prods., Inc*., 511 U.S. 244, 280 (1994). This is because the *Order* is entirely *prospective*: that is, it does not mandate the return of USF disbursements already made but only reduces or eliminates federal subsidies going forward.

[10] Petitioners fleetingly claim that it was arbitrary and capricious for the FCC to rely on only cost data for voice services when it updated the formula used to limit the corporate operations expenses eligible for recovery through HCLS. Br. 33 (citing *Order* ¶230 (JA at 474-475)). This argument was never presented in the proceeding below or in a subsequent petition for reconsideration of the *Order*; thus, it has been waived. *See* 47 U.S.C. §405(a); *Sorenson II*, 659 F.3d at 1044, 1048 n.8.

Petitioners concede as much, but contend that the *Order* is retroactive insofar as it precludes them from recovering expenses they incurred based on the "reasonable expectation[]" that they would receive universal service support. Br. 46. But a new rule is not retroactive "merely because it … upsets expectations based in prior law." *Landgraf*, 511 U.S. at 269.

Moreover, any expectations petitioners had that they would receive any particular funding amounts in the future (or that prior methodologies would be used to determine future subsidy disbursements) were not reasonable. As the FCC explained, "Section 254 does not mandate the receipt of support by any particular carrier." *Order* ¶221 (JA at 472); *see also id*. ¶293 (JA at 497-498). The courts agree. In rejecting a challenge to an earlier cap on HCLS, the Fifth Circuit explained that "[t]he Act does not guarantee all local telephone service providers a sufficient return on investment." *Alenco*, 201 F.3d at 620. Instead, "[t]he Act only promises universal service, and that is a goal that requires sufficient funding of customers, not providers." *Id.*; *see RCA I*, 588 F.3d at 1103.

Petitioners alternatively contend that the *Order* is "arbitrary and capricious" because it "alter[s] future regulation in a manner that makes worthless substantial past investment incurred in reliance upon the prior rule[s]." Br. 47 (citing *Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 220

(1988) (Scalia, J., concurring)). As set forth above, petitioners have not demonstrated that the *Order* renders their past investments "worthless," *see* pp. 39-40, and a waiver process in the *Order* exempts carriers from support reductions that would imperil their financial viability, *see* p. 35-36. Significantly, the FCC has only received a handful of waiver petitioners to date. *Id*. Even if petitioners had made that showing, however, there is no presumption against such "secondary" retroactive effects, and a rule "may nonetheless be sustained in spite of such retroactivity if it is reasonable." *Bowen*, 488 U.S. at 220 (1988) (Scalia, J., concurring); s*ee also DirecTV, Inc. v. FCC*, 110 F.3d 816, 826 (D.C. Cir. 1997). The two rule changes petitioners attack are reasonable and easily satisfy this standard.

In particular, the "benchmarking rule" (*see* pp. 41-47, above) limits the reimbursable capital and operating expenses in the formula used to determine HCLS for rate-of-return carriers. Petitioners contend that the rule is unreasonable given the *Order*'s alleged failure to explain why certain costs previously incurred by rate-of-return carriers are no longer compensable from the USF. *See* Br. 47-48. But the *Order* made clear that the benchmarking rule was necessary to "discourage companies from over-spending relative to their peers." *Order* ¶220 (JA at 472); *see id*. ¶¶211, 219 (JA at 469, 471-472). Under the FCC's prior rules, rate-of-return carriers could have 100

percent of their loop costs above a certain threshold reimbursed from the federal USF; thus, carriers that took measures to control expenses could find themselves losing support to carriers that increased costs. *Id.* ¶¶211, 219 (JA 469, 471-472). To accomplish its cost-saving goal, the FCC reasonably declined to conduct costly and burdensome audits of the more than 800 rate-of-return carriers, as demanded by petitioners (*see* Br. 47-48), and instead adopted a general rule that identifies carriers with costs that are significantly greater than their peers, *see Alenco*, 201 F.3d 620-21.

The FCC adopted the SNA rule in 2001 to provide support to rural incumbent LECs that made "additional significant investments" in their networks. *Order* ¶248 (JA at 483). According to petitioners, "the Order made no attempt to explain why a program intended to provide additional support for carriers making substantial network upgrades should be terminated." Br. 48. But petitioners fail to mention that the *Order* "conclude[d] the safety net additive is not designed effectively to encourage additional significant investment in telecommunications plant." *Order* ¶250 (JA at 484). Instead, "[t]he majority of incumbent LECs that currently are receiving the safety net additive qualified in large part due to significant loss of lines, not because of significant increases in investment, which is contrary to the intent of the rule." *Id.* ¶249 (JA at 484). Given that the rule had not

worked as intended, the FCC reasonably eliminated it. *See Bechtel v. FCC*, 957 F.2d 873, 881 (D.C. Cir. 1992) (the FCC has a "duty to evaluate its policies over time to ascertain whether they work – that is, whether they actually produce the benefits the Commission originally predicted they would").

The *Order* likewise "rejected" petitioners' claim (*see* Br. 46, 48) that carriers are entitled to SNA for investments made in 2010 and 2011 to satisfy commitments made to other federal agencies under broadband stimulus programs. *Order* ¶252 n.409 (JA at 485). As the *Order* noted, "since early 2010, the Commission has given carriers ample notice that [it] intended to undertake comprehensive universal service reform in the near term." *Id.*; *NPRM*, 26 FCC Rcd at 4620-21 (¶184) (SJA at 67-68) (proposing to eliminate SNA); *Connect America Fund*, 25 FCC Rcd 6657, 6677-78 (¶¶51-52) (2010) (JA at 21-22) (proposing to eliminate new eligibility for SNA). More fundamentally, carriers are never "entitled" to universal service support for future years and could not properly rely upon it. *See Alenco*, 201 F.3d at 620; *RCA I*, 588 F.3d at 1103.

IV. PETITIONERS' CHALLENGES TO THE FCC'S NEW SUPPORT MECHANISMS FOR AREAS SERVED BY PRICE CAP CARRIERS ARE NOT RIPE AND LACK MERIT.

In addition to reforming funding for rate-of-return carriers, the *Order* overhauled the rules that distribute high-cost universal service support to price cap carriers. "[M]ore than 83 percent of the unserved locations in the nation are in price cap areas," the FCC explained, "yet such areas currently receive approximately 25 percent of high-cost support." *Order* ¶158 (JA at 452). "[T]o meet [its] universal service mandate to unserved consumers residing in these communities," the FCC "conclude[d] that increased support to areas served by price cap carriers, coupled with rigorous, enforceable deployment obligations, [wa]s warranted." *Id.* ¶159 (JA at 452-453).

In Phase I of reform, which is still in effect, the FCC froze support for price cap carriers at existing levels. *See Order* ¶128 (JA at 439-440). "In addition, to spur the deployment of broadband in unserved areas," the FCC "allocate[d] up to $300 million in additional support to such carriers." *Id.* In Phase II, the FCC will almost double support to price cap carriers (from about $1 billion to $1.8 billion annually). *See id.* ¶158 (JA at 452). The FCC will offer each price cap carrier high-cost support in exchange for a commitment to offer (1) voice service throughout its service territory and (2) broadband service to specific areas within its service territory in a state. *See id.* ¶166 (JA

at 454-455). A price cap carrier's "right to [that] support will terminate after five years," at which time the FCC "expect[s] that support … will be awarded through a competitive bidding process in which all eligible providers will be given an equal opportunity to compete." *Id.* ¶178 (JA at 459).

Petitioners contend that the FCC "failed to consider" their argument that limiting Phase I incremental support to unserved areas is "arbitrary and discriminatory" because "carriers in states with extensive broadband development commitments … get nothing to upgrade what they have done." Br. 57. In fact, the *Order* acknowledged that "[c]arriers have been steadily expanding their broadband footprints" and "expect[ed] such deployment will continue." *Order* ¶137 (JA at 444). The FCC then reasonably concluded that, instead of subsidizing service upgrades in areas that already have access to broadband, it could most effectively promote broadband deployment by devoting Phase I funding to jump-starting broadband deployment in previously unserved areas. *See id.*; *see also Connect America Fund*, 27 FCC Rcd 4648, 4653 (¶15) (2012) (JA at 1156). Petitioners may disagree with that policy judgment, but because the FCC "adequately explained its decision," its action "was neither arbitrary nor capricious." *Vermont Public Service Board*, 661 F.3d at 63.

Petitioners also assert that the FCC "failed adequately to address arguments" that using an auction to distribute subsidies to price cap carriers in Phase II will result in inadequate service. Br. 49. This claim is not ripe for judicial review, because the FCC did not "adopt[] an auction mechanism" for price cap carriers in the *Order*. *Id.* Rather, the agency merely sought comment on how best to design and implement such a mechanism in the attached FNPRM. *See Order* ¶¶1190-222 (JA at 812-819). The FCC addressed the "arguments" that it allegedly "ignored" by seeking comment on them in that FNPRM. *Compare* Br. 50-51 *with Order* ¶¶1203-07 (JA at 815-816) (seeking comment on service quality standards); Br. 51-52 *with Order* ¶1213 (JA 817-818) (seeking comment on a bidding preference for small carriers).

Indeed, while petitioners purport to attack the FCC's discussion of the auction mechanism for price cap carriers, they rely (without acknowledgement) on the agency's discussion of a different auction mechanism for wireless carriers. *See* Br. 49-52 (citing *Order* ¶¶311, 325-26 (JA at 504, 509)). Unless the FCC adopts that specific mechanism for price cap carriers, its discussion of that mechanism is not relevant. Petitioners also seem to assume that the service quality standards applicable to price cap carriers today will be the same service quality standards that apply to price

cap carriers under a competitive bidding mechanism. *See* Br. 50-51 (citing *Order* ¶¶90, 94, 96, 98 (JA at 423, 424, 425-426)). The FCC has not yet made that determination. *See Order* ¶¶1203-07 (JA at 815-816).

Until the FCC adopts an auction mechanism based on the record developed under the outstanding FNPRM, the Court will not be able to determine whether the FCC adequately responded to petitioners' arguments that competitive bidding will degrade service and disadvantage small carriers. *See Qwest*, 240 F.3d at 894. Likewise, there will be no "'direct and immediate impact' upon [petitioners]" until the FCC issues an order adopting a competitive bidding mechanism. *Id.* (quoting *Abbott Labs. v. Gardner*, 387 U.S. 136, 152 (1967)).

V. PETITIONERS' VARIOUS CHALLENGES TO THE OTHER REFORMS IN THE *ORDER* ARE WAIVED, NOT RIPE, AND LACK MERIT.

A. The *Order* Lawfully And Reasonably Reduced Federal Universal Service Subsidies In Areas With Artificially Low End-User Rates.

To avoid "plac[ing] an undue burden on the [USF] and consumers that pay into it," the *Order* "adopt[ed] a rule to limit high-cost support where end-user rates do not meet a specified local rate floor" initially set at $10 per month. *Order* ¶¶235; *see* ¶¶237, 239 (JA at 476-477; 478-479). Evidence in the record showed that "there are a number of carriers with local rates that are

significantly lower than rates that urban customers pay" – sometimes as low as $5 per month. *Id.* ¶235 (JA at 476-477).[11] While section 254(b)(3) of the Act requires "reasonably comparable" urban and rural rates, the FCC interpreted that principle to "ensure" only "that rates in rural areas not be significantly higher than in urban areas," not to "subsidize[] artificially low local rates in rural areas." *Id.* "The agency's broad discretion to provide sufficient universal service funding includes the decision to impose cost controls to avoid excessive expenditures that will detract from universal service." *Alenco*, 201 F.3d at 620-21.

Petitioners argue that "the de facto effect" of this rule is to "set[] local rates," in violation of 47 U.S.C. §152(b). Br. 41. Petitioners cite no judicial authority for this assertion. Nor could they, because as courts have recognized, the mere fact that an FCC rule might have an incidental effect on rates does not mean that the FCC is "regulating" rates. *See, e.g.*, *Cable & Wireless*, 166 F.3d at 1230 (finding that even though "the practical effect of the Order will be to reduce settlement rates charged by foreign carriers … the Commission does not exceed its authority simply because a regulatory action has extraterritorial consequences"); *Cellular Telecomms. Indus. Ass'n v.*

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[11] By comparison, the national average local rate is $15.62 per month. *Order* ¶236 (JA at 477).

FCC, 168 F.3d 1332, 1336 (D.C. Cir. 1999) (upholding the FCC's determination that a state commission's imposition of universal service contribution requirements on wireless carriers did not amount to "rate regulation" preempted by 47 U.S.C. §332(c)(3), even though such requirements "impact the rates charged to customers"). Accordingly, the FCC's rate floor for federal universal service support does not constitute local rate-setting.

Moreover, under this Court's precedent, adopting measures that encourage states to adjust local rates is not only permissible; it is sometimes required. That is because the agency "remains obligated to create some inducement – a 'carrot' or a 'stick,' for example … – for the states to assist in implementing the goals of universal service," here avoiding excessive universal service support caused by extraordinarily low local rates. *Qwest I*, 258 F.3d at 1204; *see also Qwest II*, 398 F.3d at 1238 (upholding the FCC's authority to withhold all universal service support from states that fail to certify that rural rates within their boundaries are "reasonably comparable" to urban rates). It follows that the FCC did not unlawfully interfere with state regulation of local rates when it adopted the rate floor rule in the *Order*.

Petitioners separately contend that the rate floor rule is arbitrary and capricious due to the FCC's alleged "fail[ure] to give adequate consideration"

to comments in the record. Br. 42. Petitioners rely on a single comment (out of more than 650 formal comments and reply comments filed in this proceeding) arguing that low rates in certain rural areas might be attributed to small calling local areas. Under the theory sketched in this comment, urban and rural services are not comparable because rural customers living in the allegedly smaller calling local areas make fewer local calls but more long distance calls than their urban counterparts. *See id.* (citing Comments of the Missouri Small Company Telephone Group, WC Docket 10-90 at 10 (filed Apr. 18, 2010) (JA at 2284)). This comment, however, is "unsupported by any data" showing that rural customers actually pay as much, or more, for telecommunications services than their urban counterparts by incurring greater long distance charges. *Vermont Public Service Board*, 661 F.3d at 63. Thus, it is not a significant comment that warranted a response from the agency. *See Ark Initiative v. U.S. Forest Serv.*, 660 F.3d 1256, 1262 (10th Cir. 2011).

Petitioners also contend that the FCC neglected to consider "the fact that rate[s] may have been kept low by state funds." Br. 42. This claim has been waived because it was never presented to the FCC. *See* 47 U.S.C.

§405(a); *Sorenson II*, 659 F.3d at 1044, 1048 n.8.[12] Moreover, the argument is unavailing: if state universal service funding keeps certain rural rates artificially low, there is no reason to continue providing carriers federal universal service funding to ensure that those rates are "reasonab[ly] comparab[le]" to urban rates. *Order* ¶237 (JA at 478); *see also RCA I*, 588 F.3d at 1102 (the FCC's universal service policies must consider "not just affordability for those benefitted, but fairness for those burdened").

B. The *Order* Reasonably Eliminated Federal Universal Service Support In Areas Served By An Unsubsidized Competitor.

The FCC, in the *Order*, found that "[p]roviding universal service support in areas of the country where another voice and broadband provider is offering high-quality service without government assistance is an inefficient use of limited universal service funds." *Order* ¶281 (JA at 494). As the FCC explained, "USF support should be directed to areas where providers would not deploy and maintain network facilities absent a USF subsidy, and not in areas where unsubsidized facilities-based providers already are competing for customers." *Id.* (internal quotation marks omitted). The FCC thus "adopt[ed]

[12] The comment cited by petitioners (Br. 42) raised a very different claim, arguing that the rate floor "would penalize [the commenter] for complying with [a] state law" prohibiting local rate increases. Comments of Consolidated Communications Holdings, Inc., WC Docket No. 10-90 at 14 (filed Aug. 24, 2011) (JA at 3336).

a rule to eliminate universal service support where an unsubsidized competitor – or a combination of unsubsidized competitors – offers voice and broadband service throughout an incumbent carrier's study area." *Id.*; *see id.* ¶170 (JA at 456). The rule "reflects a reasonable balance between the Commission's mandate to ensure sufficient support for universal service and the need to combat wasteful spending." *Alenco*, 201 F.3d at 620; *see RCA I*, 588 F.3d at 1102.

Petitioners assert that "[t]he Order disregards evidence that the moment the rural carrier loses its USF support … consumers are at risk," because an unsubsidized competitor (unlike the incumbent LEC) has only market incentives, rather than an ongoing legal obligation, to continue providing voice and broadband service in these areas. Br. 55-56; *see id.* at 54. The FCC, however, made a very different predictive judgment: that an "unsubsidized competitor" – which, by definition, is a facilities-based provider that is not eligible for support yet serves the incumbent LEC's entire geographic service area (*Order* ¶¶281-83 (JA at 494-495)) – would have an incentive to recover its investment by continuing to serve every possible customer. This was entirely reasonable. *See Nuvio Corp.*, 473 F.3d at 309 ("[p]redictions regarding the actions of regulated entities are precisely the type of policy judgments that courts routinely and quite correctly leave to

administrative agencies") (internal quotation marks and citation omitted); *Melcher v. FCC*, 134 F.3d 1143, 1152 (D.C. Cir. 1998) (deferring to the FCC's predictive "judgments about future market behavior").[13]

Moreover, under 47 U.S.C. §214(e)(3), the FCC and the state commissions may compel a carrier to provide the supported universal services "to an unserved community or any portion thereof," subject to the statutory obligations imposed on ETCs. Given its ability to address petitioners' speculative parade of horribles (should they ever arise), the FCC is under no obligation to continue to distribute universal service support inefficiently.

Finally, petitioners claim that it is unfair to retain carrier-of-last-resort ("COLR") obligations[14] for incumbent LECs after they no longer receive federal universal service support. *See* Br. 56. COLR requirements, however, are imposed under state law and not by the FCC. *See Order* ¶¶15, 75 (JA at

[13] As we explain in our Response to the Additional USF Issues Principal Brief of Petitioners at 19-20, the FCC reasonably found that if an area is served by a provider without federal subsidies, there is no need to provide high-cost universal service support to any provider.

[14] "[I]ncumbent LECs in many states are designated as the carriers of last resort and thus have a preexisting obligation to ensure service to consumers who request it." *Order* ¶177 n.290 (JA at 458-459).

398-399, 418). Ultimately, it is the states' responsibility to determine whether COLR requirements are still warranted.

C. The New Competitive Bidding Mechanism For Distributing One-Time Support To Wireless Carriers Is Consistent With the Act.

Petitioners also contend (at Br. 39-40) that the *Order* violates section 214(e)(2) of the Act, which provides that a "State commission may, in the case of an area served by a rural telephone company, and shall, in the case of all other areas, designate more than one common carrier as an eligible telecommunications carrier for a service area designated by the State commission." 47 U.S.C. §214(e)(2). According to petitioners, the *Order* "usurps the role expressly reserved to the states" by "adopt[ing] various competitive bidding mechanisms to distribute USF support" and "defin[ing] the geographic service areas to be auctioned off." Br. 39-40.

Petitioners' argument fails because it conflates eligibility for subsidies with the right to receive subsidies. While state commissions under section 214(e) of Act determine which carriers are eligible for support, and where those carriers are eligible for support, a carrier is not entitled to receive support merely by virtue of its ETC designation. *See Order* ¶¶73 & n.104, 389, 390 & n.662, 392 (JA at 418, 525, 526). As the FCC explained, "nothing in the statute compels that every party eligible for support actually

receive it." *Order* ¶318 (JA at 507); *see High-Cost Universal Service Support*, 23 FCC Rcd 8834, 8847 (¶29) (2008), *aff'd*, *RCA I*, 588 F.3d 1095; FCC Response to Wireless Carrier USF Principal Br. 36-40. Because the *Order* only reformed the distribution of high-cost universal service support, and left intact the state commissions' authority to designate ETCs and their service areas, there is no section 214(e) violation.

Petitioners also mistakenly claim the *Order* created a "new conditional [ETC] designation." Br. 40 (citing *Order* ¶439 (JA at 536)). Rather, the *Order* simply held that carriers that receive an ETC designation conditioned upon receiving Mobility Fund support may participate in the Mobility Fund Phase I auction. *Order* ¶¶391 n.665, 439 (JA at 525, 526, 536). Nothing in the *Order* compels the state commission to grant such a conditional designation (though a state commission is free to make such a grant).

D. The *Order* Did Not Eliminate Federal Universal Service Support For Remote Areas.

The FCC recognized that the cost of deploying terrestrial networks can be extremely high in remote areas of the nation, and so it concluded that it should eventually support such areas through a new fund. *See Order* ¶¶533-38 (JA at 564-566). This remote areas fund is intended to help consumers "obtain affordable broadband through alternative technology platforms such as satellite and unlicensed wireless." *Id.* ¶533 (JA at 564-565). The *Order*

budgeted $100 million annually for the fund but sought comment "on the details of distributing support" in an accompanying FNPRM. *Id.* ¶¶534, 1223-90 (JA at 565, 819-834).

Petitioners seem to think the FCC eliminated universal service support to remote areas pending enactment of those rules. *See* Br. 52-53. It did not. Until the distribution rules are in place (*see Order* ¶167 (JA at 455)), extremely high-cost areas will continue to receive support under existing mechanisms for price cap and rate-of-return carriers, *see id.* ¶¶133 (JA at 442) (freezing support for price-cap carriers), 195 (JA at 465) (maintaining support for rate-of-return carriers). It follows that petitioners' claim that the *Order* "denied" support to extremely high-cost areas is incorrect and not ripe. *See Qwest*, 240 F.3d at 894-95; *Los Alamos Study Group*, 692 F.3d at 1064-65.

VI. THE FCC GAVE ADEQUATE NOTICE AND OPPORTUNITY TO COMMENT ON THE RULE CHANGES IN THE *ORDER*.

Petitioners complain that the FCC violated the notice-and-comment requirements of the APA, 5 U.S.C. §553(b). *See* Br. 58-59. That provision requires notice of "either the terms or substance of the proposed rule or a description of the subjects and issues involved." 5 U.S.C. §553(b)(3). "Since the public is generally entitled to submit their views and relevant data on any

proposals, the notice must be sufficient to fairly apprise interested parties of the issues involved, but it need not specify every precise proposal which [the agency] may ultimately adopt as a rule." *Nuvio Corp.*, 473 F.3d at 309-10 (internal quotation marks and citations omitted). Petitioners claim that "[k]ey provisions in the Order were not part of the proposed rule." Br. 58. This argument is not properly before the Court, because it was not presented to the FCC either before the FCC issued the *Order* or on reconsideration once the agency allegedly acted without notice. *See* 47 U.S.C. §405(a); *Globalstar, Inc. v. FCC*, 564 F.3d 476, 483-85 (D.C. Cir. 2009) (explaining that 47 U.S.C. §405(a) applies to claims of lack of APA notice and thus requires the filing of a reconsideration petition as a precondition to obtaining judicial review); *Cellnet Commc'ns, Inc. v. FCC*, 149 F.3d 429, 442-43 (6th Cir. 1998) (same). In any event, petitioners' claims are baseless.

Petitioners broadly assert that the FCC failed to provide notice of the new rules implementing the Access Recovery Charge ("ARC") mechanism. Br. 58. Not so. The FCC sought comment on those rules twice. In the NPRM released on February 9, 2011, the FCC "s[ought] comment … on possible recovery of reduced intercarrier compensation through a variety of mechanisms, including through end-user charges such as modifications to the interstate SLC cap." *NPRM* ¶545 (SJA at 172). Subsequently, in an August

3, 2011, Public Notice published in the Federal Register, the FCC sought comment on "the appropriate recovery mechanism for ICC reform, including the ABC Plan's … recovery proposals." *See Further Inquiry Into Certain Issues in the Universal Service-Intercarrier Compensation Transformation Proceeding*, 26 FCC Rcd 11112, 11124 (2011) ("*August 3, 2011, Public Notice*") (JA at 361); 76 Fed. Reg. 49,401-01 (Aug. 10, 2011). The ARC, as adopted in the *Order*, is largely modeled on the ABC Plan. *Compare Order* ¶¶850-53 (JA at 684-688) *with* Letter from Robert W. Quinn, AT&T, *et al.*, WC Docket 10-90 *et al.*, Attachment 1 at 11-13 (filed July 29, 2011) ("ABC Plan") (JA at 2999-3001).

Likewise, the FCC twice proposed to adopt "a dual process for ICC revenue recovery." Br. 59; *see NPRM* ¶451 (SJA 138) (seeking "comment on an incentive regulation framework for any intercarrier compensation replacement funding that would be distributed through the CAF to carriers that currently set their access charges based on a rate-of-return framework"); *August 3, 2011, Public Notice*, 26 FCC Rcd at 11125-26 (JA at 362-363) (seeking comment on separate recovery mechanisms for price cap and rate-of-return carriers).

Petitioners further allege that the FCC, without notice, amended its price cap rules to eliminate exogenous adjustments. Br. 59. The agency did

give notice, however. In the *NPRM*, it expressly "s[ought] comment regarding whether there is any basis under the Commission's price cap rules for concluding that an exogenous adjustment should not be permitted due to the transitional reduction in [Interstate Access Support]." *NPRM* ¶235 (SJA at 82-83).

Finally, the FCC sought comment on "an exclusive right of first refusal" for price cap carriers in the *August 3, 2011, Public Notice*, 26 FCC Rcd at 11114-15 (JA at 351-352). *See* Br. 59.

VII. THE FCC REASONABLY DECIDED TO ADDRESS UNIVERSAL SERVICE CONTRIBUTIONS IN A SEPARATE PROCEEDING.

The USF is financed through "assessments paid by interstate telecommunications service providers." *RCA I*, 588 F.3d at 1099. Fund assessments paid by contributors are determined by applying a quarterly "contribution factor" to the contributors' interstate revenues. *Id*. Contributors "almost always pass their contribution assessments through to their customers." *Id*.

Petitioners allege that the FCC erred by only addressing universal service distributions and not also contributions in the *Order*. *See* Br. 34-36. According to petitioners, the FCC's failure to "widen[] the … base" against which universal service contributions are assessed will render voice and

broadband services less affordable, and contributions inequitable, in violation of 47 U.S.C. §254(b)(1) and (4), respectively. *Id*. at 34.

As petitioners acknowledge, the FCC in a separate rulemaking docket has "s[ought] comment on proposals to reform and modernize how Universal Service Fund … contributions are assessed and recovered." Br. 35; *see Universal Service Contribution Methodology; A National Broadband Plan for Our Future*, 27 FCC Rcd 5357, 5358 (2012); *see also id*. at 5389-92 (¶¶65-72) (requesting comment on extending USF assessments to broadband Internet access service). Given the FCC's well-established discretion under 47 U.S.C. §154(j) to define the scope of its own proceedings, the agency acted properly in addressing universal service contributions elsewhere. *See FCC v. Pottsville Broad. Co*., 309 U.S. 134, 138 (1940) (providing that "subordinate questions of procedure," including the "scope of the inquiry," are "explicitly and by implication left to the Commission's own devising, so long … as it observes the basic requirements designed for the protection of private as well as public interest").

The FCC's decision to address contributions later is also entirely consistent with precedent upholding the agency's authority to act incrementally. As this Court has found, "the FCC is not required to address all problems 'in one fell swoop,' and may focus on problems depending on

their acuteness." *Sorenson I*, 567 F.3d at 1222 (citing *NAB v. FCC*, 740 F.2d 1190, 1207 (D.C. Cir. 1984)); *see also Brand X*, 545 U.S. at 1002 (affirming the FCC's decision to incrementally address the regulatory framework for different categories of facilities-based information service providers).

In any event, petitioners' arguments lack merit. Noting that "telecommunications voice revenues are declining," petitioners assert that universal service contributions levied on consumers will increase and render service less affordable, in violation of section 254(b)(1), "unless the contribution base is widened." Br. 34-35. But, if anything, the *Order* promotes affordability by "[f]or the first time … establish[ing] a defined budget for the high-cost component of the universal service fund." *Order* ¶123 (JA at 437-438). Had the FCC not established a budget, (*id*. ¶125 (JA at 438)), ever-growing demand for subsidies would have resulted in greater increases in the USF contributions paid by consumers, over and above any increase resulting from a decline in telecommunications revenues.

There is likewise no merit to petitioners' argument that it is "inequitable" under section 254(b)(4) to provide universal service support for broadband, but not also assess USF contributions against broadband service revenues. Br. 35. Nothing in section 254(b)(4) requires the recipients of universal service support to also contribute to the USF. Indeed, distributions

and contributions are distinct: the former concerns which providers should receive support (and how much) to preserve and advance universal service, *see* 47 U.S.C. §254(b), whereas the latter concerns which providers should be required to help fund that effort, *see id.* §254(d). Thus, "there is always likely to be a disparity between the contributions parties make to the USF and the amounts that they receive from the USF." *Order* ¶312 (JA at 504).

CONCLUSION

The petitions for review should be dismissed in part and otherwise denied.

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CERTIFICATE OF COMPLIANCE
Certificate of Compliance With Type-Volume Limitations, Typeface Requirements, Type Style Requirements, Privacy Redaction Requirements

1. This brief complies with the type-volume limitation of the Second Briefing Order. It does not exceed 15% of the size of the brief to which it is responding. The Joint Universal Service Fund Principal Brief for Petitioners was certified to be 13,190 words in length. Therefore, the FCC may file a response brief up to 15,168 words in length. This brief contains 14,726 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This brief 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.

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July 29, 2013

No. 11-9900

IN THE
UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

IN RE: FCC 11-161

On Petition for Review of
an Order of the Federal Communications Commission

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure, Intervenors in Support of Respondents Re: The Joint Universal Fund Principal Brief submit this Corporate Disclosure Statement.

AT&T Inc. ("AT&T") is a publicly traded corporation that, through its wholly owned affiliates, is principally engaged in the business of providing communications services and products to the general public. AT&T has no parent company, and no publicly held company owns ten percent or more of its stock.

The Verizon companies participating in this filing are Cellco Partnership d/b/a Verizon Wireless and the regulated, wholly owned subsidiaries of Verizon Communications Inc. Cellco Partnership, a general partnership formed under the law of the State of Delaware, is a joint venture of Verizon Communications Inc. and Vodafone Group Plc. Verizon Communications Inc. and Vodafone Group Plc indirectly hold 55 percent and 45 percent partnership interests, respectively, in Cellco Partnership. Both Verizon Communications Inc. and Vodafone Group Plc are publicly traded companies. Verizon Communications Inc. has no parent company. No publicly held company owns 10 percent or more of Verizon

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Vonage Holdings Corporation has no parent corporation and no publicly held corporation owns 10% or more of its stock.

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GLOSSARY

1996 Act	Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (amending the Communications Act of 1934, 47 U.S.C. § 151 *et seq.*)
CAF Phase II	Phase II of the Connect America Fund
Communications Act	Communications Act of 1934, as amended (47 U.S.C. § 151 *et seq.*)
ETC	eligible telecommunications carrier
FCC or Commission	Federal Communications Commission
ILEC	incumbent local exchange carrier
Order	Report and Order and Further Notice of Proposed Rulemaking, *Connect America Fund*, 26 FCC Rcd 17663 (2011)
USF	Universal Service Fund
VoIP	Voice over Internet Protocol

SUMMARY OF ARGUMENT

The FCC persuasively rebuts petitioners' challenges to the universal service components of the *Order*.[1] Intervenors write separately to stress several points.

1. Petitioners challenge the FCC's authority under subsections 254(c) and (e) to condition receipt of federal high-cost support on a recipient's commitment to deploy "dual-use" facilities that can be used to provide both voice and broadband Internet access services. But with petitioners' encouragement, the FCC has long *permitted* recipients to use federal support for that purpose, and no party challenges the lawfulness of that "no-barriers" policy. The *Order* here simply makes that permissive policy mandatory for any provider that accepts high-cost funding. The result is every bit as consistent with subsections 254(c) and (e) as the traditional no-barriers policy is. Indeed, if petitioners' statutory rationale for challenging the broadband condition had merit, the no-barriers policy—a cornerstone of federal broadband policy for ten years—would itself be unlawful.

Petitioners separately argue that, by allowing funding for interconnected VoIP providers without resolving the statutory classification of particular VoIP

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[1] Report and Order and Further Notice of Proposed Rulemaking, *Connect America Fund*, 26 FCC Rcd 17663 (2011) ("*Order*"). Except where otherwise indicated, citations below of the parties' briefs refer to the "Joint Universal Service Fund Principal Brief" of petitioners and the FCC's brief in response.

services, the FCC has triggered a chain of events that may someday lead to the disbursement of universal service funds to "non-telecommunications carriers," which, petitioners contend, cannot lawfully receive such funding. As a threshold matter, that claim presents no justiciable case or controversy. Petitioners lack Article III standing to challenge this aspect of the *Order* because they have not shown—or even alleged—that it has caused them "injury in fact" that is "actual or imminent" rather than "conjectural or hypothetical." Indeed, petitioners have not identified a single "non-telecommunications carrier" that is receiving federal support. For similar reasons, petitioners' claim is also unripe.

In any event, petitioners' statutory-authority claim would lack merit even if it were justiciable. First, as the FCC concluded, its authority under section 254(e) "to support the deployment of broadband networks" does not turn on the classification of particular VoIP *services* offered over those networks. *Order* ¶ 63 n.67. Second, section 706(b) of the Telecommunications Act of 1996 provides independent authority in the narrow context presented here. Although section 706(b) is tightly circumscribed, it provides that, upon an appropriate finding of inadequate deployment, the FCC shall take "action to accelerate deployment" of broadband infrastructure to areas that would otherwise lack it. 47 U.S.C. § 1302(b) (codifying section 706(b)); *see also id.* § 1302(c) (directing the FCC to identify

"geographical areas that are not served by any [broadband] provider"). That is exactly what the FCC has done by providing universal service support for broadband in those areas. Thus, although petitioners are correct that reading section 706(b) more broadly would be legally untenable, they are wrong to challenge the FCC's application of that provision in this narrow context.

2. Petitioners fare no better when challenging the FCC's decision to adopt a fixed budget for federal high-cost funding. The FCC reasonably balanced the benefits of such funding against the inevitable costs to consumers, who must underwrite any increase in fund size by paying higher line-item fees on their phone bills. The FCC also closely analyzed the practical effect of its budgetary decisions on fund recipients and took steps to cushion recipients against any abrupt shortfalls. The FCC thus reasonably faced up to the relevant trade-offs, and its resolution of competing interests falls within the heartland of its administrative discretion.

3. Finally, the FCC reasonably decided to use competitive bidding to distribute CAF Phase II support to carriers serving price-cap areas. Contrary to petitioners' claim, an auction mechanism does not usurp any statutory powers of the states; the states will continue to perform their statutory role of designating providers as eligible telecommunications carriers ("ETCs"), and no carrier may

receive high-cost support *without* an ETC designation. There is also no merit to petitioners' arguments that the FCC inadequately considered concerns that competitive bidding mechanisms will lead to poor service quality or disadvantage small carriers. Those arguments are unripe because the FCC has not yet adopted any auction structure for CAF Phase II or any mechanism for enforcing service commitments by auction winners. There is thus no final agency action to challenge. In any event, the FCC has shown that it will be fully capable of addressing petitioners' concerns when it formulates the relevant rules.

ARGUMENT

I. THE FCC HAS AUTHORITY TO REORIENT THE FOCUS OF THE UNIVERSAL SERVICE FUND FROM NARROWBAND TO BROADBAND TECHNOLOGIES

In their lead argument (*see* Br. 11-28), petitioners challenge two distinct aspects of the *Order*. First, they challenge what they call the "broadband condition": the FCC's decision to predicate universal service support on a recipient's commitment to deploy networks capable of providing robust broadband Internet access services. *See Order* ¶¶ 60-73. Second, petitioners challenge the FCC's separate decision to define the class of supported "voice telephony" services in a technologically neutral manner that includes interconnected VoIP services in addition to conventional circuit-switched telephony. *See id.* ¶ 62. Although petitioners sometimes conflate these two policy decisions, they are separate. The

first decision imposes obligations on federal high-cost support recipients, whereas the second concerns which services and carriers are eligible to receive support in the first place. Petitioners' challenges to both decisions are without merit, and their challenge to the second is non-justiciable as well.

A. The FCC Is Authorized To Condition Funding On The Deployment Of Broadband-Capable Facilities

As the FCC explains (Br. 12-22), it has statutory authority to require high-cost support recipients to invest in broadband-capable networks and to demonstrate their compliance with that funding condition by providing specified broadband services. Rather than repeat the FCC's arguments in full, intervenors will focus on a revealing anomaly at the heart of petitioners' position: they avidly support a program—the "no-barriers" policy—that would logically be unlawful if their rationale for challenging the *Order*'s broadband condition were valid. *See id.* at 17 & n.2 (citing petitioners' comments). But because that rationale is invalid, both the no-barriers policy and the broadband condition are lawful.

Section 254(b) directs the Commission to use federal universal service programs to promote access to broadband services. It requires that "the Commission shall base policies for the preservation and advancement of universal service on" six principles, two of which concern access to information services. 47 U.S.C. § 254(b). Specifically, section 254(b)(2) states that "[a]ccess to advanced

telecommunications *and information services* should be provided in all regions of the Nation." *Id.* § 254(b)(2) (emphasis added). And section 254(b)(3) provides that "[c]onsumers in all regions of the Nation, … should have access to telecommunications *and information services* … that are reasonably comparable to those services provided in urban areas." *Id.* § 254(b)(3) (emphasis added). These principles impose a "mandatory duty" on the FCC. *Qwest Corp. v. FCC*, 258 F.3d 1191, 1200 (10th Cir. 2001) ("*Qwest I*").

Throughout the decade preceding the *Order*, the FCC promoted these statutory goals in part by implementing its no-barriers policy. In its pre-*Order* form, that policy permitted, but did not require, carriers to use federal funds to invest in dual-use facilities in order to provide broadband Internet access and other information services alongside traditional telephone services. *See* FCC Br. 12; Fourteenth Report and Order, *Federal-State Joint Board on Universal Service*, 16 FCC Rcd 11244, 11322-23 ¶¶ 199-201 (2001). The FCC found that the "use of support to invest in infrastructure capable of providing access to [such] advanced services" comports with section 254(e). *Id.* at 11322 ¶ 200. As it reasoned, the statute permits support for facilities as well as particular services, and it thus permits initiatives to spur "the deployment of modern *plant* capable of providing access to advanced services," including "data" and "video" services. *Id.* (emphasis

added). That legal determination was plainly correct, and petitioners do not even challenge it. To the contrary, as the FCC shows, petitioners' ranks include some of the chief proponents of the no-barriers policy and some of its greatest beneficiaries. *See* FCC Br. 17 & n.2.

The *Order*, however, simply converts the no-barriers policy from a permissive program to a mandatory one. The FCC reasonably concluded that section 254 authorizes it to "go beyond the 'no barriers' policy" and to "require carriers receiving universal service support to invest in modern broadband-capable networks." *Order* ¶ 65. "[N]othing in section 254," the FCC explained, "requires [it] simply to provide federal funds to carriers and hope that they will use such support to deploy broadband facilities." *Id.* Indeed, that reading would conflict with the FCC's "mandatory duty" (*Qwest I*, 258 F.3d at 1200) to promote the availability of broadband networks and services under section 254(b).

The problem for petitioners is that if the no-barriers policy they champion is lawful (as indeed it is), their statutory logic for challenging the mandatory broadband condition must fail, because that logic would apply equally to prohibit *any* expenditure of federal funds for broadband, whether compulsory or voluntary. *See* FCC Br. 17. Petitioners argue at length (Br. 14-24) that the FCC lacks statutory authority under subsections 254(c) and (e) "to include [broadband

Internet access] on the list of supported services" (*id.* at 14). As a threshold matter (and as the FCC has explained), that argument simply misreads the *Order:* although the FCC could have designated broadband Internet access as a supported service,[2] it elected instead to support the deployment of dual-use, broadband-capable *facilities*. *See Order* ¶¶ 64-65; FCC Br. 20-21.

But even if the FCC had made broadband Internet access itself a supported service—or even if supporting broadband *facilities* were somehow equivalent to supporting broadband *services*—that support could not violate section 254 under petitioners' statutory logic unless the "voluntary" no-barriers policy itself would also violate section 254 under the same logic. Suppose, counterfactually, that petitioners were correct and that spending universal service money on broadband facilities were unlawful on the theory that section 254 permits funding only for "telecommunications services." If so, it would not matter whether a funding recipient puts the money to the prohibited use voluntarily or instead in response to a mandatory funding condition. Either way, the money would be spent for an unlawful purpose. *See* FCC Br. 17-18.

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[2] *See, e.g.*, AT&T Comments, WC Docket No. 10-90, at 112-20 (filed Apr. 18, 2011) ("AT&T 4/18/2011 Comments") (JA at 2132-40) (explaining that sections 254 and 706(b) each independently authorize direct support for broadband Internet access services).

In short, any judicial holding that invalidates the broadband funding condition in question here would disrupt existing business plans under the no-barriers policy, threaten to undermine rural broadband deployment more generally, and subvert Congress's objective, codified in section 254(b), to promote universal "[a]ccess to advanced telecommunications and information services." 47 U.S.C. § 254(b)(2), (b)(3). As the FCC explains, nothing in the Communications Act requires that anomalous result, much less unambiguously so.

B. Petitioners' Complaint About Hypothesized Future Support For "Non-Telecommunications Carriers" Is Both Nonjusticiable And Without Merit

As noted, the FCC elected not to make broadband Internet access a supported service; instead, it designated "voice telephony" as the only such service. *See Order* ¶¶ 62-63. Thus, "[a]s a condition of receiving support," ETCs must "offer voice telephony as a standalone service throughout their designated service area." *Id.* ¶ 80. To ensure technological neutrality, the FCC defined the category of "voice telephony" services broadly to include interconnected VoIP in addition to conventional circuit-switched voice services. *Id.* ¶ 63. The FCC has not identified any VoIP services that would qualify as "telecommunications

services" rather than "information services." *See id.* ¶ 718.[3] But the FCC left intact the underlying requirement that, to receive funding, a state commission must designate the provider as an "eligible telecommunications carrier" within the meaning of sections 214 and 254. *See* Order on Reconsideration, *Federal-State Joint Board on Universal Service*, 27 FCC Rcd 15383, 15384 ¶ 3 (2012) (confirming that states retain "the primary responsibility for performing ETC designations" under 47 U.S.C. § 214(e)(2)).

Petitioners nonetheless speculate that the FCC's approach might someday lead to violations of section 254. They argue that, by allowing funding for

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[3] The definitions of "telecommunications service" and "information service" are "mutually exclusive": a service can be either one or the other but cannot be both. Report and Order and Notice of Proposed Rulemaking, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd 14853, 14862, 14911 ¶¶ 12 n.32, 105 (2005), *aff'd*, *Time Warner Telecom, Inc. v. FCC*, 507 F.3d 205 (3d Cir. 2007); Report to Congress, *Federal-State Joint Board on Universal Service*, 13 FCC Rcd 11830, 11520 ¶ 39 (1998). A "telecommunications carrier" is defined as a "provider of telecommunications services." 47 U.S.C. § 153(51). A provider that offers only information services cannot be a "telecommunications carrier" within the statutory meaning because, by definition, it is not providing any telecommunications services. That said, a provider may voluntarily divide its operations into a retail entity that provides information services to end users and a wholesale affiliate that provides transmission inputs to the retail entity. If the affiliate (or any unaffiliated wholesale provider) offers those inputs in the form of generally available telecommunications services, *it* can qualify as a "telecommunications carrier," even though the retail entity might not. *See generally Order* ¶¶ 968-970; *see also id.* ¶ 71 & n.99.

interconnected VoIP providers without resolving the statutory classification of particular VoIP services, the FCC has opened the door to disbursement of universal service funds to "non-telecommunications carriers." Br. 18; *see id.* 5, 17, 22. That claim presents no justiciable case or controversy and lacks merit in any event.

1. Petitioners' Challenge Presents No Article III Case Or Controversy

A party invoking judicial review bears the burden of proving that its challenge to an agency rule satisfies Article III requirements. *See Steel Co. v. Citizens for a Better Env't*, 523 U.S. 83, 103-104 (1998); *Qwest Commc'ns Int'l, Inc. v. FCC*, 240 F.3d 886, 892-893 (10th Cir. 2001). Here, petitioners have not even tried to carry that burden with respect to their complaints about hypothesized future support for entities that are not "telecommunications carriers." Although the FCC presents that Article III defect in terms of ripeness (Br. 25), it could be phrased in terms of either ripeness or standing, given the close relationship between those two doctrines in this context. *See, e.g.*, *Southern Utah Wilderness Alliance v. Palma*, 707 F.3d 1143, 1157 (10th Cir. 2013) ("doctrines of standing and ripeness substantially overlap in many cases," including where "the question of whether [a party] faces an imminent injury involves similar concerns as whether [the] suit is ripe for adjudication"). Under either articulation, petitioners have not

alleged individualized harms sufficient to satisfy threshold jurisdictional requirements for judicial review.

To satisfy Article III *standing* requirements, petitioners must establish that the relevant FCC decision causes them "injury in fact" that is "actual or imminent, not conjectural or hypothetical." *Friends of the Earth, Inc. v. Laidlaw Envtl. Servs. (TOC), Inc.*, 528 U.S. 167, 180 (2000) (internal quotation marks omitted). Presumably, petitioners would assert that, if the FCC does someday provide support to a provider that is not a "telecommunications carrier," that might mean more competition and less funding for them. But no petitioner has submitted any affidavit or made any other effort to substantiate that any such injury is either likely or imminent.

That failure of proof is unsurprising because the chain of causation that petitioners would have to establish is long, tenuous, and highly speculative. Before any petitioner could possibly suffer a cognizable injury, each of the following events would have to occur. *First*, a retail VoIP provider must apply for ETC status while offering only interconnected VoIP as its "voice telephony" service. *Second*, that provider's VoIP service (and any other relevant service) must be deemed an "information service" and therefore not a "telecommunications service." *Third*, that VoIP provider must nonetheless win an ETC designation

from the relevant state commission. *Fourth*, any funding that the provider receives must threaten to harm a specific petitioner in a concrete and identifiable way—for example, by increasing competitive pressure on that petitioner in a discrete geographic area where they both operate. *See Sherley v. Sebelius*, 610 F.3d 69, 73, 74 (D.C. Cir. 2010) (competitor standing doctrine requires "actual or imminent increase in competition" and "actual, here-and-now injury").

Petitioners make no effort to substantiate the likelihood of any of these preconditions to a finding of injury-in-fact; indeed, they fail to identify even a *single* current recipient of universal service support that, although designated as an ETC, is providing only information services. That evidentiary default is fatal. The conjecture that petitioners "might, at some time in the future and under certain conditions," be injured by an "FCC rule with which it disagrees" "is clearly insufficient to establish standing." *U.S. West, Inc. v. FCC*, 173 F.3d 856 (unpublished), 1999 WL 147342, at *3 (10th Cir. Mar. 18, 1999). And any interest petitioners may have "in the Commission's legal reasoning and its potential precedential effect does not by itself confer standing where, as here, it is 'uncoupled' from any injury in fact caused by the substance of the FCC's adjudicatory action." *Telecommunications Research & Action Ctr. v. FCC*, 917 F.2d 585, 588 (D.C. Cir. 1990). Indeed, "mere precedential effect within an

agency is not, alone, enough to create Article III standing, no matter how foreseeable the future litigation." *Wisconsin Pub. Power, Inc. v. FERC*, 493 F.3d 239, 268 (D.C. Cir. 2007) (per curiam) (internal quotation marks omitted).

For similar reasons, petitioners' challenges to this aspect of the *Order* are also *unripe*, as the FCC explains (Br. 25). "A claim is not ripe for adjudication if it rests upon contingent future events that may not occur as anticipated, or indeed may not occur at all." *Texas v. United States*, 523 U.S. 296, 300 (1998) (internal quotation marks omitted). That principle is dispositive here. Again, petitioners have not attempted to show, nor could they show, that the speculative prospect that non-telecommunications carriers could someday receive universal service support has "an immediate and ongoing impact" on them. *Qwest Commc'ns Int'l, Inc. v. FCC*, 398 F.3d 1222, 1232 (10th Cir. 2005) ("*Qwest II*") (challenge to universal service funding was ripe where petitioners "have adequately stated an immediate and ongoing impact in the face of allegedly dwindling" universal service support); *see also Utah v. U.S. Dept. of Interior*, 210 F.3d 1193, 1198 (10th Cir. 2000) (claims based on harms that were "contingent, not certain or immediate," were not ripe). If a state commission someday confers ETC status on a provider that offers only information services, petitioners might then be able to present a challenge to

that ETC designation. But they have no basis for challenging that hypothetical future designation now.

2. Petitioners' Challenge Is Flawed On The Merits

Quite apart from these threshold Article III defects, petitioners lack any basis on the merits for challenging the FCC's decision to include interconnected VoIP within the class of supported "voice telephony services" while deferring judgment on the statutory classification of those services. As the *Order* explains, the FCC's authority to promote universal service through that inclusive approach "does not depend on whether interconnected VoIP services are telecommunications services or information services." *Order* ¶ 63. In particular, if a given voice offering is a telecommunications service, the FCC has indisputable authority to support that service directly, and if it is an information service, the FCC may "support the deployment of broadband *networks* used to provide such services." *Id.*¶ 63 n.67 (emphasis added). The FCC's brief (at 26-27) rebuts petitioners' arguments to the contrary.[4]

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[4] *See also* AT&T 4/18/2011 Comments at 113-14 (JA at 2133-34) (explaining that the language of section 254(c)(2) would authorize the FCC, if it chose, to designate information services as supported *services*, even outside the schools-and-libraries context addressed in section 254(c)(3)).

Moreover, section 706(b) of the Telecommunications Act of 1996 gives the FCC independent authority in this limited context to provide universal service support for broadband deployment in areas where broadband would otherwise not exist. *See Order* ¶¶ 66-73.[5] Petitioners do not claim that the triggering conditions for section 706(b) have not been met; instead, they argue (Br. 26) that construing the provision to apply here would give the FCC unbounded new powers. That is incorrect: in fact, section 706(b) is exceedingly narrow. By its terms, that provision states simply that, upon a finding of inadequate deployment, the FCC shall take "action to accelerate deployment" of broadband to areas that would otherwise lack it. 47 U.S.C. § 1302(b) (codifying section 706(b)); *see also id.* § 1302(c) (directing the FCC to identify "geographical areas that are not served by any [broadband] provider"). That is exactly what the FCC has done by granting universal service support to promote deployment in the limited high-cost areas that are unserved or that would be unserved absent such support.

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[5] The Commission chose for policy reasons to require funding recipients to "comply with the same universal service rules and obligations set forth in sections 254 and 214." *Order* ¶ 73. But because section 706(b) is an independent source of authority, the FCC could eliminate that requirement if necessary to fund broadband in unserved areas. *See* FCC Br. 27 n.6; *cf. WorldCom, Inc. v. FCC*, 288 F.3d 429, 434 (D.C. Cir. 2002) (remanding without vacating an FCC order where the court found "a non-trivial likelihood that the Commission has the authority" to reach its policy objectives through an alternative legal rationale).

Although section 706(b) is very narrow, petitioners are wrong to claim (Br. 25-26) that section 706(b) grants *no* independent authority for broadband funding in unserved areas and merely exhorts the FCC to exercise the powers it derives from other provisions. That argument ignores the fundamental differences between the terms of sections 706(a) and 706(b). As petitioners correctly observe, section 706*(a)* contains only aspirational language and confers no authority on the FCC. In contrast, section 706*(b)* expressly directs that, when statutory preconditions are met, the FCC "shall take immediate action" to "remov[e] barriers to infrastructure investment" in those limited and specific areas where such investment is lacking. 47 U.S.C. § 1302(b).[6] As the *Order* explains, "one of the most significant barriers to investment in broadband infrastructure" in unserved areas "is the lack of a business case for operating a broadband network." *Order*

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[6] Petitioners conflate the distinction between these two provisions throughout their brief. For example, they assert that, in 1998, the FCC construed section 706 not to grant it independent authority and that it has articulated an inadequate rationale for reversing course. Br. 24-25. But the 1998 order on which petitioners rely analyzed only whether the FCC has regulatory authority under section 706*(a)*, not section 706*(b)*. *See* Memorandum Opinion and Order, *Deployment of Wireline Servs. Offering Advanced Telecommunications Capability*, 13 FCC Rcd 24012, 24044-48 ¶¶ 69-77 (1998). The distinction between these two provisions is critical because section 706(b) is far more targeted in its focus and is a straightforward grant of very limited—but independent—broadband funding authority for unserved areas.

¶ 67 (internal quotation marks omitted). Universal service support is a key traditional means of alleviating such barriers to infrastructure investment in high-cost areas. Those considerations amply distinguish the FCC's universal service initiative here from petitioners' speculation (Br. 26) that the FCC might someday invoke section 706(b) to negate "securities and banking" requirements.

There also is no merit to petitioners' claim (Br. 27-28) that the FCC's use of section 706(b) to extend broadband service and networks to unserved areas undermines some congressional policy judgment embodied in section 254. To be sure, it would be inappropriate to rely on section 706(b) to evade explicit congressional policy choices that are embodied in other sections of the Communications Act or to impose involuntary regulatory burdens on broadband providers, given that section 706(b) specifically directs the FCC to *remove* barriers to infrastructure investment. But those concerns do not arise here because the FCC's funding program presents no conflict with section 254 or any other provision. When Congress enacted section 254 in 1996, virtually all consumers had to rely on conventional telecommunications services for all voice and data services, such as regular circuit-switched telephony for voice and dial-up technologies for access to the Internet. Not until the late 1990s did cable and telephone companies begin widely offering broadband Internet access as a bundled

information service, and VoIP services did not become common until the first years of the new millennium. *See Order* ¶ 71. In short, the category of "telecommunications services" accounted for virtually all consumer voice and data services in 1996, yet Congress nonetheless drafted section 254 to encompass support for both "telecommunications and information services." 47 U.S.C. § 254(b)(2), (b)(3).

That historical context refutes any suggestion that Congress somehow considered and rejected plans to fund the most important communications technology of the 21st century: broadband Internet access, which has supplanted dial-up as the predominant means of accessing any information service. *See generally Order* ¶ 71. In particular, nothing in section 254 could be construed as an affirmative congressional policy choice against promoting broadband through the disbursement of universal service support. On the contrary, by using the specialized term "advanced telecommunications capability" in section 706(b), Congress directed the Commission to accelerate broadband infrastructure deployment in unserved areas whether the ensuing broadband services are classified as "telecommunications services" or as "information services" instead. Section 706(b) thus authorizes the FCC to fund broadband providers that offer only information services. *See Order* ¶ 71; FCC Br. 27 n.6.

Petitioners are also wrong to argue (Br. 27) that FCC action under section 706(b) would "overrid[e] Section 254 limitations" on the theory that section 254, as a more specific provision, controls over the general authority provided by section 706(b). As the D.C. Circuit explained in an analogous context, "[w]hen two statutes apply to intersecting sets [of issues], neither is more specific." *Core Commc'ns, Inc. v. FCC*, 592 F.3d 139, 143 (D.C. Cir. 2010) (internal quotation marks and alterations omitted). That is the case here. Section 254 equips the Commission with authority with respect to universal service in general. Section 706(b) directs the Commission to accelerate broadband deployment in particular by removing barriers to infrastructure investment in those limited geographic areas where the FCC finds that broadband has not been deployed in a reasonable and timely fashion. In deciding whether and how to promote broadband deployment through universal service mechanisms, neither section 254 nor section 706(b) is more specific than the other.

II. THE FCC REASONABLY LIMITED THE SIZE OF THE FUND TO AVOID UNDULY BURDENING THE CONSUMERS WHO MUST PAY FOR THE FUND

Like any funding program, the universal service fund presents difficult trade-offs. Choosing an overall size for the fund is the most fundamental of these, and the *Order* strikes an appropriate balance between competing interests. On the one hand, the FCC wished to create a fund large enough to bring some form of

broadband—whether fixed, mobile, or satellite-based—to as many unserved areas as possible. On the other hand, the money in the fund does not appear from nowhere; it comes from "assessments paid by interstate telecommunications service providers," who "almost always pass their contribution assessments through to their customers." *Rural Cellular Ass'n v. FCC*, 588 F.3d 1095, 1099 (D.C. Cir. 2009) ("*RCA I*").

The FCC thus wished to avoid creating a fund so large that it would harm consumers, who must pay for any increase through higher line-item fees on their phone bills. As the D.C. and Fifth Circuits have explained, "excessive funding may itself violate" section 254 by "causing rates unnecessarily to rise, thereby pricing some consumers out of the market [altogether]." *RCA I*, 588 F.3d at 1103 (quoting *Alenco Commc'ns, Inc. v. FCC*, 201 F.3d 608, 620 (5th Cir. 2000)); *see Qwest I*, 258 F.3d at 1200. In statutory terms, the FCC recognized that it must ensure not only that support will be "specific, predictable, and sufficient," 47 U.S.C. § 254(b)(5), but also that services for consumers throughout the country—including those who do not benefit from universal service programs—will be "available at just, reasonable, and affordable rates," *id.* § 254(b)(1). *See generally Qwest II*, 398 F.3d at 1234 (FCC is "compelled to balance the § 254(b) principles to the extent that they conflict").

Weighing these competing principles, the FCC adopted a fixed budget for the high-cost program. This budget, supported by a "broad cross-section of interested stakeholders," is crucial to "ensure that [the FCC] ha[s] in place 'specific, predictable, and sufficient' funding mechanisms to achieve [its] universal service objectives." *Order* ¶¶ 122-123 & n.192. In particular, the fixed budget the FCC chose, which it based on FY2011 support levels, will "stabilize the contribution burden," *id.* ¶ 14, will "minimize disruption" in the administration of the fund, *id.* ¶ 125, and will suffice to meet funding needs "given the substantial reforms" the *Order* adopts "to address long-standing inefficiencies and wasteful spending," *id.* The Commission "enjoys broad discretion when conducting exactly this type of balancing" between competing statutory objectives. *RCA I*, 588 F.3d at 1103.

Petitioners nonetheless argue (Br. 31) that the FCC "improperly limited its analysis to whether, without reform, USF support would be *excessive*" and ignored the statutory direction to ensure sufficient support for rate-of-return carriers. That is not a defensible reading of the *Order*, as the FCC's brief explains (at 33-34). The FCC carefully considered the impact of its reforms on rate-of-return carriers, such as petitioners here, to ensure sufficient funding levels for rural areas. *See* *Order* ¶¶ 285-294. It pared back legacy funding for rate-of-return carriers "in a

gradual manner" so as not to "jeopardize service to consumers or investments made consistent with existing rules." *Id.* ¶ 285. And it established a waiver mechanism to address unforeseen funding shortfalls. *See id.* ¶¶ 126, 294.[7] The FCC's "balancing calculus" with respect to rate-of-return carriers thus "t[ook] into account the full range of principles Congress dictated to guide the Commission in its actions." *Qwest II*, 398 F.3d at 1234.

Petitioners' real complaint is thus not that the FCC failed to consider the "sufficiency" of support levels at all, but that it struck what they consider a suboptimal balance between "sufficiency" of support and competing statutory objectives. That challenge is untenable. As used in section 254, the term "sufficient" is "ambiguous as to what constitutes 'sufficient' support." *Texas Office of Pub. Util. Counsel v. FCC*, 183 F.3d 393, 425 (5th Cir. 1999). And whether the FCC "has sufficiently and explicitly supported universal service" "go[es] directly to the heart of FCC expertise." *Alenco*, 201 F.3d at 620.

Petitioners do not begin to overcome the "substantial judicial deference," *Alenco*, 201 F.3d at 620, that the FCC receives for such judgment calls. They

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[7] The D.C. Circuit has twice held that the existence of such safety valves answers charges that interim caps for funding violated the section 254 sufficiency criterion. *See Rural Cellular Ass'n v.* FCC, 685 F.3d 1083, 1095 (D.C. Cir. 2012); *RCA I*, 588 F.3d at 1104; *see also* FCC Br. 35 & n.7.

contend, for example, that the FCC failed to "quantify[] the substantial added cost[s] of satisfying the broadband condition" imposed on rate-of-return carriers. Br. 30, 32. But the FCC made a reasonable predictive judgment that it could ensure sufficient support by (1) building substantial flexibility into those carriers' broadband service obligations, *e.g.*, *Order* ¶¶ 206, 533, (2) adopting various funding reforms that will yield substantial savings and efficiencies, *id.* ¶¶ 194-279, and (3) creating a new explicit recovery mechanism to replace gradual reductions in intercarrier compensation revenues, *id.* ¶ 291. *See generally id.* ¶¶ 287-288. The FCC, moreover, made uncontested findings that "9 out of 10 rate-of-return carriers" will see funding increase, stay the same, or decrease "less than 20 percent annually." *Id.* ¶ 290. Finally, petitioners identify "no cost data showing they would, in fact, have to leave customers without service as result" of the *Order*, and for that reason alone, there is no "valid reason to believe the principle of 'sufficiency' … will be violated." *RCA I*, 588 F.3d at 1104.

III. THE FCC IS AUTHORIZED TO USE A REVERSE-AUCTION MECHANISM TO ALLOCATE CAF PHASE II FUNDING IN PRICE-CAP AREAS

The incumbent local exchange carriers ("ILECs") eligible for universal service funding fall into two main categories. Some ILECs, including the smallest ones, are subject to traditional *rate-of-return* regulation, which allows carriers to charge rates designed to ensure a reasonable return on the prudently incurred

investments recorded in their accounting books. Other ILECs are subject to *price-cap* regulation, which provides no similar assurance of cost recovery and, over the long term, prescribes rate caps mainly on the basis of non-carrier-specific criteria, such as the rate of inflation. Price-cap regulation gives carriers additional incentives to increase their efficiency because, unlike rate-of-return carriers, they have no guaranteed margins but *can* retain any extra profits they obtain through diligent cost-cutting. *See generally National Rural Telecom Ass'n v. FCC*, 988 F.2d 174, 177-178 (D.C. Cir. 1993).

As the *Order* explains, "[m]ore than 83 percent of the approximately 18 million Americans who lack access to fixed broadband live in price cap study areas," *Order* ¶ 127, yet such areas accounted for only 25% of high-cost support in 2010, *see id.* ¶ 158. The *Order* reorients the universal service fund to correct this anomaly and establishes two phases of augmented funding for carriers that agree to serve areas traditionally subject to price-cap regulation, including price-cap ILECs as well as non-ILECs that are not themselves subject to price-cap regulation. Petitioners object mainly to the Commission's use of reverse auctions ("competitive bidding" mechanisms) for determining who will receive support during the second of these phases: CAF Phase II, which has not yet begun. *See* Br. 48-51. As petitioners acknowledge (*id.* at 48 n.26), auctions are likely to play a

major role in distributing universal service support only after the initial five-year period of CAF Phase II.[8]

Petitioners argue that the use of auctions for allocating universal service support will "unlawfully strip[]" state commissions of their role under section 214(e) "of deciding *who* would receive universal service support." Br. 40. That is incorrect. Section 214(e) provides only that state commissions shall "designate" carriers as "eligible" to receive support. 47 U.S.C. § 214(e)(2). The *Order* fully accommodates that authority: under the *Order*, no carrier may participate in an auction unless it has been designated as an ETC by the relevant commission. *See, e.g.*, *Order* ¶ 1199; *see generally* FCC Br. 61.

Petitioners also claim (Br. 48-51) that the FCC inadequately considered concerns that competitive bidding mechanisms will result in poor service quality and disadvantage small carriers. As an initial matter, these claims are unripe

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[8] The FCC has granted each price-cap ILEC a "right of first refusal" to receive five years of support within a given state if it agrees to offer, among other things, a defined level of broadband service to all designated areas in that state by the end of the five-year term. *Order* ¶ 160. During that period, therefore, auctions will be held only insofar as ILECs opt out of this arrangement and the FCC needs to identify substitute providers. Auctions are expected to play a greater role after that period, when the right of first refusal expires and the opportunity to provide supported services will likely be opened up more broadly to competitive bidding. *Id.* ¶ 178.

because there is no final agency action to challenge. *See Schanzenbach v. Town of La Barge*, 706 F.3d 1277, 1281 (10th Cir. 2013) (the "requirement of final agency action is a general requirement for ripeness"). Despite petitioners' contrary suggestion, the FCC did not adopt (and still has not adopted) any particular auction structure for use in CAF Phase II or any mechanism for ensuring compliance with performance commitments. Instead, it issued a further notice of proposed rulemaking and invited comment on how to design such an auction. *See Order* ¶ 1190. And the FCC expressly sought comment in an *FNPRM* on the very topics that petitioners claim it ignored: service performance requirements for auction winners, *see id.* ¶¶ 1203-1204, and various issues concerning auction design, including the role of "small businesses" in the auction process, *e.g.*, *id.* ¶ 1213. As the FCC explains, any review of the FCC's CAF Phase II auction mechanism must await the future order that will create that mechanism. *See* FCC Br. 53-54.

In any event, the FCC's discussion of the auction mechanism that it *did* establish in the *Order*—in connection with the separate Mobility Fund—demonstrates that the FCC is acutely aware of the need to structure competitive bidding to address the concerns petitioners raise prematurely here. Petitioners assert, for example, that the FCC "ignored" arguments that "[b]idders in an auction system will face significant cost pressure to construct facilities meeting minimal

performance specifications." Br. 48, 49. But the FCC acknowledged that concern in connection with the Mobility Fund and explained that the solution lies in "defin[ing] clear performance standards and effective enforcement of those standards, as is prudent when seeking any commitment for specific performance." *Order* ¶ 325. As the *FNPRM* confirms, the Commission will be every bit as focused on that concern when it designs the auction mechanism for CAF Phase II. *See, e.g.*, *id.* ¶ 1203.

More generally, petitioners' concerns about incentives to "skimp on service quality" (Br. 50) are hardly specific to auctions. Regulators began implementing the price-cap approach in the 1980s and 1990s to avoid the perverse incentives that rate-of-return regulation gives carriers to "gold-plat[e]" their networks, safe in the expectation that they "can pass any cost along to ratepayers (unless it is identified as imprudent)." *National Rural Telecom Ass'n*, 988 F.3d at 178. At the time, some parties claimed that the shift to price-cap (or "incentive") regulation would present the same "race to the bottom" service quality concerns that petitioners raise here. There was no basis for such concerns then, and there is even less of a basis now. Competitive bidding for universal service support involves a standard offer-and-acceptance arrangement whereby providers agree to serve a particular area in exchange for meeting certain terms and conditions, including service quality

provisions. And there will be defined consequences for failure to comply. The same issues are presented in virtually all government contracts, which are nearly always subject to competitive bidding. The FCC is fully competent to address those issues here.

Finally, there is no basis for petitioners' claim that the FCC improperly disregarded their concerns that "an auction system would unduly favor large carriers over smaller carriers." Br. 49, 51.[9] As noted, the FCC did not disregard petitioners' arguments; instead, it sought additional comment on the role of small businesses in the CAF II auction process, *Order* ¶ 1213, and petitioners' challenge is thus unripe. In any event, the FCC *did* address "small business" concerns in the context of the separate Mobility Fund, and it found no evidence there that "small businesses are unable to meaningfully participate in a well-designed and executed reverse auction." *Id.* ¶ 326. Petitioners do not dispute that analysis on the merits;

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[9] Petitioners complain that "[i]f a carrier with existing networks in rural areas is a large one," it will likely enjoy "natural advantages" in a reverse auction because it can bid to provide service at a lower cost than alternative providers with smaller (or no) existing networks in those areas. Br. 51 (internal quotation marks omitted). Petitioners apparently wish to neutralize these "natural advantages" by making it more difficult to win a reverse auction with a low bid; under their approach, a higher bidder could win simply by virtue of being small, even if it would need to extract more money from the fund. That outcome would undermine a central goal of the universal service program: providing affordable service to the greatest number of households at the lowest cost to consumers in general.

instead, they respond only that, "[s]ince such an auction was not part of the *Order*, it is not susceptible to judicial review." Br. 51. Of course, that is our point: judicial review would be premature precisely because the FCC has not yet issued a final order adopting any CAF Phase II auction mechanism.

CONCLUSION

For the reasons stated above and in the FCC's brief, the relevant petitions for review should be denied.

Respectfully submitted,

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1. This brief contains 6714 words of the 21,400 words the Court allocated for the briefs of intervenors in support of the FCC in its October 1, 2012 Order Consolidating Case No. 12-9575 with Other FCC 11-161 Cases, Establishing Windstream Briefing Schedule, and Modifying Intervenor Participation. The intervenors in support of the FCC have complied with the type-volume limitation of that order because their briefs, combined, contain a total of fewer than 21,400 words, excluding the parts of those briefs exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This brief 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 brief has been prepared in a proportionally spaced typeface using Microsoft Word 2010 in 14-point Times New Roman font.

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July 29, 2013

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July 29, 2013

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I hereby certify that on July 29, 2013, I caused the foregoing Combined Responses of Federal Respondents and Supporting Intervenors to the Joint Universal Service Fund Principal Brief to be filed by delivering a copy to the Court via e-mail at FCC_briefs_only@ca10.uscourts.gov. I further certify that the foregoing document will be furnished by the Court through (ECF) electronic service to all parties in this case through a registered CM/ECF user. This document will be available for viewing and downloading on the CM/ECF system.

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