STATEMENT OF
COMMISSIONER KEVIN J. MARTIN
Approving in Part, Dissenting in Part

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

Joint Board Recommended Decision

I wish to thank all my colleagues on the Federal-State Joint Board for their hard work and contributions in the effort to reach consensus on the important issue of establishing a universal service support system for non-rural carriers. I believe that today's effort, however, falls short in meeting our obligation to ensure that consumers living in rural and high cost areas have access to similar telecommunications services at rates that are reasonably comparable to rates paid by urban consumers.

Congress gave the Commission a clear mandate: to ensure that consumers in all regions of the nation have access to 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* (emphasis added)."[1] Congress' direction is also clear regarding the obligation to establish mechanisms that are "…specific, predictable and sufficient…to preserve and advance universal service."[2] In remanding the Commission's previous attempt to establish a federal-high cost universal service support mechanism for non-rural carriers, the United States Court of Appeals for the Tenth Circuit agreed that these fundamental guiding principles govern Commission action on any policies regarding universal service support mechanisms.[3]

Despite this remand, the majority's recommendation essentially reaffirms the Commission's existing universal service support mechanism for non-rural carriers. The decision continues to base support on forward looking costs and creates a sparsely defined second supplemental support system based on rate comparisons. Today's recommendation falls short in its response to the court mandate that we define the statutory term "reasonably comparable" for purposes of the cost-based support mechanism and fails to demonstrate, with any degree of specificity, how the proposed secondary mechanism will satisfy

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[1] See 47 U.S.C. 254(b)(3).
[2] See 47 U.S.C. 254(b)(5).
[3] *Federal-State Join Board on Universal Service,* CC Docket No. 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, 14 FCC Rcd 20432(1999)(*Ninth Report and Order) remanded*, *Qwest Corp. v. FCC,* 258 F.3d 1191, 1199 (10th Cir. 2001).

the statutory requirement that universal service support be "specific, predictable and sufficient."

For these and the reasons explained below, I respectfully dissent from portions of the majority opinion today.[4]

Use of Costs as a Surrogate for Rates to Determine Non-Rural High Cost Support

Section 254(b)(3) of the Communications Act requires that universal service support mechanism ensure that telecommunications services in all regions of the nation be provided at reasonably comparable "rates." The majority, however, recommends continuing the practice of using costs rather then rates to determine federal support. I am not convinced that a mechanism based solely on costs would meet the statutory mandate requiring a comparison of rates.

Moreover, I fear that the recommended decision may be either arbitrary or not fully thought through. If the Joint Board is confident that a cost-based support system satisfies our statutory obligation to produce reasonably comparable rates, then why does it propose establishing an entirely new support mechanism based on rate comparisons? Similarly, if the Commission were to adopt the Joint Board's recommended "supplemental rate comparability review," why should it not abandon the cost-based support mechanism and instead rely solely on the rate-based support mechanism? If we need the supplemental rate comparison to meet our statutory obligation, would it not be simpler to have only one mechanism rather than two? These questions seem to remain unanswered by the majority.

The majority's rejection of rate-based distribution and support for a cost-based mechanism is based on two arguments: (i) an analysis of disparate local rate design practices throughout the nation remains too difficult a task; and (ii) the use of costs reflects the federal government's primary obligation to support only those states that "do not have the resources within their borders to support all of their high cost lines."[5] In my view, both of these arguments fail to support the Joint Board's position.

First, in response to the argument that such an analysis is too difficult, the majority appears to create just such an analysis in its "supplemental rate comparability review." The majority also fails to note or even address the fact that many of the issues and data necessary to perform a rate-based

[4] In addition to the reasons discussed below, I also agree with and join in many of the concerns raised in Commissioner Bob Rowe's thorough and thoughtful analysis in his dissent.
[5] Recommended Decision at paras. 19-21, 24.

comparison will be needed in the context of initiating the proposed catch all "supplemental rate comparability review." On its face, one well-defined support mechanism based on rate comparisons would appear to present an equal or lesser administrative burden for the Commission, the states and carriers compared to the dual cost-based and rate-based mechanisms recommended by the majority today.

The majority's recommendation also contains an inherent presumption that the federal government's role in establishing a support mechanism is apparently limited to equalizing cost discrepancies between states but not equalizing rate discrepancies between rural and urban areas.[6] I disagree. The statute is clear. Our job is to ensure that services in rural and high cost areas are "available at rates that are reasonably comparable to rates charged for similar services in urban areas."[7] The 10th Circuit explicitly rejected the FCC's contention that it had no duty to ensure the reasonable comparability of rural and urban rates and stated that we are "obligated to formulate policies so as to achieve the goal of reasonable comparability…"[8]

In my view, if the Commission is only going to address discrepancies between and among states, then there must be a requirement that states address such discrepancies within their borders. Whether such a requirement compels rate averaging within states or requires that a state universal service mechanism be in place, such action must address differences in cost between rural and urban areas. Yet this decision fails to require that such inequities between urban and rural rates be addressed.[9]

The proposed expanded rate certification mechanism is insufficient. Under the proposed certification process, states would be permitted to report rates that are not "reasonably comparable" according to the benchmark. Such rates

[6] Recommended Decision at paras. 25-26. "The Commission's primary role is to identify those states that do not have the resources within their borders to support all of their high-cost lines.… The Commission explained in the *Ninth Report and Order* that the non-rural high cost support mechanism "has the effect of shifting money from relatively low-cost states to relatively high-cost states. The Commission believed that its non-rural support mechanism ensured that no state with costs greater than the national benchmark would be forced to keep rates reasonably comparable without the benefit of federal support….We continue to support these policies."

[7] 47 U.S.C. 254(3).

[8] 258 F.3d at 1200.

[9] See *Ninth Report and Order* at 20482-3, para. 95 (The Commission found it most appropriate to allow states to determine how non-rural cost support is used, "[b]ecause the support…is intended to enable the reasonable comparability of intrastate rates, and states have primary jurisdiction over intrastate rates."; *see* id. At 20483, para. 96 ("As long as the uses prescribed by the state are consistent with 254(e), we believe that states should have the flexibility to decide how carriers use support provided by the federal mechanism."). See Recommended Decision at paras. 43-56. Even in light of the 10th Circuit remand requiring the Commission to consider appropriate state inducements to address reasonably comparable rates, the Joint Board fails to consider recommending either a state averaging mandate or mandatory state universal service mechanism requirement to address discrepancies between costs in rural and urban areas.

could eventually be allowed to meet the "reasonably comparable" standard if a state demonstrates "additional services included in the basic service rate" or by outlining "the method in which the state has targeted existing universal service support."[10] In my view, such a certification process is insufficient without a standard enunciating the allowable discrepancy for intrastate rates.

Sufficiency of High-Cost Support under the National Average Cost Benchmark

Even if costs can be used as a surrogate, I question the majority's recommendation to use the 135% benchmark to ensure that rural rates are "reasonably comparable."

In deciding to proceed with a cost-based methodology to ensure reasonably comparable "rural" and "urban" rates, we should compare "rural" costs to average "urban" costs. The Commission certainly has data readily available to perform this comparison. Under the Synthesis Cost model, cost data can be produced by density zone or at the wire center level. Yet, the majority summarily rejects the concept of an "urban benchmark," setting a benchmark at 135 percent of national average cost. In the process, the decision sidesteps the question of whether the benchmark produces sufficient support in light of the existing disparity between national average cost and the lower average urban cost.

As Commissioner Rowe notes, the majority's rejection of the urban benchmark is "confusing and unpersuasive."[11] The majority never tackles the uncomfortable fact that the 135 percent benchmark is too high because national average costs are already higher than urban costs because they include in the national average the very rural areas at issue. In other words, the high costs associated with serving rural areas are used twice: once to raise the national average and again in comparison.

Let me illustrate my concern with a simple example. If half of the country lived in an urban area with costs of $10 and the other half of the country lived in a rural area with costs of $30, the difference between the costs of the average urban area and average rural area would be $20. But if a national average were taken, including the costs of the rural areas, the national average cost would be $20. If support were then based on the difference between the rural cost ($30) and 135% of the national average (1.35 x $20=$27), each rural resident would have costs of $27 ($30-$3 of support) and each urban resident would have costs of $13 ($10 + $3 of support). I do not believe that such a

[10] Recommended Decision at para. 55.
[11] *See* Commissioner Bob Rowe's Separate Statement at 8.

methodology sufficiently addresses the reasonable comparability of rural and urban costs. The inclusion of rural costs in the average along with the adoption of a 135% benchmark systematically underestimates the costs of rural areas.[12]

Instead, the majority finds fault with the use of an urban benchmark based on the fact that it "substitutes costs for rates" and "compares statewide average costs to nationwide urban costs."[13] The majority's criticism appears strangely out of place given that its own recommendation is also based on a cost-based support system. I find it ironic that the majority can justify its "existing system on the ground that costs equal rates, and at the same time rejects all changes on the ground that costs do not equal rates."[14]

It also rejects the urban benchmark because it would "require more funding or a higher benchmark level because urban average costs are lower than national average costs."[15] I fail to see how the potential for greater funding levels should prevent us from adopting a support system that meets our statutory obligation.[16] Indeed, I fear that this reasoning reflects an analysis that concluded first that there would be no additional funding for rural areas and second adopted a mechanism to assess "reasonable comparability" that achieved that result. I believe our statutory obligation was to achieve reasonably comparable urban and rural rates even if that "requires more funding" than the current system provides.

Nor do I understand how the majority reaches the conclusion that the urban **cost** benchmark fails to "better satisfy the statutory comparison of urban and rural **rates**."[17] I join Commissioner Rowe in questioning how the majority finds that additional "incremental support would be ineffective at producing comparable rates, but existing support passes the test."

In addition, I question the use of forward-looking costs as the basis for distributing universal service support. Today, rates are set in most states through the use of actual costs not hypothetical replacement costs. Forward-looking costs have little, if any, nexus to the establishment of end user retail rates. Use of these costs for calculating universal service support results in

[12] National averages could be used without a benchmark or urban averages could be used with a benchmark but the combination of the two mechanisms is arbitrary.
[13] Recommended Decision at para. 39.
[14] *See* Commissioner Bob Rowe's Separate Statement at 8.
[15] Id. at 40.
[16] The United States Department of Agriculture's Rural Utilities Service (RUS) recommended adoption of a benchmark tied to the national average urban loop cost or another statistical indicator more representative of urban costs, not the national average costs. RUS notes that 135% of the national average (urban and rural) "loop cost" exceed its estimate of urban "loop costs" by 233%.
[17] Recommended Decision at 39. (emphasis in original).

support being provided to some areas with low end user rates while certain areas that have high rates receive insufficient support. In my view, we could better achieve comparability of rates if we based our universal service support system on actual rather than forward looking costs.

Finally, the majority cites three studies/analyses in support of its decision to continue using the 135 percent benchmark. I disagree with the majority's conclusion that these studies support its decision to retain the benchmark. First, the majority points to the General Accounting Office (GAO) study to show that national averages of rural, suburban and urban rates are affordable and reasonably comparable. The majority, however, fails to acknowledge serious deficiencies in the GAO study that fail to support the use of the benchmark for non-rural carriers.[18] For example, the GAO study includes data from areas served by rural carriers, areas that are not relevant to the establishment of non-rural carrier support system. In addition, GAO's rate comparison ignores whether rates in different service areas apply to comparable services. Moreover, national averages cited by GAO do not assist the Commission in addressing our core responsibility of whether rates in certain rural or high cost areas are comparable to rates in urban areas, or even whether rates vary significantly from state-to-state. To the contrary, as Commissioner Rowe points out, GAO's data demonstrates a vast disparity on state rates (e.g., residential rates at two Wyoming locations exceeding $40 versus residential rates in Roaring Springs, Texas of $7.10).[19]

I also join Commissioner Rowe's dissent asserting that a standard deviation analysis fails to justify the current benchmark.[20] I find it particularly troubling that the majority arbitrarily raises the benchmark to 135 percent even in light of its own analysis demonstrating that 2.0 standard deviation above the national mean results in a 132 percent benchmark. The majority offers no reasoned basis why states should be denied the additional $.50 per customer per month of support that would result by applying the results of the majority's own standard deviation analysis.

Supplementary Rate Review

The majority, in today's recommendation, sets forth an additional supplemental process for rate comparison. It recommends adopting a new and vaguely defined supplemental mechanism. Rather than provide a clearly defined mechanism the majority instead offers an ad hoc process where the specific mechanisms will apparently develop on a case-by-case basis.[21] The

[18] *See also* Commissioner Rowe's Separate Statement at 2-3.
[19] *Id.* at 3.
[20] *Id.* at 5-7.
[21] *Id. at* 16.

majority envisions a process where States seeking additional federal support will be required to provide a "rate analysis," and will have "great flexibility" in demonstrating that rates are not reasonably comparable.[22]

In my view, the majority's "supplementary rate review" is striking similar to the state-by-state cost study approach the Commission had originally rejected in order to pursue its flawed nation-wide universal service cost model approach. Under the recommended state-by-state approach, each state would have significant latitude to suggest its own procedures for adjusting rates. Without specific guidelines or a clearly defined standard, this approach appears to invite the potential for uneven and potentially discriminatory results.

I am troubled that majority fails to offer any specific guidance on critical areas of its newly proposed process. The item is silent, for example, on whether states should alter rates to take into account the scope of certain local calling areas or differing calling plans. In my view, without an established standard or guidance for states in this area, the poorly defined "supplementary rate review" will most likely provide results, if any, that are highly susceptible to legal challenge.

Finally, Commissioner Rowe is correct in questioning whether the proposed "supplementary rate review" would "create perverse incentives for carriers."[23] One of the reasons the Commission adopted the forward-looking cost model was because it believed that an embedded-cost support system promotes inefficient investment that would inhibit competitive entry. I find it ironic that the majority now seeks to adopt a rate-based mechanism that inherently relies on local rates which are typically based on embedded costs.

[22] Recommended Decision at para. 56.
[23] *See* Commissioner Bob Rowe's Separate Statement at 18.