Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	

FURTHER NOTICE OF PROPOSED RULEMAKING

Adopted: January 10, 2001 **Released: January 12, 2001**

Comment Date: 30 days after publication in the Federal Register
Reply Comment Date: 45 days after publication in the Federal Register

By the Commission:

I. INTRODUCTION

1. In this Further Notice of Proposed Rulemaking (Further Notice), we seek comment on the Recommended Decision of the Federal-State Joint Board on Universal Service (Joint Board) regarding a plan for reforming the rural universal service support mechanism.[1] The Joint Board sent to the Commission the Rural Task Force Recommendation as a good foundation for implementing a rural universal service plan that benefits consumers and provides a stable environment for rural carriers to invest in rural America.[2] The Joint Board also identified specific issues for the Commission to address in implementing the Rural Task Force plan.[3]

II. BACKGROUND

2. The Rural Task Force Recommendation is a proposal for the distribution of universal service support to rural carriers.[4] It represents the consensus of individual Rural Task Force members, who work for a broad range of interested parties, including rural telephone companies, competitive local exchange carriers, interexchange carriers, wireless providers, consumer advocates, and state and federal government agencies. The Rural Task Force offers its Recommendation as an integrated package, and asks that it be adopted without modification. The Recommendation is designed to be implemented immediately and to remain in place over a five-year period.[5]

---

[1] *In the Matter of Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision, FCC 00J-4 (released December 22, 2000) (Recommended Decision). The Recommended Decision, which incorporates the Rural Task Force Recommendation as Appendix A, is attached hereto as Attachment 1.

[2] *Recommended Decision*, FCC 00J-4 at paras. 1, 10-13. The Rural Task Force was appointed by the Joint Board, and presented its Recommendation to the Joint Board on September 29, 2000. *Id.* at para. 5.

[3] *Id.* at paras. 15-19.

[4] *Id.* at para. 5. "Rural carriers" are local exchange carriers (LECs) that meet the definition of a rural telephone company contained in section 153(37) of the 1996 Act. 47 U.S.C. § 153(37).

[5] *Recommended Decision*, FCC 00J-4 at para. 5.

3. The Rural Task Force recommends the use of a modified version of the current high-cost loop support mechanism, based on carriers' embedded costs.[6] It proposes various upward adjustments to current limits on high-cost loop support for rural carriers.[7] The Rural Task Force also recommends that per-line support levels within a study area become fixed once a competitive eligible telecommunications carrier begins providing service in the study area.[8] In addition, the Rural Task Force proposes the use of a new annual index to adjust the limits on high-cost loop support, and to adjust per-line support levels in competitive study areas on a going-forward basis.[9] It also suggests other reforms, such as a "safety valve" mechanism to provide additional support for meaningful post-transaction investment in high-cost telephone exchanges acquired by rural carriers, provision of "safety net additive" support in years in which the cap is triggered for rural carriers with over 14 percent growth in telecommunications plant in service, and a flexible system for disaggregating and targeting per-line support.[10]

III. ISSUES FOR COMMENT

4. We seek comment on the Joint Board's conclusion that the Rural Task Force Recommendation is a good foundation for implementing a rural universal service plan for the next several years. Should we adopt the Rural Task Force plan as a means of providing stability to rural carriers over the next several years and encouraging investment in rural infrastructure?[11] Does the Rural Task Force plan provide for universal service support that is sufficient for purposes of the Telecommunications Act of 1996?[12] Parties should comment on the public policy implications of the Rural Task Force plan and/or particular aspects of the plan, including its potential effects on the competition and universal service goals of the 1996 Act, and whether and how it would promote consumer welfare. Parties also should address how small business entities, including small incumbent local exchange carriers and new entrants, will be affected by the Rural Task Force plan.[13]

5. We also seek comment on specific implementation issues identified by the Joint Board, as well as any other issues related to implementation of the Rural Task Force Recommendation. First, we invite commenters to address the proposed safety valve mechanism for providing additional support to rural carriers that make meaningful post-transaction investments in acquired exchanges.[14] How should safety valve support be distributed if the total amount of support for which rural carriers are eligible exceeds the

[6] *Id.* at para. 6; *see* 47 C.F.R. §§ 36.601, *et seq.* The Rural Task Force recommends continuation of the other two federal support programs available to rural carriers, Long Term Support and Local Switching Support. *See Recommended Decision*, FCC 00J-4 at para. 6.

[7] *See id.* at para. 7, Appendix A at §§ IV(B)(1)(a), IV(B)(2). The proposed adjustments include recomputing the indexed cap on high-cost loop support and the corporate operations expense limitation as if they had not been in effect for the calendar year 2000.

[8] *See id.* at 4-5, para. 7, Appendix A at § IV(B)(1)(c). Under the Rural Task Force's proposal, both the incumbent carrier and the competitive eligible telecommunications carrier would receive fixed per-line support.

[9] *See id.* at 5, para. 8, Appendix A at § IV(B)(1)(b). The proposed "rural growth factor" would be the sum of annual line growth for rural carriers and a general inflation factor (Gross Domestic Product-Chained Price Index). *Id.*

[10] *Id.* at paras. 7-9, Appendix A at §§ IV(B)(1)(e), IV(B)(3), V(A).

[11] *See id.* at para. 5.

[12] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (1996 Act); *see Recommended Decision*, FCC 00J-4 at para. 12.

[13] *See* Regulatory Flexibility Act, 5 U.S.C. §§ 601, *et seq.*

[14] *See Recommended Decision*, FCC 00J-4 at para. 16, Appendix A at § IV(B)(3).

proposed cap of five percent of the high-cost loop support fund? How should "meaningful investment" be defined for purposes of safety valve support?[15] Should a carrier's safety valve support transfer to a different carrier as a result of a subsequent transfer of exchanges? Should safety valve support be fixed in competitive study areas in the same manner as other high-cost loop support, or would such an approach unduly dissuade investment? We invite commenters to address these and any other issues involved in implementing a safety valve mechanism.

6. Second, we invite commenters to address implementation of the Rural Task Force proposal to fix per-line support in competitive study areas. The Joint Board agreed with the Rural Task Force that the Commission should fix support when a competitor begins providing services in a given study area, but stated that "it is unclear how the high-cost loop fund cap would account for fixed rural carrier support."[16] We seek comment from interested parties, including the Rural Task Force, on the relationship of the cap on high-cost loop support to fixed per-line support in competitive study areas. We also seek comment on whether the proposed ability of incumbent LECs to adjust their fixed per-line support levels to recover costs associated with catastrophic events should be limited by the availability of support from other sources, such as insurance, Rural Utilities Service loans, and federal or state emergency management relief.[17] Commenters are invited to address these and any other issues involved in implementing the provisions of the Rural Task Force plan for support in competitive study areas.

7. Third, we seek comment on the Rural Task Force proposal to make above-the-cap safety net additive support available in years in which the cap on high-cost loop support is triggered to rural carriers with over 14 percent growth in telecommunications plant in service. As proposed, would the safety net additive mechanism enable rural carriers to recover more than 100 percent reimbursement on their incremental loop investment?[18] If so, how should the mechanism be modified? We invite commenters to address this and any other safety net additive implementation issues. Finally, we invite interested parties to comment on any other issues related to implementation of the Rural Task Force plan.

IV. PROCEDURAL ISSUES

A. Ex Parte Presentations

8. This is a permit but disclose rulemaking proceeding. Ex parte presentations are permitted, except during the Sunshine Agenda period, provided that they are disclosed as provided in the Commission's rules.[19]

B. Initial Regulatory Flexibility Analysis

9. As required by the Regulatory Flexibility Act (RFA),[20] the Commission has prepared this

[15] For example, is it more appropriate to define meaningful investment so that the "index year expense adjustment" is the year prior to the subsequent year "expense adjustment"? As currently proposed, the index year expense adjustment would be the study area's high-cost loop support expense adjustment calculated at the end of the acquiring company's first year of operations. *See id.* at para. 16, n. 47.

[16] *Id.* at para. 17.

[17] *See id.* at para. 18.

[18] *See id.* at para. 19.

[19] *See generally* 47 C.F.R. §§ 1.1202, 1.1203, and 1.1206.

[20] *See* 5 U.S.C. § 603. The RFA, *see* 5 U.S.C. § 601 *et seq.*, has been amended by the Contract with America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) (CWAAA). Title II of the CWAAA is the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA).

Initial Regulatory Flexibility Analysis (IRFA) of the possible significant economic impact on small entities of the proposals in this Further Notice. Written public comments are requested on the IRFA. These comments must be filed in accordance with the filing deadlines set forth below in paragraphs 31-35, and should have a separate and distinct heading designating them as responses to the IRFA. The Commission will send a copy of the Further Notice, including this IRFA, to the Chief Counsel for Advocacy of the Small Business Administration (SBA) in accordance with the RFA.[21] In addition, the Further Notice and IRFA (or summaries thereof) will be published in the Federal Register.[22]

1. Need for, and Objectives of, the Proposed Rules

10. The 1996 Act requires the Commission to consult with the Joint Board in implementing section 254, which establishes a number of principles for the preservation and advancement of universal service in a competitive telecommunications environment.[23] The Commission initiated this proceeding to consider the Recommended Decision of the Joint Board regarding a rural universal service plan developed by the Rural Task Force. The Rural Task Force plan is a proposal for the distribution of universal service support to rural carriers which is designed to be implemented immediately and to remain in place over a five-year period. The Joint Board found that the Rural Task Force sought to achieve the goals of the 1996 Act to preserve and advance universal service, facilitate competition in rural areas, and provide a predictable level of universal service support. The Joint Board stated that the Rural Task Force plan would provide rural carriers with stability for planning their investments over the next several years, while seeking to encourage competition in high-cost areas through a flexible system for disaggregating support to establish the portable per-line support amount available to all eligible telecommunications carriers. The Joint Board found that additional support under the plan is "generally designed to provide carriers serving rural areas with increased incentives to invest in new infrastructure and technologies." In sum, the Joint Board recommended the Rural Task Force plan to the Commission as a good foundation for implementing a rural universal service plan that benefits consumers and provides a stable environment for rural carriers to invest in rural America.

2. Legal Basis

11. This rulemaking action is supported by sections 4(i), 4(j), 201, 205, 254, and 403 of the Communications Act of 1934, as amended.[24]

3. Description and Estimate of the Number of Small Entities to Which the Notice will Apply

12. The RFA directs agencies to provide a description of, and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules, if adopted.[25] The RFA generally defines "small entity" as having the same meaning as the term "small business," "small organization," and "small governmental jurisdiction."[26] In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act, unless the Commission has developed one or

[21] *See* 5 U.S.C. § 603(a).

[22] *See id.*

[23] 47 U.S.C. § 254.

[24] 47 U.S.C. §§ 154(i), 154(j), 201-205, 254, and 403.

[25] 5 U.S.C. § 603(b)(3).

[26] 5 U.S.C. § 601(6).

more definitions that are appropriate to its activities.[27] Under the Small Business Act, a "small business concern" is one that: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) meets any additional criteria established by the SBA.[28]

13. We have included small incumbent carriers in this RFA analysis. A "small business" under the RFA is one that, *inter alia*, meets the pertinent small business size standard (*e.g.*, a telephone communications business having 1,500 or fewer employees), and "is not dominant in its field of operation."[29] The SBA's Office of Advocacy contends that, for RFA purposes, small incumbent carriers are not dominant in their field of operation because any such dominance is not "national" in scope.[30] We have therefore included small incumbent carriers in this RFA analysis, although we emphasize that this RFA action has no effect on the Commission's analyses and determinations in other, non-RFA contexts.

14. *Local Exchange Carriers*. Neither the Commission nor the SBA has developed a definition for small providers of local exchange services. The closest applicable definition under the SBA rules is for telephone communications companies other than radiotelephone (wireless) companies.[31] According to the most recent *Telecommunications Industry Revenue* data, 1,348 incumbent carriers reported that they were engaged in the provision of local exchange services.[32] We do not have data specifying the number of these carriers that are either dominant in their field of operations, are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of local exchange carriers that would qualify as small business concerns under the SBA's definition. Of the 1,348 incumbent carriers, 13 entities are price cap carriers that would not be subject to the rules, if adopted. Consequently, we estimate that fewer than 1,335 providers of local exchange service are small entities or small incumbent local exchange carriers that may be affected by the proposed Rural Task Force plan.

15. *Competitive Access Providers*. Neither the Commission nor the SBA has developed a definition of small entities specifically applicable to competitive access services providers (CAPs). The closest applicable definition under the SBA rules is for telephone communications companies other than except radiotelephone (wireless) companies.[33] According to the most recent *Trends in Telephone Service*

---

[27] 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 5 U.S.C. § 632). Pursuant to 15 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition in the Federal Register."

[28] 15 U.S.C. § 632.

[29] 5 U.S.C. § 601(3).

[30] *See* Letter from Jere W. Glover, Chief Counsel for Advocacy, SBA, to William E. Kennard, Chairman, FCC (May 27, 1999). The Small Business Act contains a definition of "small business concern," which the RFA incorporates into its own definition of "small business." *See* U.S.C. § 632(a) (Small Business Act); 5 U.S.C. § 601(3) (RFA). SBA regulations interpret "small business concern" to include the concept of dominance on a national basis. 13 C.F.R. § 121.102(b). Since 1996, out of an abundance of caution, the Commission has included small incumbent LECs in its regulatory flexibility analyses. *See, e.g.*, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket, 96-98, First Report and Order, 11 FCC Rcd 15499, 16144-45 (1996).

[31] 13 C.F.R. § 121.201, SIC Code 4813.

[32] FCC, Common Carrier Bureau, Industry Analysis Division, *Trends in Telephone Service*, Table 19.3 (March 2000)

[33] 13 C.F.R. § 121.201, SIC code 4813.

data, 212 CAPs/competitive local exchange carriers and 10 other local exchange carriers reported that they were engaged in the provision of competitive local exchange services.[34] We do not have data specifying the number of these carriers that are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of CAPs that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are less than 212 small entity CAPs and 10 other local exchange carriers that may be affected by the proposed Rural Task Force plan.

16. *Cellular Licensees*. Neither the Commission nor the SBA has developed a definition of small entities applicable to cellular licensees. Therefore, the applicable definition of small entity is the definition under the SBA rules applicable to radiotelephone (wireless) companies. This provides that a small entity is a radiotelephone company employing no more than 1,500 persons.[35] According to the Bureau of the Census, only twelve radiotelephone firms from a total of 1,178 such firms which operated during 1992 had 1,000 or more employees.[36] Therefore, even if all twelve of these firms were cellular telephone companies, nearly all cellular carriers were small businesses under the SBA's definition. In addition, we note that there are 1,758 cellular licenses; however, a cellular licensee may own several licenses. In addition, according to the most recent *Telecommunications Industry Revenue* data, 808 carriers reported that they were engaged in the provision of either cellular service or Personal Communications Service (PCS) services, which are placed together in the data.[37] We do not have data specifying the number of these carriers that are not independently owned and operated or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of cellular service carriers that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are fewer than 808 small cellular service carriers that may be affected by the proposed Rural Task Force plan.

17. *Broadband Personal Communications Service (PCS)*. The broadband PCS spectrum is divided into six frequency blocks designated A through F, and the Commission has held auctions for each block. The Commission defined "small entity" for Blocks C and F as an entity that has average gross revenues of less than $40 million in the three previous calendar years.[38] For Block F, an additional classification for "very small business" was added and is defined as an entity that, together with their affiliates, has average gross revenues of not more than $15 million for the preceding three calendar years.[39] These regulations defining "small entity" in the context of broadband PCS auctions have been approved by the SBA.[40] No small businesses within the SBA-approved definition bid successfully for licenses in Blocks A and B. There were 90 winning bidders that qualified as small entities in the Block C auctions. A total of 93 small and very small business bidders won approximately 40% of the 1,479 licenses for Blocks D, E,

---

[34] FCC, Common Carrier Bureau, Industry Analysis Division, *Trends in Telephone Service*, Table 19.3 (March 2000)

[35] 13 C.F.R. § 121.201, SIC code 4812.

[36] *1992 Census, Series UC92-S-1*, at Table 5, SIC code 4812.

[37] *Trends in Telephone Service*, Table 19.3 (March 2000).

[38] *See Amendment of Parts 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, FCC 96-278, paras. 57- 60 (released June 24, 1996), 61 FR 33859 (Jul. 1, 1996); *see also* 47 C.F.R. § 24.720(b).

[39] *See Amendment of Parts 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, FCC 96-278, para. 60 (1996), 61 FR 33859 (Jul. 1, 1996).

[40] *See, e.g., Implementation of Section 309(j) of the Communications Act -- Competitive Bidding*, PP Docket No. 93-253, Fifth Report and Order, 9 FCC Rcd 5532, 5581-84 (1994).

and F.[41] Based on this information, we conclude that the number of small broadband PCS licensees will include the 90 winning C Block bidders and the 93 qualifying bidders in the D, E, and F blocks, for a total of 183 small entity PCS providers as defined by the SBA and the Commission's auction rules.

18. *Rural Radiotelephone Service.* The Commission has not adopted a definition of small entity specific to the Rural Radiotelephone Service.[42] A significant subset of the Rural Radiotelephone Service is the Basic Exchange Telephone Radio Systems (BETRS).[43] We will use the SBA's definition applicable to radiotelephone companies, *i.e.*, an entity employing no more than 1,500 persons.[44] There are approximately 1,000 licensees in the Rural Radiotelephone Service, and we estimate that almost all of them qualify as small entities under the SBA's definition.

19. *Specialized Mobile Radio (SMR)*. The Commission awards bidding credits in auctions for geographic area 800 MHz and 900 MHz SMR licenses to firms that had revenues of no more than $15 million in each of the three previous calendar years.[45] In the context of 900 MHz SMR, this regulation defining "small entity" has been approved by the SBA; approval concerning 800 MHz SMR is being sought.

20. These fees apply to SMR providers in the 800 MHz and 900 MHz bands that either hold geographic area licenses or have obtained extended implementation authorizations. We do not know how many firms provide 800 MHz or 900 MHz geographic area SMR service pursuant to extended implementation authorizations, nor how many of these providers have annual revenues of no more than $15 million. One firm has over $15 million in revenues. We assume, for purposes of this IRFA, that all of the remaining existing extended implementation authorizations are held by small entities, as that term is defined by the SBA.

21. For geographic area licenses in the 900 MHz SMR band, there are 60 who qualified as small entities. For the 800 MHz SMR's, 38 are small or very small entities.

22. *Fixed Microwave Services.* Microwave services include common carrier,[46] private-operational fixed,[47] and broadcast auxiliary radio services.[48] At present, there are approximately 22,015 common carrier fixed licensees and 61,670 private operational-fixed licensees and broadcast auxiliary radio licensees in the microwave services. The Commission has not yet defined a small business with respect to microwave services. For purposes of this IRFA, we will utilize the SBA's definition applicable to

[41] FCC News, *Broadband PCS, D, E and F Block Auction Closes*, No. 71744 (released Jan. 14, 1997).

[42] The service is defined in section 22.99 of the Commission's Rules. 47 C.F.R. § 22.99.

[43] BETRS is defined in sections 22.757 and 22.759 of the Commission's Rules. 47 C.F.R. §§ 22.757, 22.759.

[44] 13 C.F.R. § 121.201, SIC code 4812.

[45] 47 C.F.R. § 90.814(b)(1).

[46] 47 C.F.R. §§ 101, *et seq*. (formerly Part 21 of the Commission's Rules).

[47] Persons eligible under Parts 80 and 90 of the Commission's rules can use Private Operational-Fixed Microwave services. *See* 47 C.F.R. Parts 80 and 90. Stations in this service are called operational-fixed to distinguish them from common carrier and public fixed stations. Only the licensee may use the operational-fixed station, and only for communications related to the licensee's commercial, industrial, or safety operations.

[48] Auxiliary Microwave Service is governed by part 74 of Title 47 of the Commission's Rules. *See* 47 C.F.R. Part 74. Available to licensees of broadcast stations and to broadcast and cable network entities, broadcast auxiliary microwave stations are used for relaying broadcast television signals from the studio to the transmitter, or between two points such as a main studio and an auxiliary studio. The service also includes mobile TV pickups, which relay signals from a remote location back to the studio.

radiotelephone companies -- *i.e.*, an entity with no more than 1,500 persons.[49] We estimate, for this purpose, that all of the Fixed Microwave licensees (excluding broadcast auxiliary licensees) would qualify as small entities under the SBA definition for radiotelephone companies.

23. *39 GHz Licensees*. Neither the Commission nor the SBA has developed a definition of small entities applicable to 39 GHz licensees. Therefore, the applicable definition of small entity is the definition under the SBA rules applicable to radiotelephone (wireless) companies. This provides that a small entity is a radiotelephone company employing no more than 1,500 persons.[50] For purposes of the 39 GHz license auction, the Commission defined "small entity" as an entity that has average gross revenues of less than $40 million in the three previous calendar years, and "very small entity" as an entity that has average gross revenues of not more that $15 million for the preceding three calendar years.. The Commission has granted licenses to 29 service providers in the 39 GHz service. We do not have data specifying the number of these carriers that are not independently owned and operated or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of 39 GHz licensees that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are no more than 29 39 GHz small business providers that may be affected by the proposed Rural Task Force plan.

4. Description of Projected Reporting, Recordkeeping, and Other Compliance Requirements

24. The Rural Task Force proposes that rural carriers be given a choice of three different options for disaggregating and targeting per-line universal service support, including high-cost loop support, Long Term Support (LTS), and Local Switching Support (LSS), to wire center cost zones.[51] Path 1 would be available to rural carriers that do not want to target high-cost support. Path 2 would be available to rural carriers that want state commission review and approval of a disaggregation plan. Path 3 would be available to rural carriers interested in self-certifying a method for disaggregating universal service support into a maximum of two cost zones per wire center.[52] A disaggregation plan filed under Path 3 must use a rationale that is reasonably related to the cost of providing service for each cost zone within each disaggregation category (high-cost loop support, LSS, and LTS). Rural carriers would be required to choose one of the paths within 270 days of the effective date of the proposed new rules. If these proposals are adopted, rural carriers that elect to disaggregate and target per-line support would be required to report loops at the cost-zone level, which would be a modification of the current requirement that carriers report loops at the study-area level. This change should require only minor increases to a carrier's reporting burdens, and predominantly only in the first year that the carrier revises its method of reporting. We estimate that the annual burden hours in the first year would be 60 hours. We estimate subsequent annual burden hours at 8 hours. We believe the burden associated with this proposed reporting requirement is appropriately balanced with the benefits reporting rural carriers would receive.

25. The Rural Task Force also proposes extension of the section 254(e) certification process to rural carriers.[53] Under this process, state regulatory commissions would provide the Commission with annual certifications indicating that the carriers in their states receiving federal universal service support

[49] 13 C.F.R. § 121.201, SIC code 4812.

[50] 13 C.F.R. § 121.201, SIC code 4812.

[51] Under the Rural Task Force's proposal, rural carriers also may disaggregate and target per-line support to cost zones within wire centers.

[52] Alternatively, the self-certified plan may comply with a prior regulatory determination that a different level of disaggregation is appropriate.

[53] 47 U.S.C. § 254(e).

will use the support "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."[54] This reporting requirement would provide states and carriers with access to federal universal service support in a way that ensures the integrity of the universal service fund. We estimate that the annual burden hours associated with the section 254(e) certification process would be 12 hours per carrier. This is a nominal burden on rural carriers and is balanced against the high degree of federal universal service benefits rural carriers would receive.

5. Steps Taken To Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered

26. The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance, rather than design, standards; and (4) an exemption from coverage of the rule, or any part thereof, for small entities.[55]

27. The Rural Task Force Recommendation under consideration herein is the product of analysis of a number of options for distributing federal universal service support to rural carriers, including the continuation or modification of the current system of support, a system of support based on forward-looking cost models, competitive bidding approaches, rate buy-down mechanisms, and a melded approach combining aspects of both the current, embedded-cost system and a forward-looking support system.[56] The results of the Rural Task Force's evaluation of these various options are set forth in the third and fourth White Papers prepared by the Rural Task Force.[57] The Rural Task Force ultimately recommended the modified version of the current high-cost loop support mechanism based on carriers' embedded costs set forth in its Recommendation.

28. Alternatives to the proposed adoption of the Rural Task Force Recommendation include continuation of the current high-cost loop support mechanism for rural carriers, developing a new support mechanism based on forward-looking economic costs, or adopting specific aspects of the Rural Task Force Recommendation instead of adopting the Recommendation as a whole. We invite comment on how any of these alternatives, or any other alternatives discussed herein, would be likely to affect small businesses.

6. Federal Rules That May Duplicate, Overlap, or Conflict With the Proposed Rules

29. None.

C. Paperwork Reduction Act

30. As part of our continuing effort to reduce paperwork burdens, we invite the general public to take this opportunity to comment on information collections contained in this Further Notice, as required by the Paperwork Reduction Act of 1995, Pub. L. No. 104-13. Public and agency comments are due at the same time as other comments on this Further Notice. Comments should address: (a) whether the proposed

---

[54] *Id.*

[55] 5 U.S.C. § 603(c).

[56] *See Recommended Decision*, FCC 00J-4 at Appendix A, §§ III(A), III(B).

[57] *See id.* at 17. The Rural Task Force White Papers are available on the Rural Task Force web site at www.wutc.wa.gov/rtf/rtfpub.nsf?open.

collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (b) the accuracy of the Commission's burden estimates; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

V. COMMENT FILING PROCEDURES

31. Pursuant to sections 1.415 and 1.419 of the Commission's rules, 47 C.F.R. §§ 1.415, 1.419, interested parties may file comments 30 days or fewer from publication in the Federal Register, and reply comments 45 days or fewer from publication in the Federal Register. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies.[58]

32. Comments filed through the ECFS can be sent as an electronic file via the Internet to <http://www.fcc.gov/e-file/ecfs.html>. Generally, only one copy of an electronic submission must be filed. If multiple docket or rulemaking numbers appear in the caption of this proceeding, however, commenters must transmit one electronic copy of the comments to each docket or rulemaking number referenced in the caption. In completing the transmittal screen, commenters should include their full name, Postal Service mailing address, and the applicable docket or rulemaking number. Parties may also submit an electronic comment by Internet e-mail. To get filing instructions for e-mail comments, commenters should send an e-mail to ecfs@fcc.gov, and should include the following words in the body of the message, "get form <your e-mail address." A sample form and directions will be sent in reply.

33. Parties who choose to file by paper must file an original and four copies of each filing. If more than one docket or rulemaking number appear in the caption of this proceeding, commenters must submit two additional copies for each additional docket or rulemaking number. All filings must be sent to the Commission's Secretary, Magalie Roman Salas, Office of the Secretary, Federal Communications Commission, 445 12th Street, S.W., Washington, D.C. 20554.

34. Parties who choose to file by paper should also submit their comments on diskette. These diskettes should be submitted to: Sheryl Todd, Accounting Policy Division, 445 12th Street, S.W., Washington, D.C. 20554. Such a submission should be on a 3.5-inch diskette formatted in an IBM compatible format using Word or compatible software. The diskette should be accompanied by a cover letter and should be submitted in "read only" mode. The diskette should be clearly labeled with the commenter's name, proceeding (including the docket number, in this case CC Docket No. 96-45, type of pleading (comment or reply comment), date of submission, and the name of the electronic file on the diskette. The label should also include the following phrase "Disk Copy - Not an Original." Each diskette should contain only one party's pleadings, preferably in a single electronic file. In addition, commenters must send diskette copies to the Commission's copy contractor, International Transcription Service, Inc., 1231 20th Street, N.W., Washington, D.C. 20037.

35. Written comments by the public on the proposed and/or modified information collections are due on or before thirty days after the date of publication in the Federal Register. Written comments must be submitted by the Office of Management and Budget (OMB) on the proposed and/or modified information collections on or before 60 days after date of publication in the Federal Register. In addition to filing comments with the Secretary, a copy of any comments on the information collections contained herein should be submitted to Judy Boley, Federal Communications Commission, Room 1-C804, 445 12th Street, S.W., Washington, DC 20554, or via the Internet to jboley@fcc.gov and to Edward Springer, OMB Desk Officer, 10236 NEOB, 725 - 17th Street, N.W., Washington, D.C. 20503.

---

[58] *See* Electronic Filing of Documents in Rulemaking Proceedings, 63 Fed. Reg. 24,121 (1998).

VI. ORDERING CLAUSES

36. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 4(i), 4(j), 201-205, 254, and 403 of the Communications Act of 1934, as amended,[59] this Further Notice of Proposed Rulemaking IS ADOPTED.

37. IT IS FURTHER ORDERED that the Commission's Consumer Information Bureau, Reference Information Center, SHALL SEND a copy of this Further Notice of Proposed Rulemaking, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

[59] 47 U.S.C. §§ 154(i), 154(j), 201-205, 254, and 403.

ATTACHMENT 1:

Federal-State Joint Board on Universal Service
Recommended Decision Concerning
Rural Task Force Recommendation

Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	
	)	

RECOMMENDED DECISION

Adopted: December 22, 2000 **Released:** December 22, 2000

1. By the Federal-State Joint Board: Joint Board Chairman Ness and Commissioners Furtchgott-Roth and Tristani issuing separate statements; Joint Board State Chairman Schoenfelder and Commissioner Rowe concurring and issuing separate statements; Public Counsel Hogerty concurring in part and dissenting in part and issuing a separate statement; Chairman Wood issuing a statement at a later date.

I. INTRODUCTION

2. In this Recommended Decision, we send to the Commission the Rural Task Force Recommendation that can serve as a good foundation for implementing a rural universal service plan that benefits consumers. Generally, we find that the Rural Task Force sought to achieve the goals of the Telecommunications Act of 1996 to preserve and advance universal service, facilitate competition in rural areas, and provide a predictable level of universal service support.[1] Moreover, we believe that implementation of the Rural Task Force's framework would provide a stable environment for rural carriers to invest in rural America.

II. BACKGROUND

A. Statutory Requirements

3. In the 1996 Act, Congress established a number of principles for the preservation and advancement of universal service in a competitive telecommunications environment. In particular, section 254 of the 1996 Act provides that consumers in all regions of the Nation, including consumers in rural, insular, and high-cost areas, should have access to telecommunications services at rates that are affordable and reasonably comparable.[2] Section 254 also provides that access to advanced telecommunications and information services should be provided in all regions of the Nation, and that federal universal service support mechanisms should be specific, predictable, and sufficient to preserve and advance universal service.[3] The Commission adopted the additional principle that federal support mechanisms should be competitively neutral, neither unfairly advantaging nor disadvantaging particular service providers or

[1] Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (1996 Act). The 1996 Act amended the Communications Act of 1934. 47 U.S.C. §§ 151, *et seq.*

[2] 47 U.S.C. § 254(b)(3).

[3] *Id.* at §§ 254(b)(2), (5).

technologies.[4] Federal universal service policies should strike a fair and reasonable balance among these principles or goals enumerated in section 254 of the 1996 Act.[5] The 1996 Act also requires the Commission to consult with the Federal-State Joint Board on Universal Service (Joint Board) in implementing section 254.[6]

B. Prior Joint Board and Commission Actions

4. Pursuant to the 1996 Act, the Joint Board provided its first set of recommendations regarding universal service to the Commission in November 1996.[7] Based on these recommendations, the Commission adopted the *First Report and Order* in May 1997.[8] Among other things, the Commission concluded that federal universal service support for all carriers, both rural and non-rural,[9] should be based on the forward-looking economic cost of constructing and operating the network used to provide the supported services, rather than each carrier's embedded costs.[10] The Commission explained that using forward-looking economic costs provides sufficient support without giving carriers an incentive to inflate their costs or to refrain from efficient cost cutting.

5. Nevertheless, the Commission adopted the Joint Board's recommendation that rural carriers not use a cost model or other means of determining forward-looking economic cost immediately to calculate their support for serving rural high-cost areas.[11] The Commission agreed with the Joint Board that, compared to the large non-rural carriers, "rural carriers generally serve fewer subscribers, serve more sparsely populated areas, and do not generally benefit as much from economies of scale and scope. For many rural carriers, universal service support provides a large share of the carriers' revenues, and thus,

---

[4] *See id.* at § 254(b)(7); *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 8801-03 paras. 46-51 (1997) (*First Report and Order*) (subsequent history omitted).

[5] *First Report and Order*, 12 FCC Rcd at 8803 para. 52.

[6] *See* 47 U.S.C. § 254(a).

[7] *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision, 12 FCC Rcd 87 (Jt. Bd. 1996) (*First Recommended Decision*).

[8] *First Report and Order*, 12 FCC Rcd 8776.

[9] "Rural carriers" are local exchange carriers (LECs) that meet the definition of a rural telephone company contained in section 153(37) of the 1996 Act, and "non-rural carriers" are LECs that do not meet this definition. 47 U.S.C. § 153(37).

[10] *First Report and Order*, 12 FCC Rcd at 8899-901 paras. 224-229. At the time of the *First Report and Order*, three federal universal service support mechanisms provided support for rural and non-rural carriers, for the most part based on embedded costs averaged over entire study areas. The high-cost loop support and Local Switching Support (formerly DEM Weighting) programs under Part 36 of the Commission's rules provided support for intrastate-allocated costs. *See infra* notes 21-22. The Long Term Support program provided support for interstate-allocated costs. *See infra* note 22. These three support mechanisms currently provide approximately $1.568 billion in annual high-cost support to over 1,300 rural carriers. *See* Letter from D. Scott Barash, Vice President and General Counsel, Universal Service Administrative Company (USAC), to Magalie Roman Salas, FCC, dated November 2, 2000, at Appendix HC 3 (USAC 1st Quarter 2001 Projections). The Commission's new, forward-looking high-cost support mechanism for non-rural carriers became effective on January 1, 2000. *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, 14 FCC Rcd 20432, 20439 (1999) (*Ninth Report and Order*), *pets. for review pending sub nom.*, *Qwest Corp. v. FCC*, 10th Cir. No. 99-9546 and consolidated cases (1999).

[11] *First Report and Order*, 12 FCC Rcd at 8934 para. 291.

any sudden change in the support mechanisms may disproportionately affect rural carriers' operations."[12] Accordingly, working with rural carriers and their associations, the Commission stated that it would not implement forward-looking support for rural carriers before January 1, 2001, and only after selecting an appropriate high-cost support mechanism based on recommendations from the Joint Board and a Rural Task Force appointed by the Joint Board.[13] In recommending a proxy model as a framework for determining non-rural carrier high-cost support, the Joint Board emphasized that it did "not intend for the Commission to create any precedent for any potential revisions to support mechanisms for rural carriers."[14] In this regard, the Commission agreed with the state Joint Board members that a task force "should provide valuable assistance in identifying the issues unique to rural carriers and analyzing the appropriateness of proxy cost models for rural carriers."[15]

C. Rural Task Force Recommendation

6. The Joint Board announced the creation of the Rural Task Force in September 1997, and appointed the Rural Task Force members in July 1998.[16] The Joint Board requested that the Rural Task Force provide its recommendations no later than nine months after the implementation of the forward-looking high-cost mechanism for non-rural carriers, which became effective on January 1, 2000.[17] Accordingly, the Rural Task Force presented its Recommendation to the Joint Board on September 29, 2000.[18] The Recommendation represents the consensus of individual Rural Task Force members, who work for a broad range of interested parties, including rural telephone companies, competitive local exchange carriers, interexchange carriers, wireless providers, consumer advocates, and state and federal government agencies. The Rural Task Force offers its Recommendation as an integrated package, and asks that it be adopted without modification. It urges that the Recommendation be implemented immediately and remain in place over a five-year period. The Recommendation is attached as Appendix A to this Recommended Decision.[19] Below, we summarize salient features of the Recommendation.

7. The Rural Task Force recommends against using the Commission's forward-looking high-cost mechanism for non-rural carriers to distribute high-cost support for rural carriers.[20] Instead, it recommends the use over the next five years of a modified version of the current high-cost loop support

[12] *Id.* at 8936 para. 294.

[13] *Id.* at 8917 para. 252-53, 8936 para. 294.

[14] *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Second Recommended Decision, 13 FCC Rcd 24744 at 24758 para. 30 (Jt. Bd. 1998) (Second Recommended Decision).

[15] *Id.* at 8917 para. 253; *see also id.* at para. 255; *Second Recommended Decision*, 13 FCC Rcd 24744 at para. 30 (Jt. Bd. 1998).

[16] *See Federal-State Joint Board on Universal Service Announces Rural Task Force Members*, CC Docket No. 96-45, Public Notice, FCC 98J-1 (Jt. Bd. rel. July 1, 1998); *Federal-State Joint Board on Universal Service Announces the Creation of a Rural Task Force*, CC Docket No. 96-45, Public Notice, 12 FCC Rcd 15752 (Jt. Bd. 1997).

[17] *See id.*

[18] Letter from William R. Gillis, Chair, Rural Task Force, to Magalie Roman Salas, FCC, dated September 29, 2000 (Rural Task Force Recommendation or Recommendation).

[19] Appendix A; *see also* Rural Task Force web site at www.wutc.wa.gov/rtf/rtfpub.nsf?open.

[20] The Rural Task Force emphasizes that its Recommendation applies only to rural, insular, and high-cost areas served by rural carriers, and not to areas served by non-rural carriers. *See* Appendix A at 18.

mechanism under Part 36 of the Commission's rules, based on carriers' embedded costs.[21] In addition, the Rural Task Force recommends continuation of the Long Term Support (LTS) and Local Switching Support (LSS) programs.[22]

8. The Rural Task Force's proposed modifications to the high-cost loop support mechanism include various upward adjustments to current limits on universal service support for rural carriers, including (a) recomputing the indexed cap on high-cost loop support[23] and the corporate operations expense limitation[24] as if the caps had not been in effect for the calendar year 2000,[25] (b) providing above-the-cap "safety net additive" support for carriers with over 14 percent growth in telecommunications plant in service on a per-line basis, and (c) creating a "safety valve" to provide additional support for "meaningful investment" in acquired telephone exchanges.[26] The

[21] High-cost loop support under Part 36 provides support for a variable percentage of carriers' unseparated loop costs, as reflected in their books, depending on the number of working loops they serve and the degree to which their costs exceed the national average cost per loop. *See* 47 C.F.R. §§ 36.601, *et. seq.*; *First Report and Order*, 12 FCC Rcd at 8891-92 paras. 209-11. Specifically, carriers with 200,000 or fewer working loops receive support equal to 65 percent of that portion of their unseparated loop costs exceeding 115 percent of the national average but not greater than 150 percent of the national average, and 75 percent of that portion of their unseparated loop costs exceeding 150 percent of the national average. For carriers with greater than 200,000 working loops, the formula is similar, but with reduced levels of support. For example, a carrier with 200,001 loops reaches the 75 percent support level only for costs that are greater than 250 percent of the national average. The national average is calculated based on the loop costs of both rural and non-rural carriers. The term "unseparated" refers to costs as calculated before applying the jurisdictional separations process, which divides between the state and federal jurisdictions the costs of those portions of local exchange carriers' telephone plant that are used for intrastate and interstate services. *See* 47 C.F.R. § 36.631.

[22] LTS provides support for the interstate-allocated loop costs of rate-of-return carriers (typically small rural carriers) that participate in the National Exchange Carrier Association (NECA) common line pool, and LSS (formerly DEM Weighting) is available to support the intrastate switching costs of carriers with 50,000 or fewer loops. 47 C.F.R. §§ 36.125(b), 54.301, 54.303. The Commission removed LTS and LSS, as well as high-cost loop support under Part 36, from the interstate access charge system in 1997, and they are now collected from all providers of interstate telecommunications services on an equitable and non-discriminatory basis. *See generally Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Fourth Order on Reconsideration, *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge*, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, Report and Order, 13 FCC Rcd 5318, 5343-45 paras. 40-41, 5352-54 paras. 56-58 (1998) (*Fourth Order on Reconsideration*).

[23] An indexed cap that limits the increase in support each year to the annual nationwide growth in loops restricts total high-cost loop support under Part 36 of the Commission's rules. *See* 47 C.F.R. Part 36, Subpart F; *First Report and Order*, 12 FCC Rcd at 8940 para. 302 ("indexed cap effectively limits the overall growth of the fund, while protecting individual carriers from experiencing extreme reductions in support").

[24] The Commission's rules limit the amount of corporate operations expenses that carriers may recover through high-cost loop support under Part 36. *See* 47 C.F.R. § 36.621; *First Report and Order*, 12 FCC Rcd at 8930-32 paras. 283-85.

[25] The Rural Task Force estimates that this particular proposal would increase the size of the high-cost loop support fund by approximately $118.5 million in the first year, representing $83.9 million in additional high-cost loop support and $34.6 million in additional support for corporate operations expenses. For Rural Task Force estimates of the potential cost of other aspects of its Recommendation, *see* Letter from William R. Gillis, Rural Task Force, to Magalie Roman Salas, FCC, dated November 10, 2000.

[26] Section 54.305 of the Commission's rules currently limits universal service support for acquired exchanges to the per-line support received by the seller. 47 C.F.R. § 54.305.

Rural Task Force also recommends that per-line universal service support payment levels within a study area become fixed once a competitive eligible telecommunications carrier begins providing service in the study area, and subsequently adjusted for growth in lines and inflation rather than changes in cost. Under the Rural Task Force's proposal, "safety net additive" support, support for acquired exchanges and "safety valve" support, support for competitive eligible telecommunications carriers, and catastrophic event support[27] would be excluded from the cap on high-cost loop support. Total "safety valve" support would be limited to five percent of the overall cap.

9. The Rural Task Force also recommends the use of a new annual index known as the "rural growth factor" to adjust the cap on high-cost loop support, the corporate operations expense limitation, and fixed per-line support (in areas where competitive carriers are providing service) on a going-forward basis. The rural growth factor would be the sum of annual line growth for rural carriers and a general inflation factor (Gross Domestic Product-Chained Price Index).

10. The Rural Task Force suggests various other reforms. Among other things, it proposes that rural carriers be given a choice of three different options for disaggregating and targeting per-line universal service support, to be exercised within 270 days of the effective date of the proposed new rules. Furthermore, the Rural Task Force recommends adoption of a "no barriers to advanced services" policy, and suggests a number of principles for replacing any implicit subsidies in interstate access charges with explicit universal service support.[28]

III. DISCUSSION

11. The Rural Task Force faced a challenging task. Congress recognized that, while competition could encourage investment in rural infrastructure and bring new, improved services to rural America, special measures were required to preserve and advance universal service. In several areas, Congress provided separate rules for markets served by small, rural telephone companies.[29] Accordingly, in implementing the 1996 Act, the Joint Board and the Commission have consistently recognized that rural carriers face diverse circumstances and that, in considering universal service support mechanisms, "one

---

[27] Under the Rural Task Force Recommendation, fixed per-line support in areas where competitive carriers are providing service would be subject to adjustment by the incumbent carrier to recover costs associated with catastrophic events.

[28] We note that the Multi-Association Group (MAG) recently submitted to the Commission a comprehensive proposal for interstate access charge and universal service reform for rate-of-return carriers. *Petition for Rulemaking of the LEC Multi-Association Group*, RM 10011 (filed October 20, 2000) (*MAG Plan*); *see Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, CC Docket No. 98-77, Notice of Proposed Rulemaking, 13 FCC Rcd 14238 (1998). The MAG is comprised of the National Rural Telecom Association (NRTA), National Telephone Cooperative Association (NTCA), Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO), and United States Telecom Association (USTA).

[29] For example, the 1996 Act provides that state commissions may designate more than one eligible telecommunications carrier in an area served by a rural telephone company, but only after determining that such additional designation is in the public interest. *See* 47 U.S.C. § 214(e)(2). In addition, states may require a telecommunications carrier that seeks to provide service in a rural telephone company's service area to meet the eligible telecommunications carrier requirements of section 214(e)(1). *See* 47 U.S.C. §§ 214(e)(1), 253(f).

size does not fit all." The Rural Task Force thus was charged with the task of considering the needs of rural carriers.[30] The Rural Task Force recommends a flexible plan designed to balance competing goals, a plan that was endorsed by all the members of the Task Force. We find it significant that the Recommendation represents a consensus of competing views. We encourage the Commission to take advantage of this opportunity to craft a rural universal service plan that enjoys widespread support among diverse interests.

12. The Recommendation preserves a predictable level of universal service support that will provide stability to rural carriers – incumbents and competitors – for planning their investments over the next several years. By recommending a flexible system for disaggregating support to establish the portable per-line support amount available to all eligible telecommunications carriers, the Rural Task Force seeks to encourage competitors to enter high-cost areas. In addition, the Rural Task Force recommends certain modifications to the caps and limitations on high-cost loop support. These modifications are generally designed to provide carriers serving rural areas with increased incentives to invest in new infrastructure and technologies. Under the current mechanism, high-cost loop support for rural carriers is estimated to be $835 million in 2001. The Rural Task Force estimates that, under its Recommendation, high-cost loop support for rural carriers will be $961 million in 2001 and increase to $1.29 billion in 2005.[31] The Rural Task Force thus proposes to increase the rural high-cost loop fund by $1.26 billion in the aggregate over the proposed five-year period, compared to the projected growth under the current mechanism.[32]

13. In determining federal support for non-rural carriers, the Joint Board previously has recognized its obligation to provide sufficient support to ensure affordable and comparable rates. The Rural Task Force has noted that the 1996 Act sets standards to provide sufficient support while preventing "waste, windfall, and excessive expense for contributing carriers and their customers."[33] While a significant number of commenters urge the Joint Board to recommend the Rural Task Force plan without modification,[34] other

---

[30] *See Federal-State Joint Board on Universal Service Announces Rural Task Force Members*, CC Docket No. 96-45, Public Notice, FCC 98J-1 (Jt. Bd. rel. July 1, 1998); *Federal-State Joint Board on Universal Service Announces the Creation of a Rural Task Force*, CC Docket No. 96-45, Public Notice, 12 FCC Rcd 15752 (Jt. Bd. 1997).

[31] *See* Letter from William R. Gillis, Rural Task Force, to Magalie Roman Salas, FCC, dated November 10, 2000. The Rural Task Force support estimates include only high-cost loop support. In addition, based on USAC's first quarter 2001 projections, rural carriers will receive $386 million in LSS, $390 million in LTS, and $52 million in interstate access support. *See* USAC 1st Quarter 2001 Projections. These amounts also do not include implicit universal service support that may be included in rural carrier interstate access charges. The Rural Task Force recommends that LSS and LTS remain in place for the duration of its proposed plan and does not comment on the existing interstate access support program for price cap companies.

[32] Joint Board staff estimate the $1.26 billion increase as the difference between the Rural Task Force estimates and projected high-cost loop support based on the current rules. Staff derived current rule estimates by increasing the 2001 rural high-cost loop support estimate of $835 million, reported in USAC's first quarter 2001 projections, by 2.86 percent annual industry line growth factor, as reported in the NECA October 2000 filing. *See* NECA Universal Service Fund 2000 Submission of 1999 Study Results, filed October 1, 2000.

[33] *See* Appendix A at 8.

[34] *See, e.g.,* CenturyTel Comments at 1-2 (urging the Joint Board to act quickly because "[r]eform is critically needed"); Evans Comments at 2 ("The Task Force Recommendation to the Joint Board is the first comprehensive proposal for implementation of the policies and principles of the 1996 Act on the subject of universal service support for high-cost [rural carriers] that includes input of <u>and support by</u> a broad base of interested stakeholders."); GVNW Comments at 3 ("With the record now developed by a group representing the spectrum of those impacted by rural universal service public policy, it is now time to implement these recommendations for (continued….)

commenters, including some rural carriers, believe that the Rural Task Force Recommendation would provide too little support.[35] Still other commenters, including several state commissions and carriers, believe it would provide too much support.[36] We believe that the nature of these comments is consistent with a recommendation that is a consensus proposal put forth by representatives of disparate interests.

14. The Rural Task Force has proceeded with caution by proposing modifications to the current embedded cost system for a five-year period, rather than attempting to modify the Commission's forward-looking cost mechanism that currently is used to determine non-rural support. We agree with the Rural Task Force that understanding the diversity among rural carriers and the differences between small rural carriers and large carriers is desirable in designing appropriate universal service support mechanisms. The Rural Task Force provided valuable data on these differences in their second White Paper, "The Rural Difference."[37] Specifically, the Rural Task Force demonstrated the inappropriateness of using input values designed for non-rural carriers to determine support for rural carriers.[38] We urge the Commission to use the period during which a Rural Task Force Recommendation is in place to develop a long-term universal service plan that better targets support to rural companies serving the highest cost areas. The Joint Board should remain involved in the process to develop improvements to the rural system. We also urge the Commission to evaluate the rural and non-rural support systems to ensure they work together efficiently, while at the same time recognizing the significant distinctions among rural carriers and between rural and non-rural carriers.[39] In sum, we conclude that the Rural Task Force Recommendation presents a good foundation for implementing a rural universal service plan.

15. We observe that the Recommendation proposes modifications to the Commission's rules that involve specific implementation details that the Commission may need to address. Below, we highlight some of these implementation issues.

(Continued from previous page)

a five year-period."). NECA Comments at 8-9 ("The RTF *Recommendation* should be adopted immediately by the Joint Board and the Commission, with due consideration of the potential longer-term effects of imposing artificial limits, such as continuation of any form of capping, on the size of the Rural carrier high cost fund.").

[35] *See, e.g.*, Citizens Comments at 2-5 ("proposal to 'right size' the fund by ameliorating the impact of the past cap suggests the imposition of a new cap might necessitate . . . a new right sizing in order to achieve the intended result of spurring investment in rural America"); MTA Comments at 3 (arguing that loss of $130 million due to caps "is money that could have been directly invested in our telecommunications infrastructure"); NTCA Comments at 7-10 (strongly believes that no caps on the universal service support funds should be retained and that caps are unlawful); USTA Comments at 6-8 (opposing any cap on the rural high-cost fund to ensure sufficiency as mandated by section 254(b)(5) of the Act).

[36] *See, e.g.*, Charter Comments at 6-10 ("reform of rural universal service should be about reform, not about tweaking a subsidy structure that is outmoded and antithetical to competition"); New York Comments at 3-4 (no showing that total amount of support recommended would be only that amount necessary to enable sates to establish reasonably comparable rates); WorldCom Comments at 5-8 ("no evidence that rural LECs have been unable to maintain their quality of service or upgrade facilities at the support levels provided by the existing mechanisms"); Ad Hoc Reply Comments at 13-14 ("any increase or elimination of the indexed cap on the [high-cost loop] fund would only encourage a rural carrier to make inefficient investment decisions").

[37] *See* Rural Task Force, *White Paper 2: The Rural Difference* (January 2000) (*White Paper 2*), which is available on the Rural Task Force's web site at www.wutc.wa.gov/rtf/rtfpub.nsf?open.

[38] *See, id.; see, e.g.*, GCI Comments at 2-3; People Comments at 2-3; WorldCom Comments at 2; Ad Hoc Reply Comments at 5-6; AT&T Reply Comments at 3-4.

[39] *See White Paper 2* at www.wutc.wa.gov/rtf/rtfpub.nsf?open.

A. Mergers and Acquisitions Cap & the "Safety Valve" Mechanism

16. Section 54.305 of the Commission's rules provides that a carrier acquiring exchanges from an unaffiliated carrier shall receive the same per-line levels of high-cost universal service support for which the acquired exchanges were eligible prior to their transfer.[40] The Rural Task Force recommends that the Commission retain section 54.305 of its rules, but establish an appropriate "safety valve" mechanism to enable rural carriers acquiring access lines eligible for high-cost loop support to recover additional support reflecting "meaningful investment" in acquired access lines.[41] The Rural Task Force provides an illustration of such a mechanism in Appendix D of its Recommendation.[42] In Appendix D, the Rural Task Force defines "meaningful investment" for purposes of qualifying a rural carrier for "safety valve" support as the difference between the "index year expense adjustment" calculated in accordance with section 36.631 of the Commission's rules[43] and subsequent year expense adjustments.[44] The Rural Task Force's example also proposes to limit the total "safety valve" support available to all eligible study areas to no more than five percent of the indexed high-cost loop fund cap for rural carriers.[45]

17. We support the Rural Task Force's proposal for providing additional support to rural carriers that acquire high-cost exchanges and make post-transaction investments to enhance the network infrastructure. We note, however, that the Task Force's proposal does not address a number of important implementation issues. In order to ensure effective implementation of the "safety-valve" mechanism, we encourage the Commission to address several implementation issues. First, the Commission should consider the distribution of "safety valve" support if the total amount of eligible "safety valve" support exceeds the cap of five percent of the indexed high-cost loop support fund.[46] The Commission should also examine the definition of "meaningful investment."[47] In addition, the Commission should address whether a carrier's "safety valve" support should transfer to a different carrier as a result of a subsequent transfer of exchanges. Finally, the Commission should consider whether "safety valve" support is "frozen" when a competitive eligible telecommunications carrier enters the study area, just as other high-cost loop support would be frozen when a competitive eligible telecommunications carrier enters the incumbent's service area, and whether such an approach would unduly dissuade investment.

---

[40] 47 C.F.R. § 54.305. High-cost support mechanisms currently include non-rural carrier forward-looking high-cost support, interim hold-harmless support for non-rural carriers, rural carrier high-cost loop support, local switching support, and Long Term Support (LTS). *See* 47 C.F.R. §§ 36.601-36.631, 54.301, 54.303, 54.309, 54.311.

[41] *See* Appendix A at 29.

[42] *See id.* at Appendix D.

[43] *See* 47 C.F.R. § 36.631.

[44] *See* Appendix A at Appendix D-1.

[45] *See id.*

[46] *See, e.g.*, USTA Comments at 9-10 (arguing that increased support resulting from a single transfer could exceed the five percent cap).

[47] For example, it may be more appropriate to define "meaningful investment" so that the "index year expense adjustment" is the year prior to the subsequent year "expense adjustment." As currently proposed, the "index year expense adjustment" is the study area's high-cost loop support "expense adjustment" calculated at the end of the acquiring company's first year of operations.

B. Support in Competitive Study Areas

18. As discussed above, the Rural Task Force recommends that the Commission "freeze" per-line high-cost loop support directed to a rural study area if a competitive eligible telecommunications carrier has been designated and begins providing service in that study area.[48] Under the Rural Task Force's proposal, both the incumbent LEC and the competitive eligible telecommunications carrier would receive fixed per-line support. The Rural Task Force also recommends that the Commission increase such fixed per-line support by the Rural Task Force's proposed Rural Growth Factor.[49] Although we agree with the Rural Task Force that the Commission should "freeze" per-line high-cost loop support when a competitor begins providing services in a given study area, it is unclear how the high-cost loop fund cap would account for fixed rural carrier support. The Commission should seek additional input from commenters, including the Rural Task Force, on the operation of the high-cost loop fund cap on fixed rural carrier support.

19. The Rural Task Force also recommends that the Commission permit incumbent LECs receiving "frozen" per-line high-cost to adjust frozen per-line support to recover costs associated with catastrophic events affecting the carrier's ability to provide supported services.[50] The Commission should seek further input on the impact of "catastrophic" support provided by other sources such as insurance, Rural Utilities Service loans, and federal or state emergency management relief.[51]

C. The "Safety Net Additive"

20. In years in which the Rural Task Force's new indexed cap on the high-cost loop support fund is triggered and growth in telecommunications plant in service (TPIS) per line in a rural study area is at least 14 percent greater than the study area's TPIS per line in the prior year, the Rural Task Force proposes a "safety net additive," which would enable a carrier to recover 50 percent of the difference between capped and uncapped support.[52] Any study area that qualifies for the safety net additive support also would qualify for safety net additive support in each of the four succeeding years, regardless of whether the study area meets the 14 percent criterion in those years.[53] Safety net additive support would be in addition to capped high-cost loop support, and would not be subject to the Rural Task Force's new indexed cap on such support.[54] We agree with the Rural Task Force that additional support in the form of a safety net additive should be available to rural carriers that make significant investment in rural infrastructure, but urge the Commission to seek further comment on whether the safety net additive mechanism enables a carrier to recover more than 100 percent reimbursement on incremental loop investment.[55]

---

[48] *See* Appendix A at 26.

[49] *Id.*

[50] *Id.*

[51] *See* Sprint Comments at 3 ("fund should not become substitute for carriers' insurance policies").

[52] *See* Appendix A at 27.

[53] *Id.*

[54] *Id.*

[55] *See, e.g.,* Bristol Comments at 3; TDS Telecom Comments at 8.

D. Interstate Access Universal Service Support for Non-Price Cap Carriers

21. The Rural Task Force recommends that the Commission replace implicit universal service support included in rural carrier interstate access charges with an uncapped "High Cost Fund III."[56] The Rural Task Force also articulates several principles that the Commission should follow in implementing that task.[57] We concur with the Rural Task Force that the Commission should consider creating an explicit universal service support mechanism to replace support that may be implicit within interstate access charges collected by rural carriers.[58] We acknowledge, however, that the access charge issues raised by the Rural Task Force and the MAG are interstate in nature and, therefore, are properly before the Commission.[59] However, the MAG plan raises issues beyond interstate access reform, and proposes universal service policy and procedural changes, including rate comparability under section 254(b)(3) and the overall size of the universal service mechanisms. Section 254(b) and 254(c) of the 1996 Act both contemplate that the Joint Board remain involved in matters related to universal service.[60] We therefore encourage the Commission to ensure the Joint Board remains actively involved in review of those aspects of the MAG plan that relate to universal service. A significant number of Joint Board members urge that this involvement include a referral to the Joint Board of the universal service issues raised by the MAG plan.

E. Future Steps

22. As discussed above, the Rural Task Force urges that its recommendation be implemented immediately and remain in place over a five-year period.[61] In addition to the Commission's ongoing consultation with the Joint Board during this period, we urge the Commission to refer to the Joint Board, no later than January 1, 2002, a proceeding to consider implementation of an appropriate high-cost mechanism for rural carriers after the expiration of the Rural Task Force's plan. We note that the Commission and the Joint Board are already committed to review the operation of the high-cost support mechanism for non-rural carriers on or before January 1, 2003.[62] This proposed timing would permit the Joint Board and the Commission to consider the appropriate rural mechanism to succeed the plan that the Commission adopts pursuant to the Rural Task Force's recommendation and devote sufficient time to the task prior to the termination of that plan. We also recommend eventual comprehensive review of the high-cost support mechanisms for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently and in a coordinated fashion. We urge the Commission to use the transitional period during which a modified embedded cost mechanism is in place to develop a long-term universal service plan that better targets support to rural companies serving the highest cost areas, while at the same time recognizing the

---

[56] *See* Appendix A at 30-32.

[57] *See id.*

[58] *See* AT&T Comments at 5-6; CenturyTel Comments at 2; NTCA Comments at 18; Roseville Comments at 4; TDS Telecom Comments at 6-7.

[59] *See* NTCA Comments at 19; Roseville Comments at 4; TDS Telecom Comments at 6-7; USTA Comments at 11.

[60] *See* 47 U.S.C. §§ 254(b), (c).

[61] *See supra* discussion at para. 5.

[62] *Federal-State Joint Board on Universal Service, Access Charge Reform*, CC Docket Nos. 96-45, 96-262, Seventh Report & Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45, Fourth Report & Order in CC Docket No. 96-262, and Further Notice of Proposed Rulemaking, 14 FCC Rcd 8077, 8123 para. 94 (1999).

significant distinctions among rural carriers and between rural and non-rural carriers.

IV. RECOMMENDING CLAUSE

23. For the reasons discussed herein, the Federal-State Joint Board on Universal Service, pursuant to section 254(a)(1) and section 410(c) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 254(a)(1), 410(c), recommends that the Commission adopt the Rural Task Force Recommendation as a foundation for implementing a rural universal service plan.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary

APPENDIX A

RURAL TASK FORCE
RECOMMENDATION TO
THE FEDERAL-STATE JOINT BOARD ON UNIVERSAL SERVICE

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	

RURAL TASK FORCE
RECOMMENDATION TO THE FEDERAL-STATE JOINT BOARD ON UNIVERSAL SERVICE

Adopted: September 22, 2000 ....

By the Rural Task Force:

TABLE OF CONTENTS

Page

I. EXECUTIVE SUMMARY 3

II. CONTEXT AND EVIDENTIARY FOUNDATION 5

A. Overview 5

B. Legal and Policy Foundation for the Task Force Recommendation 7

C. Empirical Justification for a Distinct Rural Carrier Universal Service Mechanism 11

D. Policy Context Facilitating Both ILEC and CLEC Investment in Rural Communities 14

III. METHODS AND POLICIES TO ESTABLISH PREDICTABLE AND SUFFICIENT SUPPORT FOR RURAL CARRIERS 15

A. Alternative Methods for Sizing the Fund –Overview of Options Considered 15

B. Evaluation of the Synthesis Model Applied to Rural Carriers 17

C. Tools versus Application 18

D. Recommended Method for Sizing the Fund 20

IV. POLICY CHOICES AFFECTING REQUIRED FUND SIZE 21

A. Recommendations Requiring Sufficient Funding to Achieve Advanced Telecommunications Service Access and Comparability Provisions of Section 254 21

1. Advanced Services 22

2. Information Services 23

B. Recommendations Providing for Fund Growth Necessary to Achieve Section 254 Mandates – Caps and Limitations to the Existing HCL 23
1. Indexed Cap On High Cost Loop Support 24
2. Corporate Operations Expense Limitation 27
3. Merger and Acquisition Cap 29

C. Principles for Preserving any Current Universal Service Support Which May be Implicit Within Interstate Access Charges – The Underlying Basis for High Cost Fund III (HCF III) 29

D. Accountability 31

V. REFORMS TO ACHIEVE COMPETITIVE PROVISIONS OF THE 1996 ACT 33

A. Disaggregation and Targeting of Support 33

B. Portability Implementation 36
1. Per Line Support 36
2. Transparency of Universal Service Support 36
3. Frequency of Reporting and Lag in Support 37
4. Identification of Service Locations 37
5. Supported Lines 38
6. Stranded Costs 38

VI. RECOMMENDING CLAUSES 38

Appendix A - Signatory Rural Task Force Members 38

Appendix B - Meetings and Conference Calls 40

Appendix C - List of Rural Task Force White Papers 40

Appendix D - Example of the “Safety Valve” Mechanism for the Mergers and Acquisition Cap 41

I. EXECUTIVE SUMMARY

This document contains a comprehensive, balanced package that is the final Recommendation (Recommendation) of the Rural Task Force (Task Force). The Task Force was appointed by the Federal-State Joint Board on Universal Service (Joint Board) in CC Docket No. 96-45 pursuant to the Telecommunications Act of 1996 (1996 Act).[1] We urge that the Recommendation be implemented immediately and remain in place for five years. Plans should be made to reevaluate appropriate universal service funding approaches for areas served by “rural telephone companies”[2] prior to the end of the five-year period. The Recommendation represents

[1] Pub. L. No. 104-104, 110 Stat. 56 (1996 Act). The 1996 Act amended the Communications Act of 1934, 47 U.S.C. Section 151 *et seq.* (1996 Act).

[2] “Rural telephone company" means a local exchange carrier operating entity to the extent that such entity-- (A) provides common carrier service to any local exchange carrier study area that does not include either-- (i) any incorporated place of 10,000 inhabitants or more, or any part thereof, based on the most recently available (continued….)

the consensus of individual Task Force members.[3] The Recommendation may or may not represent the positions of organizations or companies to which Task Force members belong.

The Task Force has expended considerable time over the past two years in learning, discussing, debating, negotiating, and compromising to develop this Recommendation. As a delicately-crafted package, it is meant to balance the mandate to preserve and advance universal service while at the same time facilitating competition in areas served by Rural Carriers. The Recommendation also strikes a careful balance between the need to provide a fund that is "sufficient" under the provisions of the 1996 Act while insuring that the overall size of the fund is reasonable. Each of the elements of this comprehensive package are interdependent and should be considered in concert with each other, and should be implemented expeditiously. The Task Force strongly recommends that this balance be honored in reviewing the complete package that comprises its Recommendation.

The following summarizes the major conclusions of the Task Force:

- The Task Force's Recommendation should be implemented immediately and remain in place for a five-year period. Plans should be made to reevaluate appropriate universal service funding approaches for areas served by Rural Carriers prior to the end of this five-year period.

- The Task Force recommends that the Synthesis Model not be used for determining the forward-looking costs of Rural Carriers.

- The Task Force recommends the Modified Embedded Cost Mechanism of federal universal service support for Rural Carriers be adopted for sizing the Rural Carrier federal universal service fund.

(Continued from previous page)
population statistics of the Bureau of the Census; or (ii) any territory, incorporated or unincorporated, included in an urbanized area, as defined by the Bureau of the Census as of August 10, 1993; (B) provides telephone exchange service, including exchange access, to fewer than 50,000 access lines; (C) provides telephone exchange service to any local exchange carrier study area with fewer than 100,000 access lines; or (D) has less than 15 percent of its access lines in communities of more than 50,000 on the date of enactment of the Telecommunications Act of 1996 (47 U.S.C. Section 153 (37)). The term "Rural Carrier" as used in this Recommendation is meant to include carriers serving insular areas and to incorporate the statutory definition of "rural telephone company" as applied in the FCC rules. *See* In re: Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Report and Order* (rel. May 8, 1997) at paragraph 96. *See also* FCC *Public Notice*, CC Docket No. 96-45, DA 98-1205 (rel. June 22, 1998) lists recognized self-certified "Rural Telephone Companies." This list is updated periodically. S*ee* for example, FCC *Public Notice*, CC Docket No. 96-45, DA001705 (rel. Aug. 1, 2000).

[3] Several appointees were not present or involved during the final months of meetings and conference calls of the Task Force. Because they did not take part in the final deliberations and because the Task Force had agreed early on that they must be present to vote, several appointees' names do not appear on the Recommendation signature page.

- The Task Force recommends a flexible system for disaggregating support to establish the portable per line support available to all eligible telecommunications carriers with timely distributions.

- The Task Force recommends that states be delegated responsibility for oversight of the use of universal service support in a manner similar to that used for the non-rural LECs.

- The Task Force recommends that the Joint Board review the definition of the services that are supported by federal universal service support mechanisms, and that a "no barriers to advanced services" policy be adopted.

- The Task Force recommends the Joint Board and Federal Communications Commission (FCC) enact modifications to the caps and limitations on universal service funding which currently exist:
  - The High Cost Loop Fund should be re-based by increasing it $118.5 million, grown by an annual factor, and include a "safety net;"
  - The corporate operations expense limitation should be adjusted for growth; and
  - A "safety valve mechanism" should be added to the limitation on support for acquired or transferred exchanges.

- The Task Force recommends a set of principles to be used in addressing implicit support in interstate access charges, and recommends creation of High Cost Fund III to take the place of any implicit support removed from interstate access.

II. CONTEXT AND EVIDENTIARY FOUNDATION

A. Overview

Shortly after its formal organization in July of 1998, the Task Force developed a mission statement, working objectives and guiding principles for its ultimate recommendation to the Joint Board. Specifically, the Task Force clarified its mission " . . . to review and evaluate alternative universal support mechanisms which affect consumers in rural and insular areas served by rural telephone companies and to make recommendations to the CC 96-45 Joint Board on appropriate universal service support mechanisms, methods and policies to faithfully implement the universal service provisions of the Telecommunications Act of 1996 for these rural and insular areas."[4]

Three specific objectives were established to guide the work of the Task Force:

1. The Task Force should review a broad range of options, including the continuation or adaptation of the current system of support, a system of support based on forward-looking cost models, and any other mechanism consistent with the universal service support and pro-competitive provisions of the 1996 Act;

[4] *See* "Mission Statement, Objectives and Principles for Developing a Recommendation", adopted by the Task Force December 12, 1998, available at www.wutc.wa.gov/rtf.

2. The Task Force should identify issues that are unique to carriers that serve rural or insular areas and recommend means to address those unique characteristics; and

3. Where necessary, the Task Force should recommend transitional mechanisms, hold harmless provisions, or modifications to minimize adverse impacts to rural or insular consumers and to facilitate investment in modern telecommunications infrastructure by service providers serving rural and insular areas.

These three objectives formed the work plan underlying the Recommendation described in this final report. In preparing this Recommendation, the Task Force has also relied on three broad principles established during its early organizational phase. First, the Recommendation must conform to the universal service principles established by Congress in Section 254(b) of the 1996 Act.[5] Second, any support mechanism recommended by the Task Force must be economically and administratively workable. Third, the Recommendation must be consistent with extending benefits of competitive telecommunications markets to rural and insular areas and with the principle of competitive neutrality. We believe that this final Recommendation to the Joint Board is consistent with these three guiding principles.

In its deliberations, the Task Force has utilized an open, collegial process, involving not only its members, but also a diverse group of interested stakeholders. In general, the Task Force has developed its Recommendation through consensus rather than hard votes around alternative positions. This approach is pragmatic, and it is intended to deliver to the Joint Board a package of recommendations with the potential of being implemented promptly and without legal challenge from affected parties. We observe that while every party has a right to challenge regulatory decisions through appropriate legal avenues, such challenges ultimately result in uncertainty for all parties. Uncertainty over available universal service support ultimately discourages investment in high cost rural areas by both ILECs and CLECs.[6] Our Recommendation builds on the strengths of the Task Force members by developing an up-front consensus among a diverse group of stakeholders on an appropriate universal service mechanism

[5] (1) QUALITY AND RATES.--Quality services should be available at just, reasonable, and affordable rates. (2) ACCESS TO ADVANCED SERVICES.--Access to advanced telecommunications and information services should be provided in all regions of the Nation. (3) ACCESS IN RURAL AND HIGH COST AREAS.--Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas. (4) EQUITABLE AND NONDISCRIMINATORY CONTRIBUTIONS.--All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service. (5) SPECIFIC AND PREDICTABLE SUPPORT MECHANISMS.--There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service. (6) ACCESS TO ADVANCED TELECOMMUNICATIONS SERVICES FOR SCHOOLS, HEALTH CARE, AND LIBRARIES.--Elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services as described in subsection (h). (7) ADDITIONAL PRINCIPLES.--Such other principles as the Joint Board and the Commission determine are necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act.

[6] "ILEC" means incumbent local exchange company; "CLEC" means competitive local exchange company. As used in the Recommendation, we intend to include all competitive service providers, including wireless carriers, in the term CLEC.

for Rural Carriers.

The Recommendation has its foundation in a deliberate written evidentiary record. That record has been assembled in the form of six white papers available on the Rural Task Force web page.[7] Within this final report to the Joint Board, the Task Force will cite and develop appropriate linkages to the written evidentiary record contained in these white papers, as well as to the foundation laid by the 1996 Act and FCC policy documents.

B. Legal and Policy Foundation for the Task Force Recommendation

Early in its process, the Task Force reached consensus on the legal and policy foundation underlying this Recommendation on the appropriate universal service mechanism and policies for universal service in areas served by Rural Carriers. That consensus was formalized in the Task Force's first White Paper entitled, "Rural Task Force Mission and Purpose," published December 1998.

The Task Force recognizes that many of the nation's rural communities are currently served by ILECs and CLECs that provide service to high-cost areas served by non-Rural Carriers. The universal service support needs of these communities were addressed by the FCC in November 1999.[8]

This Recommendation specifically addresses the universal service support needs of the remaining rural, insular and high cost communities currently served by Rural Carriers and CLECs serving those same areas. Both the 1996 Act and statements by the FCC make clear that the universal service mechanism, as well as policies applied in implementing that mechanism for Rural Carriers, may be appropriately different than those adopted for non-Rural Carriers.[9] The Task Force's White Paper 1 provides a complete record detailing relevant citations from the 1996 Act and FCC orders. For purposes of establishing a foundation for this Recommendation, we highlight only a few of the key legal and policy citations in this document.

An essential foundation to our Recommendation is the statutory framework and underlying national policy objectives enacted by Congress in the 1996 Act. The Recommendation considers all relevant provisions of the law including those consistent with extending the benefits of a competitive telecommunications market to rural or insular areas along with the principle of competitive neutrality. However, the heart of the Congressional directive is contained in the universal service principles of Section 254.

The 1996 Act's universal service policies articulated in Section 254(b) generally ensure that all individuals and businesses will have the opportunity to share not only the benefits of a nationwide telephone network, but also the benefits generated by the ongoing global transformation of the

[7] *See* www.wutc.wa.gov/rtf. For any references to Task Force white papers hereafter, please refer to the Task Force web pages for copies.

[8] In re: Federal-State Universal Service Joint Board, CC Docket No. 96-45 *Ninth Report and Order and Eighteenth Order on Reconsideration* (rel. Nov. 2, 1999). This order will be referred to hereinafter as the "Non-Rural Order."

[9] Id. Non-Rural Order at paragraph 11.

availability and uses of information.[10] The 1996 Act broadens the traditional concept of universally available quality telephone service at just, reasonable and affordable rates to include a commitment to make available access to advanced telecommunications and information services "…in all regions of the Nation."[11] The law requires the FCC and the Joint Board to define the services that will receive federal support. The 1996 Act also institutes a program for ensuring nationwide progress as telecommunications and information development unfolds, by requiring regular reexamination of an evolving definition of universal service pursuant to Section 254(c).

Section 254(d) of the 1996 Act requires all carriers that provide interstate service to contribute on an equitable and non-discriminatory basis to support the costs of ensuring nationwide service and network development at affordable and reasonably comparable rates. As a result, the federal mechanism was intended to spread the burden of maintaining and advancing a nationwide public switched network across all carriers and their customers.[12] Section 254(f) provides that a state may adopt regulations not inconsistent with the FCC's rules to preserve and advance universal service. A state may adopt regulations providing additional definitions and standards to preserve and advance universal service within that state only to the extent that such regulations adopt additional specific, predictable, and sufficient mechanisms to support such definitions or standards that do not rely on or burden Federal universal service support mechanisms.

The 1996 Act expressly sets a standard of adequacy for the federal universal support program in that the support "should be explicit and sufficient to achieve the purposes of this section." Sufficiency of support must be gauged against the standards embodied in the universal service principles set forth in Section 254(b).

The 1996 Act also sets standards to prevent waste, windfalls and excessive expense for contributing carriers and their customers. Support may be provided only to a carrier designated as eligible pursuant to Section 214(e). In addition, Section 254(e) provides that any carrier that receives federal support "shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended." Finally, services that are not competitive should "bear no more than a reasonable share of the joint and common costs of facilities used to provide those services."[13]

---

[10] The Task Force notes the parallel language of Section 706 of the 1996 Act, 47 U.S.C. 157.

[11] The 1996 Act also provides for discounts for schools, libraries and rural health care providers and support for low-income consumers.

[12] Section 254 (b) (4) of the 1996 Act establishes the principal that "all providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service." Section 254 (d) establishes the obligation that "every telecommunications carrier that provides interstate telecommunications services shall contribute on an equitable and nondiscriminatory basis, to the specific, predictable and sufficient mechanisms established by the Commission to preserve and advance universal service." That section also gives the Commission the authority to exempt *de minimis* contributions and require contributions from "any other provider of interstate telecommunications." The law does not distinguish between interstate and intrastate revenues but requires all carriers to contribute. In addition, the act defines the term "telecommunications" broadly. The Task Force recommends in order to help ensure the long term stability of universal service funding that universal service support contributions should be assessed on the broadest possible base.

[13] Section 254(k) of the 1996 Act.

The principles in Section 254(b) spell out the results Congress expects to achieve with the universal service mechanisms. Congress also allowed the Joint Board and the FCC to adopt additional principles they found are "necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act."[14] In its May 8, 1997, Universal Service Order the FCC added the principle of competitive neutrality for support mechanisms, which the Task Force took into account in framing its recommendations.[15]
While the universal service principles of the 1996 Act apply equally to Rural Carriers and non-Rural Carriers, Congress explicitly recognized in the 1996 Act that policies pertaining to competitive entry and universal service reform for the "rural telephone companies" may be appropriately different than for other companies. The 1996 Act gives state commissions a degree of latitude to make determinations about which carriers are eligible to receive support based on local circumstances affecting the pace and impact of competitive entry and universal service reform.

Section 214(e)(2) of the 1996 Act gives state commissions a role in deciding whether to designate multiple providers as eligible telecommunications carriers (ETCs) able to receive support for providing federally-defined universal service in an area served by a Rural Carrier.[16] Before designating an additional ETC for an area served by a Rural Carrier, the state commission is required to find that the designation is in the public interest. Section 214(e)(5) defines the term "service area" for the purpose of determining universal service obligations. For areas served by Rural Carriers, this section adds the requirement that an ETC must serve the ILEC's entire study area[17] unless and until the FCC and the states, after taking into account recommendations of the Joint Board, establish a different definition of service area for each company.

Section 251(f)(1) of the 1996 Act exempts Rural Carriers from certain duties to interconnect and provide unbundled network access that apply to other non-rural ILECs. State commissions must evaluate any *bona fide* request to a Rural Carrier for interconnection or network elements to ensure that the request is not unduly economically burdensome, is technically feasible, and is consistent with Section 254.

For an area served by a Rural Carrier, Section 253(f) permits a state commission to require a CLEC to be an ETC as a condition of providing telephone exchange service or exchange access in a Rural Carrier's service area.[18] In effect, the law requires the state commission to

---

[14] Section 254(b)(7) of the 1996 Act.

[15] The FCC recognized, however, that given the complexities and diversity of the telecommunications marketplace, it would be extremely difficult to achieve strict competitive neutrality. *See* In re: Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Report and Order* (rel. May 8, 1997) at Paragraph 48.

[16] The FCC has not adopted rate or service obligations for competitive ETCs (CETCs).

[17] A "study area" is generally the entire territory within a single state served by a telephone company.

[18] Section 253 of the 1996 Act. [47 U.S.C. 253] REMOVAL OF BARRIERS TO ENTRY (f) RURAL MARKETS.--It shall not be a violation of this section for a State to require a telecommunications carrier that seeks to provide telephone exchange service or exchange access in a service area served by a rural telephone company to meet the requirements in Section 214(e)(1) for designation as an eligible telecommunications carrier for that area before being permitted to provide such service. This subsection shall not apply--(1) to a service area served by a rural telephone company that has obtained an exemption, suspension, or modification of Section 251(c)(4) that (continued….)

examine public interest questions concerning a Rural Carrier's study area. By including this provision Congress recognized that unrestricted entry may not be beneficial to consumers in some rural ILEC areas. At the same time, Congress did not intend to deny rural consumers the benefits of competition when the state determines that competition is in the public interest. Notably, Congress did not place similar restrictions on areas served by non-Rural Carriers. This demonstrates a decision by Congress to allow policies pertaining to competitive entry and universal service reform for Rural Carriers to be appropriately different than for non-Rural Carriers.

The Task Force notes that recent Joint Board recommendations and FCC orders also recognize appropriate universal service mechanisms and policies for Rural Carriers may differ from those adopted for non-Rural Carriers. For example, the Joint Board on Universal Service officially moderated its commitment to using a universal service support mechanism based on forward-looking economic cost (FLEC) for the Rural Carriers, even as it moved toward implementing such a support system for non-Rural Carriers. The Joint Board's Second Recommended Decision cautions that "in recommending this framework for determining non-rural carriers' high cost support based on forward-looking cost, we do not intend for the FCC to create any precedent for any potential revisions to support mechanisms for rural carriers."[19] This important aspect of the Joint Board's Second Recommended Decision was adopted and expanded upon by the FCC in its Non-Rural Order adopting the FLEC proxy cost model for non-Rural Carriers.[20]

Rural and insular differences have been a principal reason for delay of access reform for rate-of-return regulated ILECS. These differences convinced the FCC that it should not implement reform for the primarily small and rural rate-of-return regulated ILECs in the same manner, or at the same time, that it reformed access charges for the larger price cap-regulated carriers. On May 26, 1998, the FCC opened a separate access reform proceeding for rate-of-return-regulated ILECs. In the Notice of Proposed Rulemaking (NPRM), the FCC acknowledged that rate-of-return-regulated ILECs face significantly higher costs and recover a much larger percentage of their total revenues from access charges than do price cap-regulated ILECs.[21] The FCC also acknowledged the substantial differences among rate-of-return-regulated carriers, stating that "[t]hey are not, however, a homogenous group, and their operating conditions vary significantly."[22] These different circumstances, the FCC recognized, "may require different approaches to reform, including a different transition to more economically efficient, cost-based

(Continued from previous page)
effectively prevents a competitor from meeting the requirements of Section 214(e)(1); and (2) to a provider of commercial mobile services.

[19] In re: Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Second Recommended Decision* (rel. Nov. 25, 1998) at Paragraph 30.

[20] "The support mechanism for rural carriers will remain unchanged at least until January 1, 2001, and reform will be undertaken only after the Commission, the Joint Board, and a Rural Task Force appointed by the Joint Board have selected an appropriate methodology for rural support." Non-Rural Order at Paragraph 11.

[21] Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, CC Docket No. 98-77, *Notice of Proposed Rulemaking*, FCC 98-101 (rel. June 4, 1998), Paragraphs 16 and 35 (Rate-of-Return Access NPRM).

[22] *Id.*, Paragraph 14.

interstate access charges."[23]

C. Empirical Justification for a Distinct Rural Carrier Universal Service Mechanism

Congress, the FCC and the Joint Board have each concluded that universal service mechanisms and policies applying such mechanisms must be flexible in recognition that market and operational factors associated with Rural Carriers may be substantially different from those associated with non-Rural Carriers. For the most part, however, the precise scope and magnitude of those differences had not been documented. Recognizing this gap in the evidentiary record, the Task Force undertook a detailed study of the "rural differences." Conclusions from that study are summarized in White Paper 2, "The Rural Difference," released by the Task Force in January 2000.[24] White Paper 2 analyzes publicly available national data assembled for the first time, to systematically compare and contrast Rural Carriers and non-Rural Carriers. Equally important, the analysis conducted by the Task Force documents a substantial diversity among Rural Carriers themselves. An understanding of the differences between Rural Carriers and non-Rural Carriers and the diversity among Rural Carriers is key to designing appropriate mechanisms and policies which will allow the fulfillment of the 1996 Act's universal service principles.

The following are major Rural Carrier differences identified by the Task Force and described in White Paper 2:

<u>Rural Carriers serve more sparsely populated areas</u>

- Both Rural Carriers and non-Rural Carriers serve rural communities. However, Rural Carriers' operations tend to be focused in the more geographically remote areas of the nation with widely dispersed populations.
- Nationwide, Rural Carriers serve about eight percent of the nation's access lines, 38 percent of the nation's land area, and 93 percent of the study areas.
- The average population density is only 13 persons per square mile for areas served by Rural Carriers compared with 105 persons per square mile in areas served by non-Rural Carriers.
- Evaluating proxy cost model output for a representative sample of ten states, Rural Carriers serve 70 percent of the modeled serving areas with fewer than five lines per carrier serving area, but only ten percent of the modeled serving areas with over 100 lines per carrier serving area.

<u>There is significant variation in study area sizes and customer bases among Rural Carriers</u>

---

[23] *Id.*, Paragraph 4.

[24] *See* www.wutc.wa.gov/rtf.

- The vast majority of access lines served by Rural Carriers are clustered in the largest study areas in terms of line size.

- Rural Carriers serving the three smallest study area groupings (2,500 lines or less) encompass 48 percent of all study areas in terms of line size, but only five percent of all access lines served by Rural Carriers. On the other hand, Rural Carriers serving the three largest study area groupings (20,000 lines or more) contain only 10.5 percent of all study areas, but 67 percent of all Rural Carrier access lines.

- The average population density of areas served by Rural Carriers varies dramatically. Rural Carriers in Alaska and Wyoming serve populations of 0.58 and 1.25 persons per square mile respectively, while Rural Carriers in some states serve populations of over 100 persons per square mile.

<u>Isolation of areas served by Rural Carriers results in numerous operational challenges</u>

- Rural Carriers have relatively high loop costs because of the lack of economies of scale and density.

- Rural Carriers experience difficulty and high cost in moving personnel, equipment and supplies to remote and insular communities.

- Geographic surface conditions - such as coral, volcanic rock and permafrost - require expensive specialized outside plant construction practices.

- More resources, including duplicate facilities and backup equipment are required to protect network reliability.

<u>Compared to non-Rural Carriers, the customer base of Rural Carriers generally includes fewer high-volume users, depriving Rural Carriers of economies of scale</u>

- On average, multi-line business customers represent about 13 percent of total business lines served by Rural Carriers compared to over 21 percent of the lines served by non-Rural Carriers.

- Non-Rural Carrier study areas typically have higher business customer density than Rural Carrier study areas.

- On average, special access services purchased by large users only represent about three percent of total interstate revenues for Rural Carriers compared to nearly 18 percent for non-Rural Carriers.

- There is substantial diversity among Rural Carriers in providing special access service to customers. Interstate special access revenues compared to total interstate revenues for Rural Carriers range from zero to 36 percent.

<u>Compared to customers of non-Rural Carriers, customers of Rural Carriers tend to have a relatively small local calling scope and make proportionately more toll calls</u>

- On average, local minutes comprise 85 percent of total intrastate minutes for non-Rural Carriers, but only about 69 percent of total intrastate minutes for Rural Carriers.

- Rural Carriers have a higher average proportion of interstate toll minutes to total minutes (21 percent) than non-Rural Carriers (16 percent).

- Seventy to 80 percent of customers of smaller Rural Carriers can reach less than 5,000 other customers with a local call. Only 10 percent of smaller Rural Carriers have local calling capability to reach as many as 25,000 other subscribers.

<u>Rural Carriers frequently have substantially fewer lines per switch than do non-Rural Carriers, providing fewer customers over which to spread high fixed network costs</u>

- On average, Rural Carriers have only 1,254 customers per switch compared to over 7,000 customers per switch for non-Rural Carriers.

- For Rural Carriers, the number of lines per switch decreases dramatically as the line size of the study area served decreases. Rural Carrier study areas with more than 100,000 lines average nearly 3,000 lines per switch, compared to an average of only 223 lines per switch for study areas with less than 500 lines.

<u>Total investment in plant per loop is substantially higher for Rural Carriers than for non-Rural Carriers</u>

- On average, total plant investment per loop is over $5,000 for Rural Carriers compared to less than $3,000 for non-Rural Carriers.

- Average total plant investment per line for Rural Carriers increases as the line size of the study area decreases. Average total plant investment per line ranges from $3,000 for Rural Carriers with the largest study areas to over $10,000 for Rural Carriers with the smallest study areas.

- The range of values for total plant investment per loop for Rural Carriers ($1,400 to $40,500) is far greater than the range for non-Rural Carriers ($1,570 to $4,350).

<u>Plant specific and operations expenses for Rural Carriers tend to be substantially higher than for non-Rural Carriers</u>

- On average, plant specific expenses per loop are $180 for Rural Carriers compared to $97 per loop for non-Rural Carriers.

- Average Rural Carrier plant specific expenses increase consistently as the number of lines served decreases, from approximately $110 per loop for carriers with more than 20,000 lines to $445 per loop for carriers with study areas having less than 500 lines.

- The range of total plant specific expenses per loop for Rural Carriers ($4 to $1,585) is substantially greater than for non-Rural Carriers ($38 to $163).

- Depreciation expenses and corporate operations expenses per loop tend to follow similar trends as plant specific expenses, that is, they increase as the number of lines served decreases.

<u>Customers served by Rural Carriers have different demographic characteristics from customers in areas served by non-Rural Carriers</u>

- 1990 U.S. Census data indicates the average annual household income for customers in Rural Carrier Service areas was $31,211, twenty percent lower than that of non-Rural Carrier customers ($38,983).

- Native Americans are disproportionately represented among those without phone service. Rural Carriers serve a higher percentage of Native American customers than non-Rural Carriers.[25]

- The Kindergarten – 12th Grade school is the point of Internet access for 30 percent of persons in rural areas, compared to only 21.8 percent for the nation as a whole.[26]

In passing the 1996 Act, Congress was clear that we are one nation, and that national universal service policy must ensure that the benefits of telecommunications industry reform accrue to all Americans, including those in remote, rural and insular regions. The evidentiary record assembled by the Task Force clearly supports a conclusion that a "one-size-fits-all" national universal service policy is unlikely to be successful in fulfilling the national universal service principles contained in the 1996 Act. To be successful, the policies and mechanisms ultimately adopted must be flexible enough to accommodate the wide range of market and operational circumstances faced by telecommunications carriers serving rural populations. This observation, grounded in empirical evidence, is fundamental to the choices and recommendations advanced by the Task Force.

D. Policy Context Facilitating Both ILEC and CLEC Investment in Rural Communities

A high quality telecommunications infrastructure is necessary in order to provide for the economic, educational, health care and other opportunities essential to the future vitality of our rural communities. The Task Force reached agreement that a primary purpose of universal service support is to promote investment by both ILECs and CLECs in rural America's telecommunications infrastructure. This investment is necessary to ensure universal access to telecommunications services which are comparable to those available in urban areas, and to provide a platform for delivery of advanced services.

A universal service system which delivers sufficient support should also provide proper

---

[25] For more information on Rural Carrier service to Native Americans, *see* National Telephone Cooperative Association (NTCA) paper, *Dial Tone is Not Enough: Serving Tribal Lands*; NTCA, November 1999, and *NTCA Members Serving Tribal Areas Survey Report*, NTCA, December 10, 1999. *See* www.ntca.org.

[26] National Telecommunications and Information Administration, *Falling Through the Net: Defining the Digital Divide* (July 1999), page 36, Chart II-15.

incentives for investment in rural America. In order to provide these incentives, the universal support mechanism should be transparent, stable, predictable, and competitively neutral as well as sufficient. To this end, the Recommendation is based on a consensus of diverse interests. This should minimize controversy and legal challenges which create delay and uncertainty, and discourage investment. The Recommendation also attempts to provide sufficient support on an economically viable, administratively workable, and accountable basis. This should ensure that support is available to all carriers who accept the responsibilities of becoming ETCs, and that support is targeted to rural areas in a cost-effective manner.

The universal service mechanism recommended by the Task Force is a package of initiatives designed to provide both ILECs and CLECs with predictable and stable funding to motivate investment over the near-term future. The Task Force recognizes that the telecommunications industry is dynamic and changing rapidly. We believe it is unrealistic to expect any universal service mechanism to provide a stable, predictable and workable funding source for a period longer than five years. Consequently, we recommend that the Recommendation be implemented immediately and remain in place for a five year period. Plans should be made to evaluate appropriate universal service funding approaches for areas served by Rural Carriers prior to the end of this five year period.

III. METHODS AND POLICIES TO ESTABLISH PREDICTABLE AND SUFFICIENT SUPPORT FOR RURAL CARRIERS

Over the past two years the Task Force has undertaken a deliberative process to consider alternative methods and specific policies to establish predictable and sufficient financial support for Rural Carriers operating within high cost areas. In evaluating these alternative methods and policies, the Task Force gave careful consideration to all aspects of the 1996 Act, including the competitive provisions and universal service principles outlined in Section 254(b). Further, the Task Force gave significant weight to the administrative and economic viability of each alternative. As has been noted, a detailed record of the Task Force's proceedings are documented by the Task Force in a series of white papers and in meeting minutes available on the Task Force website.[27] Our purpose here is to highlight only briefly the key considerations and describe the specific recommendations agreed to by Task Force members.

A. Alternative Methods for Sizing the Fund –Overview of Options Considered

In its Mission Statement the Task Force made a commitment to explore alternative mechanisms for determining universal service support for Rural Carriers.[28] Throughout the course of its work, the Task Force considered a number of options for determining appropriate levels of universal service support for rural companies. In evaluating the different methods, the Task Force was guided by criteria developed early in the Task Force deliberations. These criteria are not simple restatements of the universal service principles.[29] They combine the universal service principles with the tenets of technological and competitive neutrality, network evolvability,

[27] *See* www.wutc.wa.gov/rtf.

[28] *See Mission Statement, Objectives and Principles for Developing a Recommendation*, adopted by the Task Force December 12, 1998, available at www.wutc.wa.gov/rtf.

[29] Id.

and economic and administrative viability.[30]

The Task Force criteria for an appropriate support mechanism for Rural Carriers may be summarized as follows:

1. **Sufficiency**: Does the mechanism ensure comparability of service and rates between urban or suburban customers and rural or insular customers?

2. **Affordability**: Does the mechanism enable providers to offer the supported services in an affordable manner?

3. **Competition**: Does the mechanism encourage and facilitate competition by precisely targeting support to high cost customers?

4. **Flexibility**: Is the mechanism able to evolve as new technologies are introduced, as competition develops, and as the definition of universal services changes over time?

5. **Protection and Advancement:** Does the mechanism prevent degradation of the existing infrastructure and the current level of service? Does the mechanism produce an investment incentive to upgrade facilities used to provide universal service?

6. **Portability**: Can the mechanism provide to all ETCs an appropriate amount of support in a competitively neutral manner?

7. **Predictability**: Does the mechanism enable a competitor or incumbent carrier to determine in advance the amount of support it will receive on behalf of a customer?

8. **Practicality**: Is the mechanism economically and administratively viable?

In reviewing the different alternative support mechanisms set forth below, the Task Force applied these criteria to each alternative. In developing its record, the Task Force considered several alternative methods to size the Rural Carrier fund including:

a) The Current Rural Support Mechanism (also referred to as the "Embedded Cost" Mechanism);

b) A Modified Embedded Cost Mechanism explicitly considering policy applications to address sufficiency and competitive concerns;

c) The FCC's mechanism for non-Rural Carriers using a forward-looking cost model;

d) Competitive bidding approaches;

[30] See *Criteria to Determine if the Final Universal Service Support Mechanism for RTC's is Reasonable*, available at www.wutc.wa.gov/rtf.

e) Rate Buy-down Mechanisms, which allow rates to float to market level with an adjustment assuring customers pay no more than a targeted affordable level; and

f) A Melded Approach representing an attempt to blend the strengths of both the embedded cost mechanism and the Synthesis Model.

The strengths and weaknesses of each of these alternatives were identified and compared in White Paper 3, "Alternative Mechanisms for Sizing A Universal Service Fund for Rural Telephone Companies," published in August, 2000. Of the approaches evaluated, the Modified Embedded Cost Mechanism, with policy modifications to accommodate the sufficiency and competitive mandates of the 1996 Act, and the FCC non-rural method were considered to be the primary candidates for recommendation as the appropriate mechanism to size the universal service fund for Rural Carriers.

B. Evaluation of the Synthesis Model Applied to Rural Carriers

The Public Notice establishing the Rural Task Force directed the Task Force to give special consideration to the proxy cost models used for sizing and targeting universal service support to non-Rural Carriers.[31] The FCC, in fact, ultimately adopted a proxy cost model for use in sizing and targeting the non-rural fund in its Non-Rural Order.[32] The Task Force gave careful consideration to the model adopted by the FCC for non-Rural Carriers, and examined both the potential value and risks associated with applying the same model for determining forward-looking support for Rural Carriers and competitors serving customers in those areas. In conducting this analysis, the Task Force developed and adopted criteria in November 1999 for the evaluation of the proxy model tool for use with Rural Carriers. The criteria are detailed in White Paper 4 "A Review of the FCC's Non-Rural Universal Service Fund Method and the Synthesis Model for Rural Telephone Companies."

A detailed study was made of 23 sample companies. Also, a comparison of model results to actual company data for 195 additional companies was made. Attempts were made to study a diverse group of companies in terms of size, geography and regions of the nation. Application of the FCC Synthesis Model to the rural test companies produced the following results:

- The model lines differed significantly from actual lines served. While the model generally tended to underestimate lines, in about one-third of the wire centers it overestimated lines.

- Comparisons of the number of route-miles of plant summarized in the model with actual

---

[31] "Federal-State Joint Board on Universal Service Announces the Creation of Rural Task Force; Solicits Nominations for Membership on the Rural Task Force." *Public Notice* FCC 97J-1, (rel. Sept. 17, 1997).

[32] *See* Non-Rural Order. These support calculations were revised on January 20, 2000, and April 7, 2000. *See*, "Common Carrier Bureau Announces Procedures for Releasing High-Cost Support Amounts for Non-Rural Carriers and Revised Model Results," FCC *Public Notice*, CC Docket No. 96-45, 97-160, DA 00-110 (Jan. 20, 2000) and In re: Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Twentieth Order on Reconsideration,* FCC 00-126 (April 7, 2000). Under these revised figures total annual funding for non-rural companies is estimated to be $220 million (exclusive of "hold harmless" support).

data produced significant variations. Again, differences occurred on both the high and low ends with a general tendency for the model results to overestimate the actual data. In 12 percent of the wire centers studied, the model overestimated route miles by more than 200 percent.

- Model results for the type of plant varied widely from actual plant constructed. The model generally tended to overestimate the percentage of aerial and underground plant, and underestimated the percentage of buried plant. This was likely due to the diverse character of the rural geography, and the use of a single set of inputs by density zone that was based on the experience of non-Rural Carriers.

- In calculating the applicable density zones, the model significantly underestimated wire center area. In 95 percent of wire centers the land area was understated, and in over one third of these the understatement exceeded 90 percent.

- The Synthesis Model significantly underestimated central office equipment (COE) Switching investment. This was likely due to the lack of economies of scale of the Rural Carriers, and the general tendency of the model to underestimate lines served.

- The Synthesis Model results for various elements of general support investment varied widely from actual data and from rational forward-looking assumptions, with almost as many cases of overestimation as underestimation.

- Network Operations and Customer Operations expenses were significantly underestimated. This was likely related to the lack of economies of scale of Rural Carriers.

The analysis also indicated that the model does not currently contain customer location and other data to produce results for rural wire centers in Alaska and the insular areas. The reasons for this are detailed in White Paper 4.

The aggregate results of this study suggest that, when viewed on an individual rural wire center or individual Rural Carrier basis, the costs generated by the Synthesis Model are likely to vary widely from reasonable estimates of forward-looking costs. As a result, it is the opinion of the Task Force that the current model is not an appropriate tool for determining the forward-looking cost of Rural Carriers.

In making this recommendation, the Task Force recognizes that policy makers, after the development and rigorous analysis of the Synthesis Model, have determined that it should be applied in developing universal service support for non-Rural Carriers. While the Task Force arrived at a different conclusion in regard to use of the model for Rural Carriers, we do not intend to imply in any way that revisions are needed to support mechanisms for non-Rural Carriers. Our analysis and recommendations are focused solely on Rural Carriers.

C. Tools versus Application

In considering both the potential value and risks associated with applying the FCC's Synthesis Model to estimate and target sufficient universal service support to Rural Carriers and competitors serving the same areas, it was obvious that the policies underlying the application of the proxy cost model tool were equally important, if not more important than the tool itself. An initial step in the Task Force's analysis was to directly apply both the Synthesis Model and the FCC's method for determining high-cost support for non-Rural Carriers. The results of that analysis are documented in White Paper 4.

We note here that applying the FCC's Synthesis Cost Model directly to the task of sizing the national Rural Carrier high cost fund and using the same policy mandates adopted for non-Rural Carriers would reduce available support to Rural Carriers from the current $1.553 billion to $451 million, a reduction of over one billion dollars. A primary reason for that reduction was the FCC's decision to rely on a nationwide benchmark and statewide cost-averaging to determine a "sufficient" level of federal funding for non-Rural Carriers. Because Rural Carriers represent only a fraction of the overall industry, their addition in determining the national average cost benchmark changes the average by only a small amount,[33] even though as a group the average total cost of service for Rural Carriers is more than twice that of non-Rural Carriers.[34] For the same reason, averaging the cost of Rural Carriers with the costs of all other carriers within a state would eliminate funding for many Rural Carriers. Thirty-seven states, territories, and protectorates which receive federal universal service support for Rural Carriers today would receive zero support if statewide cost-averaging and a national benchmark were used in sizing the universal service fund available to Rural Carriers.[35]

The Task Force recognizes that policymakers would not likely adopt a statewide cost-averaging and a national benchmark for application to the Rural Carrier mechanism with this knowledge available to them. We further recognize that alternative benchmarks are easily considered. However, the exercise of applying the non-Rural Carrier policies directly in considering use of the Synthesis Model for sizing the Rural Carrier fund was helpful to Task Force members, highlighting the importance of specific policy choices in designing an appropriate support mechanism tool and policy.

This line of inquiry and the record assembled to support the inquiry is instrumental to the Task Force's recommendation of the method to size the fund necessary to provide sufficient support to Rural Carriers and competitors providing service in those areas. Weaknesses associated with both the Synthesis Cost Model and embedded cost approaches can potentially be mitigated by appropriate policy choices. Consequently, the choice of method to size and target the fund may appropriately rest at least in part on practical considerations; such as administrative simplicity and ease of minimizing unintended consequences.[36]

---

[33] The estimated nationwide average cost per line increases from $23.52 per line for non-Rural Carriers to $26.09 per line for non-Rural Carriers and Rural Carriers combined.

[34] The estimated average cost per line for Rural Carriers is $59.36 per line compared to an estimated $23.52 per line for non-Rural Carriers. It should be noted that based on subsequent input changes for the Synthesis Model, the current estimated nationwide average cost per line for non-Rural Carriers has changed to $23.35 per line.

[35] *See* Appendix D of White Paper 4.

[36] The Task Force did not compute the impact on Rural Carriers of using the current Rural Carrier benchmarks and policies with the Synthesis Model. This was not done for several reasons in addition to the fact that the costs generated by the Synthesis Model are likely to vary widely from reasonable estimates of forward-looking costs. These reasons included the perceived administrative complexity of adapting the Part 36 Rules for calculating the (continued….)

D. Recommended Method for Sizing the Fund

For the reasons detailed in White Paper 4, we conclude that the non-rural method and Synthesis Model developed for the non-Rural Carriers are not the appropriate tool and application for Rural Carriers and will not produce a sufficient universal service mechanism for Rural Carriers that is in the public interest and consistent with the principles of the 1996 Act. The Task Force Recommendation relies on the Modified Embedded Cost Mechanism for Rural Carriers as a baseline to size the fund for Rural Carriers. This method is based on embedded costs of each ILEC's study area. In other words, support is based on the investments and expenses of each study area.

There are three forms of support currently flowing to Rural Carriers:

1. The High Cost Loop[37] (HCL) fund helps offset the cost of loop facilities used to provide local service. When a study area's average loop cost exceeds 115 percent of the national average loop cost, that study area receives a portion of its costs above 115 percent from the fund. The amount of support increases in specified steps as the percentage of cost that exceed the national average rises.

2. Long-Term Support[38] (LTS) helps offset the cost of interstate access for Rural Carriers remaining in the National Exchange Carrier Pool (NECA) pool.

3. Local Switching Support[39] (LSS) provides support for the high per-line local switch equipment costs incurred by carriers with less than 50,000 loops.

These three funds currently provide approximately $1.553 billion in annual support to the over 1,300 Rural Carrier study areas in the United States and its territories. Each form of support is determined by averaging costs over the company's entire study area. (LTS is averaged over all companies participating in the NECA common line pool.) Per line support is determined by dividing total support by the total number of lines within a study area.

The total amount of the HCL available for Rural Carriers is currently capped. Under the cap, overall high cost support grows at the same rate as the growth in the number of access lines, including the lines of non-Rural Carriers. It is estimated that without the cap, the High Cost Fund for Rural Carriers would be approximately $83.9 million higher.[40] The Task Force studied the

(Continued from previous page)
High Cost Loop fund and Local Switching Support to the Synthesis Model, and the anticipated significant increase in high cost support that would result from such an analysis, which would be applied on a study area basis.

[37] *See* 47 C.F.R. Section 36.631.

[38] *See* 47 C.F.R. Section 54.303.

[39] *See* 47 C.F.R. Section 54.301.

[40] In addition to the cap on the growth of the HCL fund, there is a limitation on recovery of corporate operations expense and caps on universal service funds related to newly acquired exchanges. It is estimated that removal of the corporate operations expense limitation would increase the fund for rural carriers by $34.6 million, and that removal of the cap on acquired exchanges would increase the fund by $12.8 million. *Universal Service Fund 1999 Submission*, NECA (Oct. 1, 1999).

characteristics and operation of the current support system as a benchmark for comparison of all other support mechanisms.

In recommending the Modified Embedded Cost Mechanism for federal universal service support for Rural Carriers, the Task Force recognized some of the weaknesses of the current system and included modifications to address these weaknesses and to adapt the mechanism to the current environment. Modifications are necessary to ensure support is sufficient to achieve the universal service principles contained in Section 254 of the 1996 Act. Universal service funding is not a static need, but rather must be dynamic, adjusting to provide support available in sufficient amounts to ensure the mandates of the 1996 Act are achieved in rural areas as technology advances. Specific recommendations for modification to the current method of federal universal service support are made in Section IV of the Recommendation.

Modifications necessary to make the current rural funding mechanism consistent with the competitive provisions of the 1996 Act and the principle of competitive neutrality are equally important. In recommending the use of the Modified Embedded Cost Mechanism to implement federal universal service support for Rural Carriers, the Task Force urges the FCC to also adopt specific actions to ensure ILECs and CLECs have access to available funding on an equivalent basis. Specific recommendations are made in Section V of this Recommendation.

Finally, in recommending the Modified Embedded Cost Mechanism for Rural Carriers, the Task Force represents to the Joint Board and the FCC that we have carefully considered available checks and balances within the system to ensure universal service dollars are spent for the purposes they are intended by the 1996 Act as discussed hereafter. Specific recommendations are made in Section IV (D) below.

IV. POLICY CHOICES AFFECTING REQUIRED FUND SIZE

In recommending the Modified Embedded Cost Mechanism of universal service support for Rural Carriers, the Task Force recognizes certain changes are necessary to ensure funding available to both CLECs and ILECs is sufficient to achieve the universal service mandates of the 1996 Act and is available to all ETCs on an equitable and competitively neutral basis. Below we highlight specific recommendations necessary to provide sufficient support.

A. Recommendations Requiring Sufficient Funding to Achieve Advanced Telecommunications Service Access and Comparability Provisions of Section 254

The 1996 Act delineates the requirements related to advanced services in Sections 254 and 706. Working from these statutory mandates and cognizant that recent studies indicate that advanced services and broadband infrastructure have been deployed much more extensively in the more urbanized areas of the United States, the Task Force has examined the issue of providing access to advanced services.[41] The provision of access to advanced services is required under

[41] An April 2000 report by the National Telecommunications and Information Administration and Rural Utilities Service found that digital subscriber line (DSL) and cable modem deployment in large cities surpassed that in small towns by more than a factor of ten. *See Advanced Telecommunications in Rural America: The Challenge* (continued….)

Section 254(b) and is separate and distinct from the actual provision of advanced services when and if they have been added to the supported services defined periodically by the FCC under Section 254(c).

1. Advanced Services

Under the 1996 Act, universal service is an evolving level of telecommunications services that the FCC shall establish periodically, taking into account advances in telecommunications and information technologies and services. Because of advances in telecommunications services, the Task Force recommends that the Joint Board review the definition of the services that are supported by federal universal service support mechanisms.

In recommending that support for Rural Carriers be based on embedded costs, the Task Force is recommending a support mechanism that inherently provides incentives for the infrastructure investments necessary for providing access to advanced services. Just as the FCC "removed barriers from infrastructure investment" in its implementation of the Synthesis Model, policies should be adopted that remove barriers from infrastructure investment for the rural ETCs, and encourage the provision of comparable and comparably-priced access to advanced services.

The Task Force also recommends that a "no barriers to advanced services" policy be adopted that incorporates the following principles:

a. Universal service funding should support plant that can, either as built or with the addition of plant elements, when available, provide access to advanced services. State commissions could facilitate this infrastructure evolution and may make an exception for carriers with functional but non-complying facilities.[42]

b. Telecommunications carriers should be encouraged by regulatory measures to remove infrastructure barriers relating to access to advanced services.

c. The federal universal service support fund should be sized so that it presents no barriers to investment in plant needed to provide access to advanced services. Specifically, to remain "sufficient" under the 1996 Act, the fund should be sized so that investment in rural infrastructure will be permitted to grow.[43]

(Continued from previous page)
of Bringing Broadband Service to All Americans, at page ii. In August 2000, the FCC identified, among others, "those living in sparsely populated areas . . . and . . . in the U.S. territories" as "particularly vulnerable to not having access to advanced services." *Deployment of Advanced Telecommunications Capability*: Second Report, page 6.

[42] Not all ETCs can provide access to advanced services over existing infrastructure, and the Task Force recommends that an ETC should not lose universal service support, or be denied ETC designation because it cannot provide access to advanced services, as currently defined, if it otherwise provides all of the supported services.

[43] *See* 47 U.S.C. 254(b)(4).

2. Information Services

In addition to requiring access to advanced services, Sections 254(b)(2) and (3) require access to information services that is reasonably comparable to that provided in urban areas. This access is separate and distinct from access to advanced services. Information services can be accessed over voice grade circuits to Internet service providers. For this access to be comparable to urban areas, it should be at a bit rate equal to that received by urban customers. About two-thirds of urban customers are in areas served by plant capable of receiving this service at a rate of at least 28.8 kilobits per second.[44]

While this service is different from access to advanced services, there is an important relationship between the plant architectures that provide the two services. The "no barriers to advanced services" plant architecture recommended above supports 28.8 kilobits per second modem access. Investments made to comply with the 1996 Act's requirements to provide access to advanced services would thus serve a double function.

The Task Force recommends that the list of supported services should evolve to include access to information services at a rate that is reasonably comparable to that provided in urban areas. Plant that will provide access to advanced services will also provide access to information services at this rate.

B. Recommendations Providing for Fund Growth Necessary to Achieve Section 254 Mandates – Caps and Limitations to the Existing HCL

Current FCC rules limit the availability of HCL assistance to carriers in three ways:

1. Growth in total HCL funds available is limited to the prior year's level of payments increased by the growth in lines subject to Section 36.601(c) universal service rules;

2. Corporate operations expenses assigned to the HCL fund calculation is limited; and

3. Individual study area expense adjustment limitations are imposed by the FCC when granting some study area waivers for some entities involved in the purchase or acquisition of exchanges[45] and Section 54.305 of the FCC rules which limits the universal service support for an acquiring company to the support received by the selling company.

---

[44] *See* Comments of the Rural Utilities Service, In The Matter of Requests to Redefine "Voice Grade Access" For Purposes of Federal Universal Service Support, January 19, 2000, CC Docket No. 96-45, www.usda.gov/rus/unisrv/01-19com.htm.

[45] On August 4, 2000, the FCC adopted an Order removing the interim caps for all carriers who had previously had limitations placed on their universal service support as a result of purchase or acquisition of property from another local exchange carrier. Petitions for Waiver Concerning Definition of "Study Area," CC Docket No. 96-45, *Order* (rel. Aug.4, 2000).

In order to provide appropriate incentives to invest in rural America while maintaining the fund at a reasonable level, the Task Force recommends that the Joint Board and FCC enact the following modifications to the caps and limitations which currently exist related to the universal service support mechanisms for Rural Carriers.

1. Indexed Cap On High Cost Loop Support

In general the Task Force recommends that the HCL fund be re-based and a new cap factor be applied on a going-forward basis. In addition, a new procedure should be established to determine per-line support when a competitive ETC (CETC) begins providing service in a Rural Carrier service area. Finally, a new HCL fund "safety net" calculation is proposed to provide additional support to Rural Carriers who make a significant investment in rural infrastructure. In particular, the Task Force recommends:

a. Re-basing the Cap

i) The existing indexed cap on the HCL fund should be removed and the portion of the HCL fund for Rural Carriers should be separated from the non-Rural Carriers' portion of the fund.

A) The rural portion should initially be recomputed by the fund administrator at the level required for Rural Carriers as if the indexed fund cap and the corporate limitation had not been in effect for support for the calendar year 2000 (i.e., based on 1998 calendar year data using the October 1, 1999 data submission).[46]

B) For 2001 and future years, the Rural Carrier fund should be calculated using the existing methods as modified by the recommendations outlined below.

ii) The national average loop cost should be frozen at $240.00, which approximates the actual average for year 2000 support (i.e., based on 1998 data).

iii) The total individual company study area support should continue to be calculated based on the ILEC's costs and loops under the current "expense adjustment" formulas with the modification to corporate operation expenses discussed below.

b. New Indexed HCL Fund Cap

i) A new indexed cap on the ILECs' portion of the HCL fund should be imposed with annual maximum growth derived by the "Rural Growth Factor" (RGF).

A) The RGF is the sum of the annual percentage change in Gross Domestic Product-Chained Price Index[47] plus the percentage change in loop count for Rural Carriers, using a

[46] This re-basing should result in an increase to the HCL fund of approximately $118.5 million consisting of $83.9 million for the indexed fund cap and $34.6 million for the corporate operations expense limitation based on October 1, 1999 data and calculations supplied by NECA to the Task Force.

[47] This is the same factor used for the LTS calculation.

consistent definition of Rural Carrier study areas in the numerator and denominator of the equation calculating the change in loop counts. The RGF should be computed annually by the federal universal service fund administrator to determine the succeeding year HCL fund cap level for Rural Carriers.

B) The maximum support under the indexed HCL fund cap for 2001 for the ILECs' portion of the HCL fund should be the year 2000 HCL amount described in Subsection IV(B)(1)(a)(i)(A) times one plus the RGF.

C) For each of the succeeding years, the cap should be computed by taking the total loop cost expense adjustment for the immediately preceding calendar year, times one plus the RGF.

D) In any year when the cap is reached, the "safety net" provisions described in Subsection IV (B)(2)(e) below should be computed and implemented by the federal universal service fund administrator.

ii) Current procedures will remain in place excluding the HCL fund support paid to CETCs from the indexed cap calculation.

c. Support in Areas with CETCs

i) In areas served by Rural Carriers where a CETC has not submitted revenue producing lines to the federal universal service administrator in order to receive support, per line support available to the CETC would be determined pursuant to the disaggregation paths set forth V(A). However, support paid to the ILEC would be based on Subsection IV(B)(1)(a)(iii) of the Recommendation.[48]

ii) In study areas where a CETC has been approved and the CETC is providing service, universal service support payments per loop to the ILEC and CETC serving the same area should be the same and should be determined by freezing the ILEC support per loop.

A) The disaggregated support per loop should be frozen based on the data for the twelve month period ending with the end of the quarter prior to the quarter in which the CETC first reports revenue-producing lines to the federal universal service administrator to receive support.[49] In no event will the ILEC's HCL fund support

---

[48] For transparency purposes, the ILEC's disaggregation plan would disaggregate the study area support on a per line basis as set forth in Section V(B)(2). It should be noted that in areas served by Rural Carriers where a CETC has not submitted revenue producing lines to the federal universal service administrator, the ILEC would receive monthly universal service support payments based on the annual USF support (i.e., HCL, LTS and LSS) divided by 12.

[49] The ILEC would be required to update their universal service fund data for the twelve months ended the quarter prior to the CETC submitting loops to the federal universal service fund administrator. The universal service fund data submissions would include the ILEC updating all of the investments, expenses and loop data. The frozen support per line would be computed by taking the ILEC's support divided by the lines at the end of the twelve month reporting period.

Month CETC submits lines to the Administrator	ILEC submits updated data for the 12 months ending:

(continued….)

exceed the amount the ILEC would receive under the method set forth in Subsection IV(B)(1)(b)(i).

B) Both the ILEC and the CETC's support should be adjusted quarterly for actual revenue-producing lines in service.

C) The support per loop would be increased annually by the RGF used to grow the indexed cap for the fund.

D) In a year when the overall indexed HCL fund cap is invoked, the ILEC HCL payments for the study area will be the lesser of the amount calculated in sections IV(B)(1)(c)(ii)(A) through IV(B)(1)(c)(ii)(C) above or the "expense adjustment" calculated pursuant to normal rules under the new cap mechanism described in Subsection IV(B)(1)(b) above.

E) Notwithstanding the above limitation on per line support, an ILEC may adjust frozen per loop support to recover costs of catastrophic events affecting the ability of ETCs to provide universal service.[50] Such catastrophic events shall include hurricanes, floods, earthquakes, fires or other natural disasters evidenced by a declaration of natural disaster by state or federal authorities and which directly affect the ability of ETCs to deliver universal service.

F) Under any circumstances set forth above, ILECs and CETCs serving the same area would receive the same amount of support per loop.[51]

d. New Supported Services

The indexed cap should be resized whenever the definition of supported services is changed.

e. Safety Net

In a year where the new indexed cap on the HCL fund limits the study area's expense adjustment, the federal universal service fund administrator will determine if any study areas

(Continued from previous page)

January, February, March	December 31
April, May, June	March 31
July, August, September	June 30
October, November, December	September 30

For example, if a CETC submits lines in June 2001 to the federal universal service fund administrator, the ILEC would be required to update the ILEC's universal service fund data submission for the 12 months ending March 31, 2001. The frozen support per line would be computed by taking the ILEC's support for the 12 months ending March 31, 2001 divided by the lines as of March 31, 2001. These amounts would be disaggregated pursuant to other provisions in the Task Force's Recommendation.

[50] The term "costs" as used herein is intended to include both expenses and investment.

[51] It should be noted that the Task Force could not reach agreement on the "stranded cost" issue. *See* Subsection V(B)(6) of this Recommendation. *See also* White Paper 5 for more discussion on this subject.

qualify for the following "safety net." The "safety net" would never allow the study area to receive more with the safety net than the study area's HCL fund support (i.e., the study area expense adjustment) would have been if the indexed cap had not taken effect for the year. The "safety net" computation would be as follows:

i) The "safety net additive" will be calculated for each study area where the growth in telecommunications plant in service (TPIS) per line is 14 percent[52] greater than the study area TPIS per line in the prior year.

ii) The "safety net additive" will be equal to 50 percent of the difference between the capped "expense adjustment" for the study area and the uncapped amount for the study area.

iii) The "safety net additive" will be paid in addition to the "expense adjustment" calculated for the study area.

iv) "Safety net additives" for all eligible study areas will be paid over and above the indexed HCL fund cap amount.

v) Any study area that qualifies for the "safety net additive" will also qualify for a "safety net additive" in each of the four succeeding years regardless of whether it meets the 14 percent criterion in those years.

2. Corporate Operations Expense Limitation

The corporate operations expense limitation imposed in the FCC's rules limits the amount of the corporate operations expense that is assigned to the HCL fund "expense adjustment" calculation for certain study areas.[53] The Task Force proposes modifying the existing formula by re-basing and indexing the dollar values in the "expense adjustment" calculation and by adding an alternative calculation for determining the maximum amount of corporate operations expense assigned to the "expense adjustment" calculation.

a. The corporate operations expenses assigned to the HCL fund calculation for each study area would be the lower of the actual corporate operations expenses for the study period or the calculated amount of corporate operations expenses under Subsection IV(B)(2)(b) below.

b. The calculated amount of corporate operations expense would be the higher of the amounts calculated under Subsections IV(B)(2)(b)(i) or IV(B)(2)(b)(ii) below.

i) The corporate operations expense assignment to the HCL fund calculation under this alternative would be based on modifying the existing Section 36.621(a)(4) formula.[54]

---

[52] The 14 percent factor was chosen as an estimate of twice the average RGF in recent years.

[53] Based on information provided by NECA, 205 rural study areas were affected in 2000 based on 1998 data. The number of Rural Carriers impacted by this limitation has increased by 15 percent in the two years since this limitation was imposed.

[54] Part 36.621(a)(4) states: "Total Corporate Operations Expense, for purposes of calculating universal service support payments beginning January 1, 1998, shall be limited to the lesser of: (i) the actual average monthly per-

(continued….)

A) The dollar values in this formula would be grown annually by the RGF to reflect increased costs since the formula was put into place due to increased work requirements, labor, and other costs.[55]

B) Upon implementation of this Recommendation the dollar values in this formula would be grown by the RGF for each year since the formula was adopted. In each subsequent year the dollar values would be grown by the RGF for the subsequent year.

ii) The corporate operations expense assignment to the HCL fund calculation under this alternative would be based on the following calculation:

A) The year 2000 uncapped corporate operations expense per line (i.e., using 1998 data) will be calculated for each study area. The corporate operations expense per line will be multiplied by the number of lines to yield the corporate operations expense.

B) For 2001 and each subsequent year, the study area corporate operations expense amount per line will be grown by multiplying the previous year's amount per line times one plus the RGF. The corporate operations expense amount per line will be multiplied by loops at the end of the study period to arrive at the calculated corporate operations expense.

The purpose for the additional alternative proposed is to provide an option other than the waiver process for companies which have corporate operations expenses above the Section 36.621(a)(4) limitation. Some companies consistently have corporate expenses which are higher than this formula would allow. While the waiver process is an option to obtain relief, it is very expensive for a small Rural Carrier like Interior Telephone in Alaska, and has yielded petitioners only a one-year waiver.[56]

The Task Force acknowledges that the waiver process can be economically infeasible for some rural carriers. Therefore, in order to provide a cost-efficient alternative to the waiver

(Continued from previous page)

line Corporate Operations Expense; or (ii) a per-line amount computed according to paragraphs (a)(4)(ii)(A), (a)(4)(ii)(B), and (a)(4)(ii)(C) of this section. To the extent that some carriers' corporate operations expenses are disallowed pursuant to these limitations, the national average unseparated cost per loop shall be adjusted accordingly. (A) For study areas with 6,000 or fewer working loops the amount per working loop shall be $31.188 - (.0023 x the number of working loops), or, $25,000 divided by the number of working loops, whichever is greater; (B) For study areas with more than 6,000 but fewer than 18,006 working loops, the amount per working loop shall be 3.588 + (82,827.60 divided by the number of working loops); and (C) for study areas with 18,006 or more working loops, the amount per working loop shall be $8.188."

[55] An analysis of this alternative indicates that if the FCC included a modest annual growth of five percent in the dollar amounts associated with this alternative, the number of Rural Carriers experiencing a limitation on their corporate operations expenses would have actually declined rather than growing by 15 percent over the past two years, and the shortfall amount would have been $15.1 million less than 1/2 of its current level ($34.6 million based on data provided by NECA at the request of the Task Force).

[56] For example, the FCC granted Artic Slope Telephone Association Cooperative, Inc. a limited one-year waiver of the corporate operation expense recognizing that costs incurred to provide telephone service in Alaska are higher than in the lower 48 states and that it was in the public interest of maintaining affordable rates. Order DA 98-2586 (rel. Dec. 22, 1998).

process the Task Force has proposed the alternative calculation described above.

3. Merger and Acquisition Cap

Section 54.305 of the FCC's rules state "A carrier that acquires telephone exchanges from an unaffiliated carrier shall receive universal service support for the acquired exchanges at the same per-line support levels for which those exchanges were eligible prior to the transfer of the exchanges." The Task Force has concerns that in many cases, this Section limits the ability and motivation of the acquiring entity to make new investments to upgrade the networks in these acquired properties in spite of their high cost and rural nature. The Task Force agreed that the following principles should be applied in considering universal service support for acquired or transferred exchanges:

a. Customers in high cost rural exchanges involved in sale/transfer transactions should not be "doomed" to poor service because they live in exchanges that have been involved in sale/transfer transactions where the previous owner had limited access to universal service support funds.

b. A mere transfer of ownership should not result in an increase in support associated with the acquired lines. At the same time, universal service support should provide incentives for new investment in rural America.

c. The universal service support system should not artificially inflate the price on sale/transfer transactions.

d. Where meaningful new investments are made a universal service support "safety valve" mechanism should provide some support to high cost rural exchanges involved in sale/transfer transactions. Any additional universal service support should be driven by post-transaction investments made to enhance the infrastructure of and improve the service in these exchanges.

e. Any transferred universal service support under current rules or additional support under this "safety valve mechanism" is over and above the indexed HCL fund cap.

f. The "safety valve mechanism" should be capped at some appropriate level.

The Task Force recommends that the FCC establish an appropriate "safety valve mechanism" for Rural Carriers which acquire access lines due to sale or merger. Under this mechanism Rural Carriers would receive, over a period of five years, support for new investments that enhance the infrastructure in rural exchanges. An illustration of the specifics of a "safety valve" mechanism is attached as Appendix D.

C. Principles for Preserving any Current Universal Service Support Which May be Implicit Within Interstate Access Charges – The Underlying Basis for High Cost Fund III (HCF III)

The Task Force recognizes that interstate access may also include high cost universal service support in the form of implicit support. The Task Force accordingly identified the potential need for an additional universal support fund, High Cost Fund III, to replace support implicit within current interstate access charges collected by Rural Carriers.

High Cost Fund III is needed, in part, to respond to a disparity of access rates between Rural Carriers and non-Rural Carriers. Disparity of access rates between Rural Carriers and non-Rural Carriers results from at least two different phenomena: cost differences between these companies and differences in implicit support inherent in their current access rates.

Cost differences in the provision of service between Rural Carriers and non-Rural Carriers result from a host of factors including customer density, distance, average switch size, average trunk usage, and company size as shown in Task Force White Paper 2. These cost differences are real and discernable under whatever cost measurement is employed.

Rate disparity between the Rural Carriers and non-Rural Carriers related to the current level of implicit support inherent in access rates arise from a number of prior public policy decisions. Key among these decisions are policies to average rates across broad areas (the study area) and to recover basically fixed costs of operations through usage-sensitive rates, and costs which may be considerably higher in areas served by Rural Carriers because of the higher cost of operations in those areas. The implicit support that comes from the broad averaging of costs across high cost and low cost areas or the above-cost pricing of certain market segments may be incompatible with a competitive environment.

The continuing development of interstate toll competition and the access reform policies implemented for price-cap companies have the potential to increase the rate disparity between interstate access rates of price-cap (primarily non-Rural Carrier) and rate-of-return (primarily Rural Carrier) local exchange companies. These disparities potentially can cause significant pressures on interexchange carriers to geographically deaverage toll rates. In light of the conflict between these pressures and the requirements of Section 254(g) to maintain geographically averaged toll rates, some industry participants propose expansion of the role of the federal universal service fund to address some of the concerns related to interstate access rate differentials between large and small local exchange carriers.

The Task Force discussed the issue of implicit support in access rates in relationship to its role to provide recommendations regarding the federal universal service fund for Rural Carriers. The Task Force recommends the following principles:

1. Current interstate access charges of Rural Carriers may contain some amount of implicit interstate universal service support, although there is no agreement on how much or how to determine the amount of implicit support.

2. When the FCC addresses interstate access charges for Rural Carriers, it should identify the appropriate unit prices of interstate access. The Task Force is not recommending any particular method for arriving at appropriate interstate access prices.

3. The difference between current interstate access revenues and the repriced interstate revenues should be replaced by an un-capped High Cost Fund III. These payments from High Cost Fund III should be distributed on a per line basis.

4. HCF III should be funded by equitable and nondiscriminatory assessments on all interstate telecommunications carriers.

5. HCF III support may be geographically deaveraged by cost zone and targeted to high cost areas served by Rural Carriers.

6. HCF III support should be portable and should be available to all eligible telecommunications carriers on an equitable, non-discriminatory, and competitively neutral basis.

7. Once determined, HCF III should be adjusted annually, based on the annual interstate access filings of the Rural Carriers that are rate-of-return regulated. These annual adjustments to HCF III would continue until these carriers are no longer rate-of-return regulated, save for any low-end-type adjustment.[57] Rate-of-return carriers that shift to incentive regulation should have a comparable hold harmless adjustment, but the Task Force takes no position at this time on the nature of that mechanism.

8. Compliance should be economically and administratively workable.

9. Consumers should receive benefits from HCF III in the form of lower rates and/or greater choice.

D. Accountability

During the Task Force's review, NECA presented information regarding the existing system of checks and balances applicable to rural carriers.[58] Currently NECA collects unseparated cost data from prospective high cost support recipients on an annual basis, and reviews the data for reasonableness. NECA then recommends the level of support to the Universal Service Administrative Company (USAC), and ultimately to the FCC.

For the past several years, NECA has utilized a mechanized data collection process that allows ILECs or their authorized consultants to enter and review data for consistency. This system uses an extensive set of edit and range controls to check data for reasonableness by automatically comparing new data to prior year data. Each system user is alerted to significant variations through automated reporting that identifies unusual data and requires explanations, which NECA reviews for compliance purposes. Where necessary, additional supporting material is obtained from the carrier.

ILECs submit data to NECA on or before July 31st each year. The ILECs include with their data submission signed letters of certification attesting to the accuracy of their data.[59]

---

[57] *See* 47 CFR 61.45(d)(1)(viii).

[58] *See* NECA, Presentation before the Task Force, July 20-21, 2000, Seattle, Washington, available at www.wutc.wa.gov/rtf.

[59] Section 69.601 of the Commission's rules, 47 C.F.R. 69.601, requires that all data submissions made to NECA must be accompanied by a certification statement signed by the officer or employee responsible for overall (continued….)

NECA reviews this data for accuracy and conformance with FCC rules. As part of its data integrity review process, NECA reconciles the data to financial records underlying the ILECs' cost studies. Prior to the submission of the data, NECA performs a reconciliation of the largest ILECs' data to audited company financials. When errors are detected, corrections are made to the data and expense adjustments are then recomputed.

NECA requires ILECs to provide explanations or corroborating information to substantiate questionable data and or significant increases/decreases from the prior year amounts. NECA staff reviews ILEC responses for reasonableness and where necessary contacts the ILEC to correct discrepancies. In addition to the internal review performed by NECA, each year a group of industry experts review the results of the annual submission prior to its being filed with the FCC and USAC.

If there is a disagreement between the applying carrier and NECA concerning a data submission, there is an attempt to settle the conflict at that level. If this fails, the FCC is brought in to settle the dispute. Concurrently, state commissions (intrastate) and the FCC (interstate) have the legal jurisdiction to directly determine the regulatory reasonableness of expenditures for many of the participating carriers.

Based on its limited review of existing procedures, the Task Force believes that the process currently used by NECA, USAC, the FCC, and state commissions reasonably promotes accountability. Such assurances are, of course, critical. Failure to achieve accountability could result in excessive costs and unjustified benefits, leading to an artificially large fund. Coupled with the Task Force's reasoned recommendations concerning the cap on funding, these accountability measures should assure regulators that the new support system will operate in the public interest.

The Task Force reiterates that, under Section 254(e), a carrier receiving such support shall use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. The Task Force recommends that states be delegated responsibility for oversight of this section in a manner similar to that used for the non-rural LECs (i.e., annual certifications).[60]

Consumers are and should be the ultimate beneficiary of the 1996 Act. Section 254 (b)(1) requires "just, reasonable, and affordable rates" and 254(b)(3) requires "reasonably comparable" rates and services in all regions of the nation. In White Paper 2, the Task Force observed that prior to the enactment of the 1996 Act, that on average the combined monthly bills for local and long distance service for customers of Rural Carriers and non-Rural Carriers were within pennies of each other. The Task Force also noted in that paper that telephone penetration rates were 94.9 percent for non-Rural Carriers and 92.5 percent for Rural Carriers.

(Continued from previous page)
preparation of the data submission. *See* 47 C.F.R. 69.601 (c) and Safeguards to Improve the Administration of the Interstate Access Tariff and Revenue Distribution Processes, CC Docket No. 93-6, RM 7736, and Consideration of NECA's Incentive Compensation Plan, AAD 95-34, Report and Order and Order to Show Cause, 10 FCC Rcd 6243, 6264 (1995). NECA has required certification for all universal service fund data reports since 1990.

[60] *See* Non-Rural Order at Paragraph 93. *See also* 47 CFR, Part 54.3.

As competitive and universal service reforms are implemented, the Task Force urges state and federal policy makers carefully monitor the affordability of rates and the ubiquity of the modern telecommunications services to ensure that the benefits of the law are realized.

V. REFORMS TO ACHIEVE COMPETITIVE PROVISIONS OF THE 1996 ACT

The Task Force recognizes the current method of Rural Carrier support must also be modified to be consistent with the competitive provisions of the 1996 Act and the principle of competitive neutrality. To this end the Task Force recommends that support be disaggregated, and that transparent, portable per line support be established for each Rural Carrier. Below are specific recommended modifications to the current mechanism.

A. Disaggregation and Targeting of Support

In White Paper 6 "Disaggregation and Targeting of Universal Service Support," the Task Force discussed the need and options for targeting universal service support. It does not appear that an adequate "one size fits all" approach is workable for disaggregation. As set forth in White Paper 2, Rural Carriers are not only different from non-Rural Carriers but the population of Rural Carriers contains disparate characteristics and operating environments. The need to target funds and the method used for disaggregation also needs to meet the unique regulatory and competitive environments in each state. Notably, states have the authority to designate ETC status,[61] suggest changes in service areas for ETC status to a Joint-Board and the FCC,[62] and establish many of the other rules and parameters for local competition.[63] Additionally, some states have already acted on a variety of ETC and disaggregation issues, and the Task Force does not wish to disrupt any tailored situations that are already in place.

The Task Force recommends a system that allows for adequate flexibility to take into account the unique needs of companies with widely varying geographic cost characteristics and the competitive and regulatory environment in each state. The Task Force also recognizes the need for safeguards to prevent gaming the system.

The Task Force recommends that the mechanics of the disaggregation system be based on the following general requirements.

1) The ILEC's study area support available in total for a study area from the disaggregated method(s) would equal the total support available without disaggregation.

2) The relative per line support relationships[64] between disaggregation zones for each disaggregated category of support would remain fixed over time (except as changes are allowed by the Path descriptions). These relationships would be publicly available as described in Section V (B)(2).

[61] *See* 47 U.S.C. 214(e)(2).

[62] *See* 47 U.S.C. 214(e)(5).

[63] *See* e.g. 47 U.S.C. 251(f) and 47 U.S.C. 252.

[64] These relationships may be most easily understood by expressing them in support per line per month format.

3) Until a CETC is certified in a study area, monthly payments to ILECs will be made using current procedures based on total annual amounts for a study area divided by 12.

4) When a CETC is certified for a study area, per line amounts to determine the CETC's disaggregated support would be based on the ILEC's then current total support levels, lines, and disaggregated support relationships.

   a) Support per line for each category of support for each disaggregation zone would be determined such that the relative support relationships between zones would be maintained and that the product of all of the ILEC's lines for each cost zone times the per line support for those zones would sum to the total ILEC support.

   b) Per line support amounts for each zone would be recalculated whenever the ILEC's total annual support amount changed using the changed support amounts and lines at that point in time.

The Task Force recommends establishing a targeting system that allows Rural Carriers to use different paths based on the circumstances and needs encountered by each carrier. The Task Force recommends all of the following individual paths be established to meet these goals:

Path 1: For Rural Carriers that do <u>not</u> want to target high cost support

A) Within 270 days from the effective date of the final rules, Rural Carrier certifies to the state commission, or other appropriate regulatory authority, that it does not want to disaggregate high cost support.[65]

B) The plan becomes effective upon filing with certification.

C) Certification lasts for at least four years[66] from the effective date, unless during that time the state commission or other appropriate regulatory authority requires, on its own motion or upon petition by an interested party, the disaggregation of support, grants ETC status below the study area level, state or federal laws or regulations change, or if a change in ownership occurs. At that time, the Rural Carrier may target support through the use of either Path 2 or Path 3.

Path 2: For Rural Carriers that want review and approval for targeting high cost support

A) Within 270 days from the effective date of the final rules, the Rural Carrier files a disaggregation plan with the state commission or other appropriate regulatory authority.

[65] Throughout this discussion the Task Force recognizes that some state commissions may lack the authority to implement the Recommendation with regard to targeting of high cost support, in which case we assume the appropriate regulatory authority will govern.

[66] With the 270 day period prior to filing, plus the four year effective period, the total period elapsed is nearly the five years prescribed for these recommendations.

B) There are no constraints on Rural Carrier proposals under this path.

C) Regulatory authority holds workshops, hearings or other appropriate administrative proceeding in which interested parties may participate. Any such proceedings should be economically and administratively workable.

D) Regulatory authority issues an order on targeting support, including a description of the zones, and a per line amount of support for each element in each zone.

E) The plan is effective until the regulatory authority approves a new plan. The targeting plan is subject to change or challenge at any time.

Path 3: For Rural Carriers that want to self-certify a method for geographic disaggregation

A) Within 270 days from the effective date of the final rules, Rural Carrier files a disaggregation plan with the state commission or other appropriate regulatory authority along with a statement certifying each of the following:

1. Plan disaggregates support to the wire center level. Carriers may choose to further disaggregate support into no more than two cost zones per wire center. Alternatively, the plan may comply with a prior regulatory determination that a different level of disaggregation is appropriate.

2. If the appropriate regulatory authority has previously adopted a method of disaggregation, the plan uses the rationale previously adopted.

3. The plan uses a rationale that is reasonably related to the cost of providing service for each cost zone within each disaggregated category (HCL, LSS, LTS).

4. If the plan uses a benchmark, it must be generally consistent with how the total study area level of support for each category of costs (HCL, LSS, LTS) is derived, to compare the disaggregated costs for determining support for each cost zone.

4. The filing must provide a description of the rationale used, including the methods and data, and a discussion of how the plan complies with the self-certification guidelines. The filing need not contain a complete cost study. If the plan uses a benchmark, the filing must explain what the benchmark is and how it was determined. The plan must show a per line amount of support for each element in each zone.

B) The plan becomes effective upon self-certified filing.

C) Self-certification lasts for at least four years from the effective date, unless during that time the regulatory authority requires, on its own motion or upon petition by an interested party, the disaggregation of support, grants ETC status below the study area level, state or federal laws or regulations change, or if a change in ownership occurs.

D) At any time while in effect, the plan is subject to complaint by interested parties before regulatory authority on the grounds that it does not comply with the requirements above. The relevant regulatory administrative procedures (including burden of proof allocation and availability of discovery) will apply to such complaints.

The Task Force recognizes that the state commission has authority to determine whether more than one ETC should be designated in an area served by a Rural Carrier and that the responsibility and process for changing the ETC designation area to a geographic area other than a Rural Carrier's study area are as set forth in Section 214(e)(5) and the FCC's rules. However, the Task Force recommends that the level of disaggregation of support be considered in determining whether to certify new ETCs for a service area other than a full Rural Carrier ETC study area.

B. Portability Implementation

The Task Force's principles stated that any support mechanisms recommended should be consistent with extending the benefits of a competitive telecommunications market to rural or insular areas, and should be competitively neutral. The previous section discussed the need to disaggregate support and target that support to high-cost areas. In this section, the Task Force addresses issues which must be resolved in order to determine available per line support and to make that support available to all ETCs in a transparent and competitively neutral manner.

1. Per Line Support

The Task Force has recommended that universal service support for Rural Carriers continue to be based on the embedded costs of the incumbent carrier. The Task Force has also recommended that support be disaggregated and targeted to high cost areas. Because per line support will be based on embedded costs, because these costs will change each year, and because the number of customers in each area will change, the per line support available for each area will also change.[67]

The Task Force has recommended that per line support available to an incumbent Rural Carrier continue to change based on changes in costs. The Task Force has also recommended that once an additional ETC is designated and begins providing service in a Rural Carrier's study area, that per line support for both the ILEC and the CETC be frozen and grown by the annual RGF. The procedures for determining per line support for all carriers are set forth in Section IV(B)(1)(c) above. The Task Force believes that its recommended approach will continue to provide appropriate incentives for investment in rural America, while at the same time providing fair and reasonable procedures to facilitate competitive entry.

2. Transparency of Universal Service Support

As discussed above, the Task Force recommends that federal universal service support per study area continue to be based on embedded costs, but be disaggregated. Because embedded

---

[67] In this respect the method of support recommended by the Task Force differs from the mechanism adopted by the FCC for non-Rural Carriers. Under the non-rural mechanism per line support for each area is established by the Synthesis Model. The amount of per line support available does not change until the model is run again, presumably some years hence.

support will change from year to year, it is very important that per line support for each area of each company, and the basis of disaggregation for each company, be readily available so that potential competitors may make reasonable decisions about whether to enter an area served by a Rural Carrier. Once a CETC is providing the supported services in an area served by a Rural Carrier, the CETC would receive the same per-line support as received by an incumbent Rural Carrier in the disaggregated area.

The amount of explicit universal service support that the ILEC receives[68] should be available for review, as is currently done today, via the FCC's web site.[69] Public information of the per-line universal service support would allow competitors to obtain information necessary for business planning purposes. The Task Force recommends that this transparency of support continue. Since the support would be disaggregated, the public information would need to contain information on the basis of the relative distribution of the ILEC's per-line support.

3. Frequency of Reporting and Lag in Support

The entry of a competitive carrier into a Rural Carrier's service area means the number of lines served by the ILEC and the CETC within that area may change in a dynamic manner. Issues concerning the frequency and method of line count reporting were raised by several parties. Since the competitive inroad of the CETC usually begins with a slow ramp-up as customers are signed on for service, customer additions are likely to occur at anytime. Similarly, to the extent customers are replacing an ILEC service with a CETC service, the ILEC's line count can decline precipitously throughout the same period. The Task Force discusses frequency of line count reporting in White Paper 5 "Competition and Universal Service."

The Task Force recommends that the interval between the provision of service and receipt of universal service funding (known as the "lag") should be as short as technically and administratively feasible to ensure provision of universal service. In addition, the line count submissions to the federal universal service fund administrator must be sufficiently sensitive to mid-period competitive activity. Thus, continuing support for the ILEC for a whole period when it is not serving the customer for the whole period, coupled with the failure to compensate the CETC for the portion of the period that it is providing service may constitute a barrier to entry for the CETC. The Task Force recommends using the average of the quarter (i.e., beginning of quarter plus end of quarter divided by two) data.

4. Identification of Service Locations

If a carrier using wireless mobile technologies is designated as an ETC in an area served by a Rural Carrier, an issue arises regarding the location of the customer. The local service areas and network configurations for wireless mobile services may be significantly different than for wireline services. Since support may be disaggregated below the study area or wire center level and must be used in accordance with Section 254(e), the issue arises of how to relate a wireless mobile (i.e., non-fixed location) customer to the proper ILEC wire center, and to the appropriate sub-zone in the wire center, if any.

---

[68] Explicit universal service support would include any explicit support as discussed in HCF III.

[69] *See* www.fcc.gov/ccb/universal_service/quarter.html.

The Task Force recommends that the wireless carrier use the customer's residential or business location as the basis for determining in which disaggregation zone the customer resides for purposes of universal service support implementation. The Task Force recognizes that the use of any location address could allow arbitrage of the universal service support system. The Task Force recommends that the FCC establish a reasonable method for determining customer location for wireless customers. The FCC or other appropriate regulatory authority should retain authority to prevent misuse of wireless customer locations and assure that universal service support is used in accordance with Section 254(e).

5. Supported Lines

The Task Force recommends continuing provision of support to all lines in areas served by Rural Carriers, as opposed to supporting only primary lines. This is consistent with current universal service procedures.[70]

6. Stranded Costs

The previous sections above have discussed how to introduce competition into areas served by Rural Carriers. However, the introduction of competition raises the possibility of not only loss of customers by incumbent Rural Carriers, but also loss of historic universal service support. A Rural Carrier that experiences significant line losses to a competitor may face the problem of un-recovered investment, also known as "stranded costs." In White Paper 5 the Task Force discussed the "stranded cost" issue, which is an issue that is subject to a high degree of controversy and disagreement. The Task Force recommends that the FCC address the "stranded cost" issue.[71]

VI. RECOMMENDING CLAUSES

For the reasons discussed herein, this Rural Task Force, appointed by the Federal-State Joint Board on Universal Service, pursuant to Section 254(a)(1) and Section 410(c) of the Communications Act of 1934, as amended, 47 U.S.C. Sections 254(a)(1) and 410(c), recommends that the Federal-State Joint Board recommend to the Federal Communications Commission adoption of the proposals described above relating to federal high-cost universal service support mechanisms for Rural Carriers. The elements of this comprehensive package should be considered in concert with each other and implemented immediately.

Appendix A - Signatory Rural Task Force Members[72]

William R. Gillis, Commissioner
Washington Utilities and Transportation Commission

[70] *See* White Paper 5.

[71] *See* White Paper 5 for further discussion.

[72] Several appointees were not present or involved during the final months of meetings and conference calls of the Task Force. Because they did not take part in the final deliberations and because the Task Force had agreed early on that they must be present to vote, several appointees' names do not appear on the Recommendation signature page.

Chair-Rural Task Force
P. O. Box 47250
Olympia, WA 98504-7250

Robert C. Schoonmaker, Vice President
GVNW Consulting, Inc.
Secretary-Rural Task Force
2270 La Montana Way
Colorado Springs, CO 80918

Carol Ann Bischoff, Executive Vice President and General Counsel
Competitive Telecommunications Association
1900 "M" Street, NW, Suite 800
Washington, D.C. 20036-3508

David R. Conn, Associate General Counsel and
Vice President Product and Policy
McLeodUSA Incorporated
McLeodUSA Technology Park
6400 "C" Street SW
P. O. Box 3177
Cedar Rapids, IA 52406-3177

Gene DeJordy, Executive Director: Regulatory Affairs
Western Wireless Corp.
3650-131st Avenue, SE, Suite 400
Bellevue, WA 98006

Billy Jack Gregg, Director
West Virginia Consumer Advocate Division
723 Kanawha Blvd. East
700 Union Building
Charleston, WV 25301

Evelyn Jerden, Director - Revenue Requirements
Western New Mexico Telephone Company
4070 N. Circulo Manzanillo
Tucson, AZ 85750

Joel Lubin, Regulatory VP - Law and Public Policy
AT&T
1120 – 20th Street, N.W., Suite 1000
Washington, D.C. 20036

Joan Mandeville, Vice President Administration
Blackfoot Telephone Cooperative
1221 N. Russell Street
Missoula, MT 59802-1898

Christopher A. McLean, Administrator
Rural Utilities Service, USDA
1400 Independence Avenue SW
Mail stop: 1510
Washington, D.C. 20250

Jack Rhyner, President and CEO
Telalaska
201 East 56th Avenue
Anchorage, AK 99518

David Sharp, Senior Vice President
Innovative Communication Corp.
P. O. Box 7610
St. Thomas, VI 00801

Stephen G. Ward, Public Advocate
State of Maine Public Advocate Office
112 State House Station
193 State Street
Augusta, ME 04333-0112

APPENDIX B - MEETINGS AND CONFERENCE CALLS

The Task Force conducted its business through a series of face-to-face meetings and periodic conference calls. The minutes of these sessions may be found at www.wutc.wa.gov/rtf.
The meetings of the Task Force included:
July 29, 1998 in Seattle, Washington
September 23, 1998 in Washington, D.C.
December 10-11, 1998 in Washington, D.C.
March 4-5, 1999 in Tucson, Arizona
June 24-25, 1999 in Washington, D.C.
September 30-October 1, 1999 in Portland, Maine
January 13-14, 2000 in Washington, D.C.
March 23-24, 2000 in Washington, D.C.
May 25-26, 2000 in Anchorage, Alaska
July 20-21, 2000 in Seattle, Washington
August 24-25, 2000 in Denver, Colorado
September 20-22, 2000 in Washington, D.C.

The Task Force held conference calls on the following dates:
1998: August 25, November 17

> 1999: January 13, February 3, May 20, August 27, September 17, November 1, November 23, December 6, December 30
>
> 2000: February 29, May 18, June 12, June 19, July 11, August 4, August 7, August 14, August 21, August 31, September 5, September 7, September 11, September 13, September 25, September 26, September 27

In addition, sub-group calls were held on numerous occasions.

APPENDIX C - LIST OF RURAL TASK FORCE WHITE PAPERS

White Paper 1 "Rural Task Force Mission and Purpose"

White Paper 2 "The Rural Difference"

White Paper 3 "Alternative Mechanisms for Sizing A Universal Service Fund for Rural Telephone Companies"

White Paper 4 "A Review of the FCC's Non-Rural Universal Service Fund Method and the Synthesis Model for Rural Telephone Companies"

White Paper 5 "Competition and Universal Service"

White Paper 6 "Disaggregation and Targeting of Universal Service Support"

Note 1: White Paper 4 is released concurrently with the Recommendation to the Federal-State Joint Board on Universal Service.

Note 2: All other White Papers are available at www.wutc.wa.gov/rtf.

APPENDIX D - EXAMPLE OF THE "SAFETY VALVE" MECHANISM FOR THE MERGERS AND ACQUISITION CAP

1. An appropriate "safety valve" mechanism that would meet the Task Force principles for exchanges that are sold or transferred. The following example illustrates how the "safety valve" mechanism should work.
2. Sold/transferred exchanges acquired by an entity would be designated as a new study area within the state.
3. New study areas thus created that meet the definition of a "rural telephone company" (Rural Carrier) under the 1996 Act will be eligible for treatment under this mechanism.
4. Universal service support provided to these study areas served by Rural Carriers would not be included in the Rural Carrier indexed HCL fund cap.
5. Loops in these study areas would not be included in the calculation of the Rural Growth Factor.
6. Universal service support transferable to the study area under the provisions of Section 54.305 would be available to these study areas.
7. In addition to the universal service support available under Section 54.305, additional HCL support related to new investment in these study areas would be provided in accordance with the following calculations:
    a. At the end of the first year of operations a study area HCL "expense adjustment" using the existing rules would be calculated. This amount would become the "index year expense adjustment."
    b. At the end of each subsequent year a study area HCL "expense adjustment" using the existing rules would be calculated and would be compared to the "index year expense adjustment."
    c. Fifty percent of any positive difference between the subsequent year "expense adjustment" and the "index year expense adjustment" would be designated as the "sale/transfer safety valve expense adjustment" and would be provided as universal service support to the study area in addition to amounts available under Section 54.305.
8. The sum of the "sale/transfer safety valve expense adjustments" for all study areas eligible for the adjustment would not exceed 5 percent of the indexed HCL fund cap for Rural Carriers.
9. Per loop equivalent amounts of the "sale/transfer safety valve expense adjustment" would be

portable to a CETC operating within the study area.

APPENDIX B
PARTIES FILING INITIAL COMMENTS

Commenter	**Abbreviation**
Alaska, Regulatory Commission	RCA
Alaska, State of Rural Task Force	Alaska
AT&T Corp.	AT&T
Bristol Bay Telephone Cooperative, Inc.	Bristol
CenturyTel Service Group, Inc.	CenturyTel
Charter Communications, Inc.	Charter
Chugwater Telephone Company	Chugwater
Citizens Communications Company	Citizens
Direct Communications Rockland Telephone Co.	Rockland
Evans Telephone Company	
Happy Valley Telephone Co.	
Hornitos Telephone Co.	
Humboldt Telephone Co.	
Kerman Telephone Co.	
Oregon-Idaho Utilities, Inc.	
Pine Tree Telephone & Telegraph Co.	
Pinnacles Telephone Co.	
The Ponderosa Telephone Co.	
The Siskiyou Telephone Co.	
The Volcano Telephone Co.	
War Telephone Co.	
Winterhaven Telephone Co.	Evans
Fremont Telephone Company	Fremont
General Communication, Inc.	GCI
GVNW Consulting, Inc.	GVNW
Iowa Telecommunications Services, Inc.	Iowa Telecom
Ketchikan, City of	
d.b.a. Ketchikan Public Utilities	Ketchikan
Maine Public Utilities Commission	
Vermont Department of Public Service	
Vermont Public Service Board	Maine
Manti Telephone Company	Manti
Mike Stagg	Mike Stagg
Montana Telecommunications Association	MTA
Mt. Angel Telephone Company	Angel
National Association of State Utility	
Consumer Advocates	NASUCA
National Exchange Carrier Association, Inc.	NECA
National Telephone Cooperative Association	NTCA
Nebraska Rural Independent Companies	Nebraska
New York State Dept. of Public Service	
Connecticut Dept. of Public Utility Control	
Illinois Commerce Commission	
Maryland Public Service Commission	New York
North-State Telephone company	North-State

Oregon Exchange Carrier Association	OECA
Oregon Telecommunications Association	OTA
Oregon Telephone Corporation	OTC
People, State of California	
California Public Utilities Commission	People
Pioneer Telephone Cooperative	PTC
Qwest Corporation	Qwest
Roseville Telephone Company	Roseville
Rural Independent Competitive Alliance	RICA
Rural Utilities Service	RUS
Sprint Corporation	Sprint
South Dakota Independent Telephone Coalition, Inc.	SDITC
TDS Telecommunications Corporation	TDS Telecom
Tularosa Basin Telephone Company, Inc.	Tularosa
United States Telecom Association	
Organization for the Promotion & Advancement	
Of Small Telecommunications Companies	
National Rural Telecom Association	USTA
Valor Telecommunications Enterprises, LLC	Valor
Verizon	Verizon
Virgin Islands Telephone Corporation	Vitelco
Western Alliance	Western
Washington Independent Telephone Association	WITA
WorldCom, Inc.	WorldCom
Wyoming Public Service Commission	WPSC
YCOM Networks	YCOM

APPENDIX C
PARTIES FILING REPLY COMMENTS

Commenter	Abbreviation
Ad Hoc Telecommunications User Committee	Ad Hoc
Alaska Rural Coalition	Alaska Rural Coalition
Alaska, State of	Alaska or the State
AT&T Corp.	AT&T
Competitive Universal Service Coalition	CUSC
Florida Public Service Commission	Florida PSC
Gold West Telecommunications Coop., Inc and Vivian Telephone Company	Gold West and Vivian
GVNW Consulting, Inc.	GVNW
Hanson County Telephone Company	Hanson
Hawaii, State of	Hawaii
Interstate Telecommunications Cooperative, Inc.	Interstate
Kennebec Telephone Company	Kennebec
Maine, State of	Maine
McCook Cooperative Telephone Company	McKook
Nebraska Rural Independent Companies	Nebraska (Companies)
National Telephone Cooperative Association	NTCA
Sanborn Telephone Cooperative	Sanborn
Sancom, Incorporated	Sancom
SBC Communications, Inc.	SBC
Sioux Valley Telephone Company	Sioux
Small Rural LECs Evans Telephone Company Happy Valley Telephone Company Hornitos Telephone Company Humboldt Telephone Company Kerman Telephone Company Oregon-Idaho Utilities, Inc. Pine Tree Telephone & Telegraph Company Pinnacles Telephone Company The Ponderosa Telephone Company The Siskiyou Telephone Company The Volcano Telephone Company War Telephone Company Winterhaven Telephone Company	Small Rural LECs
Sprint Corporation	Sprint
Stockholm Strandburg Telephone Company	Stockholm-Strandburg
Sully Buttes Telephone Cooperative, Inc.	Sully Buttes
United States Telecom Association Organization for the Promotion & Advancement of Small Telecommunications Companies National Rural Telecom Association	Associations
United States Virgin Islands, Public Service Commission	US Virgin Islands
Valley Telecommunications Cooperative Assn., Inc.	Valley
Virgin Islands Telephone Corporation	Virgin Islands

Warinner, Gesinger & Associates	WGA
West Virginia Public Service Commission	West Virginia
Western Telephone Company	Western
Wyoming Public Service Commission	WPSC

SEPARATE STATEMENT OF JOINT BOARD CHAIRMAN SUSAN NESS

Re: Federal-State Joint Board on Universal Service, Recommended Decision, CC Docket No. 96-45

A core principle of the Telecommunications Act of 1996 is that all Americans should have access to reasonably comparable services at reasonably comparable rates. When the Joint Board and the FCC undertook a thorough review of the high-cost universal service mechanism following passage of the 1996 Act, we recognized the unique circumstances of rural carriers and did not adopt a "one-size-fits-all" solution. Rather, we worked with the rural carriers and their associations to convene a Rural Task Force that brought together a diverse range of companies, consumer advocates, and government representatives to examine the cost structures and competitive circumstances of rural carriers.

After two years of intensive deliberations, the Rural Task Force unanimously recommended a high-cost mechanism for rural carriers that recognizes not only the significant differences *between* rural and non-rural carriers, but also the vastly different cost structures *among* rural carriers. As is the case with any consensus proposal, the framework may not be exactly what any one entity would want. Nevertheless, the Task Force's framework represents a good compromise – a reasonable, but delicate balance -- among disparate interests that provides the certainty and stability essential for investment in rural America.

I commend the Rural Task Force for their unwavering efforts to develop a predictable and sufficient universal service mechanism for rural consumers. We owe them a debt of gratitude for their hard work. I especially want to thank the chair of the Task Force, Commissioner Bill Gillis of the Washington Utilities and Transportation Commission. He has worked with uncommon fortitude and patience to forge a consensus among warring factions.

For the past ten weeks, the Joint Board has had an opportunity to review the Report and to provide additional guidance to the FCC on the conclusions reached, including the targeting, magnitude, and duration of the support. Some commissioners would have preferred a vastly different regime or a more simplified one, some a significantly shorter timeframe, some a few points of fine-tuning to more precisely direct the funds toward the higher cost areas, while others would have expanded the scope of the review to include issues beyond the Rural Task Force report. In the end, in the interest of time, and with deep appreciation of the hard work of the Rural Task Force, the Joint Board agreed simply to forward the Report to the FCC without recommendations.

Now that the Rural Task Force has completed its work and the Joint Board has sent that recommendation to the Commission, I urge the Commission to move forward as rapidly as possible to bring this process to a successful conclusion. It is essential that we provide certainty to rural carriers by putting in place a high-cost mechanism that makes both economic sense and common sense. The stability offered by such a system will allow rural carriers to plan for the future and undertake necessary investment that benefits rural communities.

In this decision, a number of Joint Board members also request that the Commission refer to the Joint Board the interstate universal service aspects of an access charge reform plan recently submitted by rural carrier associations. I would prefer to proceed concurrently with universal service and access charge reform. The two go hand in glove. Although I agree that the Joint Board should be actively involved in issues that affect high-cost universal service mechanisms, I fear that a formal referral to the Joint Board could delay the process of implementing these reforms beyond the July 1, 2001 target date. Thus, any referral of these issues to the Joint Board should include concrete deadlines that would allow the Commission the ability to adopt appropriate access charge reform on the same timetable that it implements reform of the high-cost mechanism for rural carriers.

I look forward to continuing the dialogue with the Joint Board members as partners in this proceeding as we continue our efforts to fulfill the statutory requirement to preserve and advance universal service for the benefit of all Americans.

SEPARATE STATEMENT OF COMMISSIONER HAROLD FURCHTGOTT-ROTH

Re: Federal-State Joint Board on Universal Service, CC Docket No. 96-45 (rel. December 22, 2000)

I am pleased to endorse this Joint Board referral of the Rural Task Force report to the Federal Communications Commission. The inescapable meaning of the language of Section 254 of the Communications Act is that its primary purpose is the preservation and advancement of telecommunications services in rural America. This purpose has not been addressed by the Commission since the passage of the Telecommunications Act nearly five years ago, although the Commission has seen fit to spend billions of dollars of consumer fees for other purposes divined under Section 254.

Chairman William Gillis led the Rural Task Force in a mission designed to fail: from disparate and conflicting parties, form a consensus view on universal service for small rural telephone companies. Chairman Gillis believed the Rural Task Force could succeed; practically all outside observers believed no consensus could be reached. He was proved correct; others were proved wrong. The members of Rural Task Force have proven to have a greater sense of the public interest in reaching an agreement than others believed possible.

The Rural Task Force was and is the creation of the Joint Board on Universal Service. Where we sought their advice and when we waited two years to receive it, we must give it some substantial degree of respect. I cannot pretend to agree with every word in the recommendations; there is much that I would have written differently. Moreover, many parts of the recommendations lack detail. The FCC will have much work to fill in the details, but surely the FCC will have the Joint Board and the Rural Task Force to thank for an auspicious starting point.

Statement of Commissioner Gloria Tristani

Re: Federal State Joint Board on Universal Service Recommend Decision, Docket CC 96-45

I am pleased to support the recommendation of the Rural Task Force on the means to reform rural high-cost support for the next five years. The recommendation of the Rural Task Force reflects a tremendous effort to reform rural high-cost support in a reasonable manner that addresses multiple competing interests. I note in particular that concerns have been expressed about the length of time that the plan remains in place. One of the principal goals the Rural Task Force, however, was creating stability for investment in rural areas. I agree with the Rural Task Force that implementation for a period of five years is an important aspect of the recommendation and emphasize that the five-year period should not be shortened.

As noted in the recommended decision, several members of the Joint Board support recommending that the Commission refer the universal service aspects of the proposal for interstate access charge and universal service reform filed with the Commission by the Multi-Association Group (MAG) to the Joint Board. I agree that the MAG Plan raises significant questions of universal service policy, and that the input of the members of the Joint Board on this plan is invaluable. Nonetheless, I cannot support recommending a formal referral of the universal service aspects of the plan to the Joint Board. In light of the time limitations and resource constraints that the Commission faces, it is not practical. In particular, the Commission has a limited amount of time to implement the RTF proposal and consider whether the MAG plan is an appropriate access and universal service reform package. If acceptable, both matters before the Commission anticipate a July 1, 2001, implementation date.

Should the Commission decide not to refer the MAG Plan to the Joint Board, the lack of a formal referral should not prevent the Joint Board from participation in the process. I strongly encourage the Commission to ensure that the Joint Board remains actively involved in the Commission's consideration of the universal service aspects of the MAG Plan.

Concurring Statement
of
Commissioner Laska Schoenfelder
with Recommendation for Further Study
and Concurrence with
Commissioner Rowe's Statement

Docket CC 96-45

The Rural Task Force Recommendation (Recommendation) is remarkable when one considers multiple industry interests and regulators gathered to debate issues and policy with service requirements, subsidies, high and low cost states, rural protection and competition issues in play. The Recommendation represents substantial progress toward melding disparate interests inherent in the crafting of national telecommunications policy. The Recommendation of the Rural Task Force should be adopted in its entirety, and it should remain in effect for a minimum of five years.

Even so, with the future benefit of hindsight and further study, there will be acknowledged mistakes and the need for policy change. There are current unknowns that beg for data collection and study. My particular concern is the Recommendation's intent to provide universal service funding support for per customer multiple lines that may be conjunctively provided by ILEC, CLEC, and wireless companies. It's troubling that we may be providing the framework to massively inflate high cost support programs, potentially tripling them, without advancing universal service. I fully understand the need to resolve administrative problems before we can fully address this issue.

We know there are customers who now have multiple wireline and wireless options offered by eligible telecommunications carriers. I expect the scale of this issue to grow. There is an obvious need to intensify our examination of this issue in upcoming reviews. This issue should now be marked for tracking and measurement. We need to focus on the possibility of requiring multi-line customers to designate one line for receipt of universal service support. Commissioner Rowe is also filing additional comments addressing universal service issues which should be examined in the near future, and I support his statement.

The Multi-Association Group Plan (MAG Plan) which has been filed before the FCC is a comprehensive rural carrier reform plan which includes specific universal service recommendations. Those elements of the MAG Plan related to universal service should formally be referred to the Joint Board.

Statement of
Public Counsel Martha Hogerty
Concurring in part and Dissenting in part

I appreciate the tremendous effort of Commissioner Bill Gillis and the other members of the Rural Task Force in investigating and developing a joint recommendation regarding rural universal service issues. Their thorough and tireless research has significantly advanced our understanding of rural telecommunications issues.

I recognize that the Rural Task Force Recommendation is a compromise presented as an integrated package by a broad range of interested parties. The Joint Board Members examined all facets of the Recommendation and during discussions addressed questions about the wisdom of various components. Ultimately I agree that the proposal should be adopted for a five year period. I support the Recommendation primarily because the plan provides stability and predictability for a period of five years. This provides carriers with a reasonable planning horizon and provides investment incentives for rural carriers.

But I believe that the work initiated by the Rural Task Force is incomplete. The Rural Task Force Recommendation puts forth mechanisms that ensure that in the aggregate rural companies can provide the supported services. However, it falls short of ensuring that the support provided on a company basis is properly targeted. I believe that first obligation of the members of the Joint Board is accountability to the consumers that pay for the universal service fund. An inflated fund size or questionable allocation of funding threatens universal service.

This Joint Board has the responsibility to the public to properly target the universal fund. USAC collected $4 billion for the universal service fund in the year 2000. The proposed USF assessment on carriers for the first quarter of 2001 is 6.68%. The RTF will add another 1.6 billion to the fund. My fellow Joint Board members and I are certainly aware that customers continue to object to increasing federal and state surcharges on their bills. We owe it to them to carefully monitor the fund. My fear is that the universal fund may not be sustainable.

Looming before us is the MAG plan. This proposal has significant universal service implications. First, it could raise customer rates by increasing and deaveraging the SLC, and this has implications for rate comparability under Section 254(b)(3) of the Act and also for telephone penetration. Second, it will increase the size of the Universal Service Fund and the rate charged against the interstate revenues of contributing carriers. Section 254(b) and 254(c) both contemplate that the Joint Board makes recommendations in matters related to universal service. Accordingly, the Commission should refer to this Joint Board the universal service issues raised by the MAG plan, just as it should refer any other proposed federal action that would increase the price of universal service or increase the size of the Universal Service Fund. I strongly oppose any decision by the FCC to proceed with consideration of the MAG without a Joint Board recommendation and I am compelled dissent to the portion of the Joint Board Recommendation insofar as it fails to recommend referral of the MAG plan to the Joint Board.

Although I am able to accept the result for a limited period of time, I am disappointed that a more concentrated effort to target support was not achieved. I believe we can do better. It is my hope that the referral that commences in 2002 will result in a mechanism that provides sufficient support, to ensure just reasonable and affordable service to high cost areas, no more and no less.

Support should be targeted narrowly to those specific geographic areas that have a demonstrated need for the support. The need would be demonstrated where unacceptably high costs prevent the provision of affordable universal service absent support.

During the term of this plan, work must begin immediately to target support where it is needed. There was testimony offered by Commissioner Dunleavy of New York that some rural carriers receive support where the necessity is not clearly demonstrated. There was also testimony presented by Commissioner Welch of Maine that some areas of the country may not have sufficient support because of extraordinary high costs, not only for loop, but also switching, transport and general service facilities. Commissioner Rowe has expressed his concern that unserved areas exist that are in need of support. These concerns must be addressed and solved. I would support Commissioner's Rowe's recommendation to open a docket to investigate areas where no service is available. We must develop funding concepts that involve cost analysis and support that is more closely grounded to the existing network and real costs of providing universal service.

Although I agree with the Rural Task Force Recommendation that additional support in the form of a "safety net additive" should be available to rural carriers that make significant investment in rural infrastructure. I am concerned that the safety net support, combined with high cost loop support, switching support and interstate support, could in some cases produce more than 100% reimbursement on incremental loop investment. I strongly support the Joint Board's Recommendation to further investigate this problem. I believe that the Commission should craft rules to ensure that safety net benefits do not produce more than full recovery of the revenue requirement caused by additional carrier investment under any circumstances.

The Rural Task Force's proposal for re-basing the high-cost loop support fund includes a $14.6 million increase to reflect the removal of the Commission's corporate operations expense limitation. While I agree with the Rural Task Force's concern that a number of rural carriers impacted by the corporate operations expense limitation, I am most concerned about its impact on smaller carriers. The corporate operations expense limitation was adopted, in part, to prevent carriers from recovering from the high-cost loop support mechanism excessive expenditures unrelated to the provision of supported services. For larger companies, I believe this is a reasonable restriction. I believe the lifting of the corporate expense would have been better targeted to very small companies.

I urge the Commission to establish an annual certification requirement for state commissions that receive federal universal service support for rural carriers serving within their territories. Such a requirement will ensure that receipt of the federal support is appropriate and being used in a manner consistent with section 254. The Commission should apply this certification requirement to all forms of federal universal service support received by rural carriers, including "safety net additive," "safety valve," and "catastrophic" support.

I share Commissioner Schoenfelder's concern that providing universal service support for multiple lines to a single customer may substantially increase the size of high cost support programs without significantly advancing universal service. We recognize that there are formidable administrative problems that must be solved before this problem can be addressed fully, but nonetheless it must be addressed. Customers in some areas today have options for second or third lines that include not only wireline service but also one or more wireless telephones offered by eligible telecommunications carriers. I believe we must look further into this issue in the upcoming reviews, and will be particularly interested in examining the feasibility of requiring multi-line customers to designate a single line to receive universal service support.

In conclusion, I accept the Rural Task Force Recommendation because it will address the needs of rural consumers, however, I recognize that we will delay implementation of further refinements to target the fund for the period this plan is in effect. My hope is that the 2002 review process leads to meaningful results. While I accept the Rural Task Force Recommendation, I strongly dissent to the extent the Recommendation fails to refer the MAG plan to the Joint Board.

STATEMENT OF COMMISSIONER BOB ROWE

Re: Federal-State Joint Board on Universal Service, CC Docket No. 96-45

The Rural Task Force recommendation should be promptly implemented, fully implemented, and implemented for the full five-year period recommended. In addition, within the next six months a proceeding should be commenced concerning the very highest cost unserved and underserved areas, as more fully described below.

Perhaps nowhere in America is telecommunications more valuable than in rural areas. Modern telecommunications can help overcome distance and dispersion, and (as an intermediate good) allow rural citizens to maximize the advantages provided by other rural attributes. Perhaps nowhere are the challenges to deployment more daunting than in rural America. This was persuasively demonstrated in the Rural Task Force's second report, The Rural Difference.

Many telecom providers, especially small providers, do a great job providing rural citizens high quality service and, increasingly, access to more advanced services. Despite the acute "rural difference" exciting things are happening in rural America. Small carriers are investing in fiber backbone, installing ATM switching, and are beginning to deploy high-speed loop. Competition is also beginning to grow in some rural areas, provided by regional and national companies, and (too-often unnoticed) by small local competitors or competitive affiliates of rural companies. All of this is to the great credit of the providers and to the communities they serve. It is also a confirmation of Congress' wisdom in embracing both competition and universal service.[1] Public policy should support and not impede private innovation and investment.

A. The Rural Task Force Presented a Balanced Recommendation That Should be Adopted.

Our challenge, squarely addressed by the Rural Task Force, is first to "do no harm," second to effectuate Congress' specific universal service objectives in Section 254, and third to do so in a way consistent with Congress' companion emphasis on competition. The Rural Task Force has done an admirable job in devising a universal service plan for rural carriers that preserves existing universal service support levels while facilitating competition in rural areas. The Rural Task Force faced a monumental challenge. Congress recognized that competition might encourage investment in infrastructure and bring new and improved services to rural America. Congress also found that special measures beyond competition are required to preserve and advance universal service in rural areas. The Rural Task Force's recommendation is a fairly comprehensive plan designed to balance the sometimes-competing goals of competition and universal service.

The recommendation is endorsed by all members of the Rural Task Force and represents a

[1] See generally, the record in the Senate Commerce Committee hearing on rural digital divide issues, March 28, 2000, and the opening statement of Chairman Burns.

consensus of their sometimes-divergent positions. As such, the plan deserves due deference. I support its prompt and complete adoption.

B. Unserved and Underserved Areas Should be Promptly Addressed.

Under the Rural Task Force recommendation support to some extremely high-cost rural areas may not be sufficient to achieve rates and service comparable to those in urban areas, as is required by Section 254 of the Act. Some areas of the country, primarily because of geography, have extraordinarily high costs for plant items not supported by the current or proposed support plans. These plans generally support high loop costs for all companies and switching costs for small companies. However, costs not covered may include, depending upon the circumstances, transport, general support facilities, and some switching costs.[2] In addition, the end result suggests that some very high cost companies may be left with intrastate revenue requirements net of federal support in excess of $50 per line per month.[3] We must develop a mechanism that assures "sufficient" support for all areas.[4] Otherwise, the sufficiency requirement of Section 254 of the Act will not be met.

I am particularly concerned that some consumers in some rural areas do not have any telephone service available.[5] Where consumers have no opportunity to purchase telephone

[2] The amount of switching cost covered is based on the size of the company (the smaller the company, the greater the support) rather than the per line switching cost. Therefore, a slightly larger company with very high switching cost might not receive adequate support.

[3] Based upon data filed by the National Exchange Carriers Association, it is possible to calculate an "all facilities" embedded cost-based revenue requirement for each rural carrier. Based upon this analysis, a "best fit" line can be calculated to the cost and support data. The results show that, on average, only 44 cents of every dollar of unseparated cost are matched by the two federal programs for intrastate services: loop support and local switching support. Thus if a company has an overall intrastate separations factor of 75%, the existing system supports 44 cents of the 75 cents of every dollar that is separated to intrastate. This leaves approximately 31 cents per dollar of cost to recover from intrastate services. Because some companies have total embedded costs in excess of $200 per line per month, this can leave companies with revenue requirements from intrastate services of $50 per line per month or more. Detailed examples cannot be offered here because the NECA cost data are under a protective order in this docket.

[4] See Maine/Vermont Comments and En Banc Comments of Maine Public Utility Chairman Thomas Welch.

[5] I am aware that unserved areas exist in numerous states. For example only, some of the unserved areas in Montana are:

*Qwest facilities extend to the General Mercantile store in Polebridge, Montana. Residents of the North Fork area north of Polebridge who have no access to telecommunications.

*The area south of Glasgow located on the "High Line" of eastern Montana is a rugged and sparsely populated area often termed the "bad lands." Ranches are up to 45 miles south of the nearest central office in Glasgow, Montana. It is not economically feasible for a rural telephone company to extend transport facilities to serve the area. Cellular service provides limited telecommunications options due to the terrain and location.

*Sixteen customers living approximately twenty miles southwest of Utica in central Montana have no access to telecommunications. The estimated cost to connect these customers to the network is $400,000 ($250,000 for fiber facilities and $150,000 for backbone). The terrain is rugged with sheer rock cliffs on the side of the road that is not much more than a few feet of dirt piled on top of rock. Burying the fiber to connect these (continued….)

service there exists a fundamental universal service concern.

Because of the pressing concern about unserved areas, I recommend that within the next six months the Commission commence a proceeding and refer to this Joint Board the question of whether additional, specific measures are needed for areas where no telephone service is currently available. Two members of the Rural Task Force suggested this approach.[6] Initiating a proceeding does not indicate any predetermination about the scope of the problem, the range of technical and policy solutions, or the appropriate balance of federal, state, and private strategies. This proceeding should also examine areas that are seriously underserved.[7] I hope the results of this new proceeding if adopted can be implemented as soon as possible.[8]

C. The Next Review of Rural Support Should Commence in Time to Allow Thoughtful Development and Consideration of Issues.

(Continued from previous page)

customers to the public switched network would require rock sawing for nearly 20 miles. The distance and the mountainous terrain limit cellular options.

*Six customers living in the Olaf area, twenty-five miles north of Two Dot in central Montana have no telecommunications service. An engineering study estimates it would cost $200,000 in predominately transport investment to provide service to these six customers. The rocky terrain and mountainous area are barriers to service access.

*Seventy-four persons filed a petition with the Montana PSC in 1998 seeking telephone service in the Little Wolf Creek area north of Helena. Again the cost of tying this area into the public switched network is prohibitive.

*A destination ranch for critically ill children is located 23 miles west of Whitefish, Montana (northwest Montana) near the Hope Ranch, a private adolescent facility. Neither the ranch nor the approximately 24 families who live in the area, have access to telecommunications. Cellular service is poor or not available due to the rugged terrain and mountains. Engineering studies have determined that the cost to extend trunking facilities needed to connect this area to the public switched network is prohibitive.

*Other examples of unserved territory can be found in Maine. In most all cases these areas consist of relatively compact settlements that are far from existing service facilities. In some cases these areas are islands or are settlements not connected to the rest of Maine by public roads. Therefore, in these areas, loop costs are likely to be low but switching costs per customer and trunking costs are likely to be extremely high.

While commenters identify the problem, these specific examples are outside the record, and are only offered to demonstrate the problem’s significance. This does not suggest the appropriate policy, technology, or balance of federal, state and private efforts to address such problems. For another time are stories about successful and unsuccessful efforts to extend service, and - where successful - about the dramatic effect on citizens receiving good telecommunications access for the first time.

[6] See Reply Comments of Maine Public Advocate Stephen Ward and West Virginia Consumer Advocate Billy Jack Gregg.

[7] On its own motion the Commission has undertaken proceedings concerning access to telecommunications on tribal lands and to promote deployment and subscribership in underserved tribal areas. State commissions have been active in implementation.

[8] The Commission should be careful not to diminish the flow of support and not take away any new support provided under the Rural Task Force recommendations when it implements any needed additional support for unserved areas.

A full five year implementation period will allow providers sufficient regulatory predictability to make critical investments. It will also allow thoughtful consideration of any universal service issues before expiration of the five year period. The next review will also be an opportunity to more fully address several issues raised by commenters in this proceeding that could not be addressed while acting promptly on the Rural Task Force Recommendation. Over the next five years markets and technology will surely change. Therefore, Joint Board and the Commission should commence its initial review of the high cost mechanism for rural carriers by January 2002.

As the Rural Task Force's findings demonstrate, there are substantial differences between the average characteristics of rural carriers and those of nonrural carriers. The Rural Task Force was charged solely with considering the needs of rural carriers and therefore did not consider the service needs of the large number of rural customers served by nonrural carriers. When the Rural Task Force recommendation is put in place the support rules for rural carriers will remain significantly different from those that apply to nonrural carriers. Furthermore, the costs for nonrural carriers' support will be measured primarily on an embedded cost basis, but nonrural costs will be measured on a forward looking basis. The difference in the way costs are measured and the method used to determine needed support will produce significantly different support amounts for comparable rural areas; those served by a rural carrier and others served by a nonrural carrier.[9] Several commenters described potential problems at the borders between the two programs.

During the next review the Joint Board should coordinate its examination of the rural and nonrural mechanisms, identify areas where the programs could benefit from harmonization,[10] and develop strategies to do so. This does not suggest that the non-rural mechanism should be adopted for rural companies. In fact some might suggest that a mechanism closer to that used for rural companies might be desirable for rural areas served by large companies if sufficient support is going to be provided for all rural areas.

Some commenters suggested that existing support mechanisms might provide some carriers support where the need for that support has not been demonstrated.[11] From reviewing

---

[9] Commenters suggested that two vastly different support mechanisms may create a risk of the kind of incentives described in the Maine/Vermont comments and in the comments of Maine Chairman Thomas Welch discussed supra.

[10] "Harmonization" does not mean uniformity, particularly due to the "rural differences" identified by the Rural Task Force, and also due to the great limitations in existing economic cost models when applied to rural areas, as identified in Rural Task Force Report 4, A Review of the FCC's Non-Rural Universal Service Fund Method and the Synthesis Model for Rural Telephone Companies. Harmonization means identifying and addressing issues arising on the seams or borders between the two programs, such as the possibly increased incentive to sell exchanges if the seller is eligible for less support, ensuring purchasers are able to invest in those exchanges, or the cost and complexity of maintaining different costing methodologies.

[11] See Maine/Vermont and New York Comments and Comments of Commissioner Thomas Dunleavy of the New York Public Service Commission and Thomas Welch of the Maine Public Utility Commission made to the Joint Board at the San Diego NARUC meeting.

rough cost data, this would appear to be of concern in at most a small number of cases. Interest expressed by some parties in greater targeting to the highest cost areas could be considered in this future proceeding

At least one commenter was concerned that the existing support mechanism may have unintended effects on carrier incentives to overbuild an area where the incumbent has significantly under-invested.[12] As pointed out at the en banc hearing, rural carriers sometimes considering overbuilding a nearby area served by a different incumbent. According to the witness the decision to overbuild is affected, however, by the current support mechanism, which treats overbuilders as CLECs, and thus limits support based upon the embedded costs of the incumbent. If the incumbent, however, has not invested in its system, this support may be small.[13] The result may be an incentive towards a buy-then-rebuild strategy as opposed to a simple overbuilding strategy. If so, the support mechanism may have the unintended effect of increasing the sale price of poor quality plant and thus the overall cost of providing service. The Joint Board should address this question when it examines the design of the rural and nonrural systems.

Long-term sustainability of support mechanisms will be a critical issue as well. We need to consider mechanisms consistent with changing markets.

For these reasons the Joint Board and the Commission should begin review of high-cost support mechanisms for rural carriers by January 2002. This timing will allow orderly examination of both rural and non-rural support mechanisms at the same time. This will facilitate the evaluation, for all rural areas, of whether rates and services are comparable to those in urban areas.

D. The Commission Should Adopt the "No Barriers" to Advanced Services Recommendation.

Finally, I strongly endorse the Rural Task Force's balanced and thoughtful approach to advanced services, and its clear statement of the relationship between the network and the services provided over the network. The Commission should ensure that the Federal universal service methodology is not a barrier to the deployment of advanced services in all areas of the nation. I look forward to the upcoming referral to the Joint Board of the definition of covered services.

E. Conclusion.

In summary, I strongly support the Rural Task Force recommendations. I urge the Commission to promptly and fully implement the package of proposals for a full five years. In addition, I recommend that the Commission initiate a proceeding within the next six months and make a referral to the Joint Board concerning whether additional universal service measures are

[12] See David Cosson's comments at the en banc hearing.

[13] On the other hand, if the carrier first buys the existing plant and then rebuilds it, the purchasing carrier gains ILEC status under the rules, but under rule 305 support is limited to the prior owner's support. The Rural Task Force's "Safety Valve" may ameliorate this problem, but does not eliminate it.

needed for unserved and significantly underserved areas where no service is available.

I thank and congratulate the Rural Task Force for its effort. I especially commend my colleague and good friend Commissioner Bill Gillis for his extraordinary leadership.

Commissioner Laska Schoenfelder concurs in this statement. Public Counsel Martha Hogerty concurs in the request for a referral concerning unserved areas.