

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

In the Matter of
High-Cost Universal Service Support
Federal-State Joint Board on
Universal Service
WC Docket No. 05-337
CC Docket No. 96-45

NOTICE OF INQUIRY

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By the Commission: Acting Chairman Copps; Commissioners Adelstein and McDowell issuing separate statements.

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I. INTRODUCTION

1. In this notice of inquiry (NOI), we seek to refresh the record regarding the issues raised by the United States Court of Appeals for the Tenth Circuit (Tenth Circuit) in the *Qwest II* decision.¹ In that decision the Tenth Circuit invalidated the Commission's high-cost universal service support mechanism for non-rural carriers, which determines the amount of support to be provided to each state by comparing the statewide average forward-looking cost per line for non-rural carriers to a nationwide cost benchmark. In December 2005, the Commission issued a notice of proposed rulemaking seeking comment on the non-rural support mechanism in light of the *Qwest II* decision.² Since the Commission issued the *Remand NPRM*, it has sought comment on various proposals for comprehensive reform of the high-cost support mechanisms, rural as well as non-rural.³ Several parties filed additional proposals in response to the *High-Cost Support Reform NPRMs* and the *Comprehensive Reform FNPRM*, as well as specific proposals to address the issues raised by the Tenth Circuit. Because these proposals may be helpful to us in crafting a support mechanism that addresses the court's concerns, we ask parties to refresh the record in this proceeding and specifically seek comment on several proposals. We also seek comment generally on how our decision in this remand proceeding should relate to more comprehensive high-cost reform and the Commission's initiatives regarding broadband deployment.

II. BACKGROUND

2. In section 254 of the Communications Act of 1934, as amended (the Act),⁴ Congress directed the Commission, after consultation with the Federal-State Joint Board on Universal Service (Joint Board), to establish specific, predictable, and sufficient support mechanisms to preserve and advance universal service.⁵ In addition, in section 254(b), Congress provided a list of principles upon which the Commission must base policies for the preservation and advancement of universal service.⁶ Among other things, section 254(b) provides that consumers in rural, insular, and high-cost areas should have access to telecommunications services at rates that are "reasonably comparable to rates charged for

¹ *Qwest Communications Int'l, Inc. v. FCC*, 398 F.3d 1222 (10th Cir. 2005) (*Qwest II*).

² *Federal-State Joint Board on Universal Service, High-Cost Universal Service Support*, CC Docket No. 96-45, WC Docket No. 05-337, Notice of Proposed Rulemaking, 20 FCC Rcd 19731 (2005) (*Remand NPRM*).

³ *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, 23 FCC Rcd 1467 (2008) (*Identical Support Rule Notice*); *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, 23 FCC Rcd 1495 (2008) (*Reverse Auctions Notice*); *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, 23 FCC Rcd 1531 (2008) (*Joint Board Comprehensive Reform Notice*) (collectively, *High-Cost Support Reform NPRMs*). In addition, the Commission issued a further notice of proposed rulemaking seeking comment on comprehensive universal service and intercarrier compensation reform on November 5, 2008. *High Cost Universal Service Reform; Federal-State Joint Board on Universal Service; Lifeline and Link Up; Universal Service Contribution Methodology; Numbering Resource Optimization; Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Developing a Unified Intercarrier Compensation Regime; Intercarrier Compensation for ISP-Bound Traffic; IP-Enabled Services*, CC Docket Nos. 96-45, 99-200, 96-98, 01-92, 99-68, WC Docket Nos. 05-337, 03-109, 06-122, 04-36, Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, FCC 08-262 (rel. Nov. 5, 2008) (*Comprehensive Reform FNPRM*).

⁴ 47 U.S.C. §§ 151, *et seq.* Section 254 was added by the Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (1996 Act).

⁵ 47 U.S.C. § 254; *see also Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Notice of Proposed Rulemaking and Order Establishing Joint Board, 11 FCC Rcd 18092 (1996).

⁶ 47 U.S.C. § 254(b)(1)-(7).

similar services in urban areas.”⁷ In addition, section 254(e) provides that federal universal service support “should be explicit and sufficient to achieve the purposes of this section.”⁸

3. In 1999, based on recommendations from the Joint Board, and building on the framework set forth by the Commission in prior orders, the Commission adopted a non-rural mechanism that provided federal high-cost support to non-rural carriers in states where the statewide average forward-looking cost per line was above 135 percent of the nationwide cost per line.⁹ In *Qwest I*, the Tenth Circuit concluded that the Commission failed to: (1) define adequately the key statutory terms “reasonably comparable” and “sufficient;” (2) adequately explain setting the funding benchmark at 135 percent of the national average; (3) provide inducements for state universal service mechanisms; and (4) explain how the non-rural funding mechanism will interact with other universal service programs.¹⁰

4. In the *Order on Remand* the Commission adopted a modified national cost benchmark based on two standard deviations above the national average cost.¹¹ The Commission also adopted the Joint Board’s recommendation to implement a rate review, and sought comment on specific issues related to the rate review. Among other things, in the *Order on Remand*, the Commission set a national urban rate benchmark at two standard deviations above the average urban residential rate in an annual rate survey, and defined the statutory term “reasonably comparable” based on the rate benchmark for purposes of the rate review.¹² The Commission defined the term “sufficient” as “enough federal support to enable states to achieve reasonable comparability of rural and urban rates in high-cost areas served by non-rural carriers.”¹³

5. On February 23, 2005, the Tenth Circuit remanded the *Order on Remand* to the Commission.¹⁴ The court again held that the Commission failed to reasonably define the terms “sufficient” and “reasonably comparable.”¹⁵ The court directed the Commission on remand to articulate a definition of “sufficient” that appropriately considers the range of principles in section 254 of the Act, and to define “reasonably comparable” in a manner that comports with its duty to preserve and advance universal service.¹⁶ Because the non-rural high-cost support mechanism rests on the application of the definition of “reasonably comparable” rates that the court invalidated, the court deemed the support mechanism invalid.¹⁷ The court further noted that the Commission based the two standard deviations *cost* benchmark on a finding that *rates* were reasonably comparable, without empirically demonstrating a

⁷ 47 U.S.C. § 254(b)(3).

⁸ 47 U.S.C. § 254(e). Similarly, section 254(b)(5) states that there “should be specific, predictable, and sufficient Federal and State mechanisms to preserve and advance universal service.” 47 U.S.C. § 254(b)(5).

⁹ *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 (1999) (*Ninth Report and Order*), remanded, *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2003) (*Qwest I*), *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Order on Remand, Further Notice of Proposed Rulemaking, and Memorandum Opinion and Order, 18 FCC Rcd 22559 (2003) (*Order on Remand*), remanded, *Qwest II*, 398 F.3d 1222.

¹⁰ *Qwest I*, 258 F.3d at 1195.

¹¹ *Order on Remand*, 18 FCC Rcd at 22589, para. 49.

¹² *Id.* at 22582, para. 38.

¹³ *Id.* at 22562, para. 4.

¹⁴ *Qwest II*, 398 F.3d 1222.

¹⁵ *Id.* at 1233.

¹⁶ *Id.* at 1237.

¹⁷ *Id.*

relationship between the costs and the rates in the record.¹⁸ On remand, the court directed the Commission to “utilize its unique expertise to craft a support mechanism taking into account all the factors that Congress identified in drafting the Act and its statutory obligation to preserve *and* advance universal service.”¹⁹

6. On December 9, 2005, the Commission issued the *Remand NPRM* seeking comment on a number of issues to enable the Commission to craft a non-rural high-cost support mechanism consistent with the court’s decision and the statute.²⁰ Specifically, the Commission sought comment on: (1) how the Commission should define the statutory term “sufficient” to take into account all of the principles enumerated in section 254(b); (2) how the Commission should define “reasonably comparable” under section 254(b)(3), consistent with its concurrent duties to preserve and advance universal service; and (3) how, in light of the interpretation of the key statutory terms, the Commission should modify the high-cost funding mechanism for non-rural carriers.²¹

III. PARTIES’ PROPOSALS

7. In response to the Commission’s request for comments responding to the Tenth Circuit’s remand of the non-rural high-cost support mechanism and in comments on reform of the overall high-cost support disbursement mechanism, several parties have filed specific proposals related to disbursement of high-cost support to non-rural carriers.

A. Qwest Proposal

8. On May 5, 2008, Qwest Communications International, Inc. (Qwest) filed a proposal for revising the methodology used to determine high-cost support for non-rural incumbent local exchange carriers (LECs) that Qwest argues would comply with the Tenth Circuit’s decision in *Qwest II*.²² Qwest claims that the Commission still relies heavily on the existence of implicit subsidies to maintain reasonably comparable rates in rural areas served by non-rural carriers, and that the current non-rural mechanism provides carriers with only a fraction of the high-cost support needed to serve those areas.²³ Qwest argues further that these implicit subsidies have eroded significantly since the 2003 *Order on Remand*, and Qwest further asserts that it is increasingly untenable for non-rural incumbent LECs to provide services in rural areas that are reasonably comparable to those provided in urban areas without corresponding explicit subsidies that recognize the actual cost of serving those areas.²⁴

9. Qwest proposes that the Commission revise the current non-rural high-cost support

¹⁸ *Id.*

¹⁹ *Id.* (emphasis in original).

²⁰ See generally *Remand NPRM*, 20 FCC Rcd 19731. The Commission also sought comment on whether the Commission should adopt a separate non-rural high-cost support mechanism for insular areas. *Id.* at 19746, para. 33.

²¹ *Id.* at 19735, para. 7.

²² Letter from R. Steven Davis, Senior Vice President – Federal Relations, and Shirley Bloomfield, Senior Vice President – Public Policy, Qwest, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 96-45, WC Docket No. 05-337 (filed May 5, 2008) (Qwest May 5th *Ex Parte* Letter) (attaching Proposal for Implementing the Tenth Circuit’s Remand in *Qwest II*) (Qwest Proposal).

²³ Qwest Proposal at 11-12.

²⁴ *Id.* at 16. Qwest cites vigorous competition, the substitution of other services, and the resulting line loss as reasons for the erosion of implicit subsidies. See *id.* at 13-16.

mechanism to target support to the highest-cost wire centers served by non-rural incumbent LECs.²⁵ To advance universal service, Qwest proposes that the Commission reduce the current non-rural high-cost support benchmark to 125 percent of the national average urban rate, and provide federal support above that threshold.²⁶ Assuming that support to competitive eligible telecommunications carriers (ETCs) is frozen, Qwest estimates that these changes to the non-rural mechanism would increase the amount of support provided to non-rural ETCs by \$1.2 billion.²⁷ Qwest suggests that the Commission could limit the increase in non-rural high-cost support to approximately \$322 million by initially targeting Qwest's proposed wire center-based high-cost support to ETCs in rural areas served by medium-size incumbent LECs.²⁸ Qwest defines medium-size incumbent LECs as non-rural carriers with fewer than 25 million access lines nationwide, and notes that all non-rural carriers except AT&T and Verizon fall under this threshold.²⁹

B. Vermont and Maine Proposal

10. In comments responding to the *Remand NPRM*, the Vermont Public Service Board, the Vermont Department of Public Service, and the Maine Public Utilities Commission (Vermont and Maine) proposed that the Commission use "net subscriber cost" as a proxy for rates in its reasonable comparability rate standard and in its support calculation.³⁰ Under this proposal, the Commission would first determine each carrier's costs for serving local customers, then deduct revenues from other sources (including intercarrier net revenue, special access revenue, private line revenue, and customer revenue from non-universal service supported services), and finally divide by the number of switched lines to determine the per-line net subscriber cost.³¹ Although in their initial comments Vermont and Maine suggested that the Commission could choose to define costs at the state, study area, or wire center level, in their reply comments they argued that the Commission should continue to determine support based on statewide average cost.³² Rather than using a benchmark based on standard deviations, Vermont and Maine proposed that the Commission use a benchmark of no more 125 percent of the nationwide urban rate (defined as net subscriber cost).³³ If the Commission continues to use its forward-looking cost model to determine non-rural support, Vermont and Maine urged the Commission to address problems with the model to improve its accuracy.³⁴ Finally, Vermont and Maine recommended consolidating the rural and

²⁵ *Id.* at 4, 22-25.

²⁶ *Id.* at 4, 24.

²⁷ *Id.* at 4, 25.

²⁸ *Id.* at 4-5, 26-27.

²⁹ *Id.* at 4-5, 26-27. Qwest argues that problems related to the loss of implicit subsidies and inadequate universal service support are most acute for non-rural incumbent LECs that lack the size, scale, and scope of AT&T and Verizon. *See id.* at 20-21.

³⁰ Comments of Vermont Public Service Board, Vermont Department of Public Service, and Maine Public Utilities Commission, CC Docket No. 96-45, WC Docket No. 05-337 at 19, 27-29 (filed Mar. 27, 2006) (Vermont/Maine Comments).

³¹ *Id.* at 27-28. Vermont and Maine suggest that the Commission could define costs as embedded, forward-looking, or a combination of both. *Id.* at 27.

³² Reply Comments of Vermont Public Service Board, Vermont Department of Public Service, and Maine Public Utilities Commission, CC Docket No. 96-45, WC Docket No. 05-337 at 23-25 (filed May 26, 2006) (Vermont/Maine Reply Comments). *See also* Reply Comments of the Vermont PSB, VDS, Maine PUC, and ConnectME Authority to Qwest Proposal to Revise the Non-Rural Mechanism, CC Docket No. 96-45, WC Docket No. 05-337 (filed June 2, 2008).

³³ Vermont/Maine Comments at 31-32.

³⁴ *Id.* at 38-39.

non-rural support mechanisms, and proposed that the Commission define “rural” areas as those areas that are not defined by the Census Bureau as “urbanized areas.”³⁵

C. Embarq Proposal

11. On September 28, 2008, Embarq proposed that the Commission replace all non-rural high-cost support and high-cost loop support in price cap study areas with a new mechanism – the Broadband and Carrier-of-Last-Resort Support (BCS) plan.³⁶ Under Embarq’s BCS Plan, support would be funded at approximately \$1 billion per year and allocated to price cap high-cost wire centers based on a proxy for household density in the wire center.³⁷ Under the BCS Plan, broadband would not be a supported service, but BCS recipients would commit to make available broadband of at least 1.5 Mbps downstream to at least 85 percent of customers in each wire center receiving support.³⁸ BCS recipients also would commit to provide local services at affordable and comparable rates, and to build out and serve the entire wire center using only their own facilities within five years.³⁹ The BCS Plan would fund only the incumbent LEC and no more than one competitive ETC in an area.⁴⁰ Embarq argues that its proposal addresses and resolves the issues raised by the Tenth Circuit remand.⁴¹

D. CostQuest Proposal

12. In a November 2008 filing, CostQuest Associates proposed that the Commission adopt an Advanced Services Model for the funding of all high-cost universal service mechanisms for all ETCs.⁴² CostQuest states that every current universal service program relies on both a “cost model” and a “support

³⁵ Vermont/Maine Reply Comments at 20, 35-36.

³⁶ Letter from David C. Bartlett, Vice President – Federal Government Affairs, to Chairman Kevin J. Martin, Commissioner Michael J. Copps, Commissioner Jonathan S. Adelstein, Commissioner Deborah Taylor Tate, Commissioner Robert M. McDowell, Federal Communications Commission, CC Docket No. 96-45, WC Docket No. 05-337 (filed Sept. 18, 2008) (Embarq September 18th *Ex Parte* Letter) (attaching A Plan to Promote Broadband Deployment and Reform High-Cost Support Without Increasing Overall USF Levels) (BCS Plan)).

³⁷ BCS Plan at 5, 20-28. The approximately \$1 billion BCS fund would be derived from the high-cost model support and high-cost loop support currently provided to price cap incumbent LECs and competitive ETCs in price cap area, and the interstate common line support and interstate access support currently provided to competitive ETCs in those areas. *Id.* at 21. The BCS Plan would use the relative costs generated by the Commission’s cost model to distribute the \$1 billion among price cap wire centers. *Id.* at 5, 27.

³⁸ *Id.* at 5.

³⁹ *Id.*

⁴⁰ *Id.* at 6.

⁴¹ *Id.* at 41-45.

⁴² Comments of CostQuest Associates, CC Docket Nos. 96-45, 96-98, 99-68, 99-200, 01-92, WC Docket Nos. 03-109, 04-36, 05-337, 06-122 (filed Nov. 26, 2008) (CostQuest Comments) (attaching, among other things, a white paper by James Stegeman, Dr. Steve Parsons, and Mike Wilson, The Advanced Services Model: Proposal for a Competitive and Efficient Universal Service High-Cost Approach for a Broadband World (CostQuest Proposal)). The CostQuest proposal was originally filed May 31, 2007 by Alltel with its comments in response to the Joint Board’s 2007 public notice seeking comment on comprehensive high-cost universal service reform. *See* Letter from Gene DeJordy *et al.*, Alltel Wireless, to Marlene H. Dortch, Secretary, Federal Communications Commission, WC Docket No. 05-337, CC Docket No. 96-45 (filed May 31, 2007). The November 26th CostQuest proposal was updated slightly from the May 31, 2007 version to remove some dates and Alltel references. *See* CostQuest Comments at 8.

model,” and focuses its white paper on the cost model side of the universal service debate.⁴³ CostQuest argues that the cost models used in the current federal universal service system are outdated, and that it is critical to get the cost model right to make meaningful changes to the support model.⁴⁴ According to CostQuest, “the ideal, modern cost model for use in a reformed universal service system is one that is designed to model forward-looking costs; all carrier types and all technologies would be modeled, and geographic granularity would be used.”⁴⁵ CostQuest identifies the issues that have been raised regarding the Commission’s currently used cost model, and describes the advances in network cost modeling that would address many of these issues.⁴⁶ In addition, CostQuest describes recent efforts in modeling the costs of wireless and broadband networks.⁴⁷ Finally, CostQuest proposes the development of a modern cost model, and describes the key design criteria for the model, the technologies to be modeled, the geographic parameters, the inputs required, and sets out some of the policy questions that would need to be addressed in adopting such a model.⁴⁸

13. We seek comment on these proposals. We also seek comments on other proposals or approaches not contained herein that would address the Tenth Circuit’s remand and issues related to the high-cost support mechanism for non-rural carriers.

IV. ADDITIONAL ISSUES FOR COMMENT

A. Definition of Reasonably Comparable

14. In *Qwest II*, the court rejected the Commission’s reliance on the range of urban rates to identify an appropriate measure of what should be considered reasonably comparable rural and urban rates.⁴⁹ The Commission had reasoned that Congress was aware of the variability of urban rates when it sought to preserve universal service by enacting section 254 of the Act, and would not have required rural rates to be any closer to the average urban rate than other urban rates.⁵⁰ The court found that “the Commission erred in premising its consideration of the term ‘preserve’ on the disparity of rates existing in 1996 while ignoring its concurrent obligation to advance universal service, a concept that certainly could include a narrowing of the existing gap between urban and rural rates.”⁵¹ The court found that by designating a comparability benchmark at two standard deviations above the national average urban rate, the Commission had “ensured that significant variance between rural and urban rates will continue unabated.”⁵² Although the rate data in the record indicated that, in most states, rural rates were the same

⁴³ CostQuest Proposal at 3. According to CostQuest, a cost model produces an estimate of the cost of providing a telecommunications service, and a support model produces a universal service support amount for the carrier or its customer based, in part, on the costs of service. *Id.*

⁴⁴ *Id.* CostQuest identifies as the current cost models the NECA embedded book process used for determining the costs of rural carriers, and the Commission’s cost model used for determining the costs of non-rural carriers. *Id.*

⁴⁵ *Id.*

⁴⁶ *Id.* at 19-32.

⁴⁷ *Id.* at 32-47.

⁴⁸ *Id.* at 48-53.

⁴⁹ *See Qwest II*, 398 F.3d at 1234-37.

⁵⁰ *See Order on Remand*, 18 FCC Rcd at 22584, para. 40. The Commission found that the goal of advancing universal service related to the provision defining universal service as an “evolving level of telecommunications services” and its understanding that the Commission’s universal service rules should evolve as markets and technology change. *See id.* at 22583, para. 39 & n. 138; 47 U.S.C. § 254(c)

⁵¹ *Qwest II*, 398 F.3d at 1236.

⁵² *Qwest II*, 398 F.3d at 1236.

or lower than urban rates in the same state, the data also showed considerable variance in both urban and rural rates among states.⁵³

15. We seek comment on the court's suggestion that "advancing" universal service is a "concept that certainly could include a narrowing of the existing gap between urban and rural rates," and on how the Commission could narrow the existing gap between urban and rural rates to advance universal service.⁵⁴ Notwithstanding the variance in urban rates and state rate-making policies, should the Commission find that a similar variance in rural rates is inconsistent with the reasonable comparability standard in section 254(b)(3) of the Act?⁵⁵ If so, how should the Commission define reasonably comparable rates? Should the Commission continue to compare rural rates in all states to a single national urban rate benchmark? If so, which urban rates should the Commission use to establish the benchmark? Should the Commission compare rural rates to a national average urban rate, rather than some benchmark above the average?⁵⁶ Should the Commission compare rural rates to the lowest urban rate? What would be the range of reasonably comparable rates? For example, should the Commission require that rural rates in all states be no more than ten percent, or perhaps twenty-five percent, above the lowest urban rate?⁵⁷ We seek comment on how the Commission would justify any particular percentage above a benchmark, and on sources of rate data to use in this analysis.

16. We also seek comment on whether we should continue to define reasonable comparability in terms of actual rates. Although the Commission sought comment in the *Remand NPRM* on using a rate-based mechanism instead of the current cost-based mechanism to determine support,⁵⁸ none of the commenters proposed a workable funding mechanism based solely on rates. The overwhelming majority of commenters supported a funding mechanism based on costs, although some proposals use a rate or revenue benchmark in determining the level of support. For example, as discussed above, Qwest proposed using wire center costs to provide support with costs higher than a rate benchmark.⁵⁹ Vermont and Maine proposed using "net subscriber cost" to calculate support, which is based on costs and revenues.⁶⁰ Should the Commission define reasonable comparability by using costs (or costs and revenues) as a proxy for rates? If so, how can we explain the relationship between costs and the resulting rates to the satisfaction of the court?⁶¹ If the Commission defines reasonably comparable costs, should it compare costs to nationwide average costs, or should it also define rural and urban areas and compare rural costs to urban costs? The court implied that the Commission could advance universal service by narrowing the gap between rural and urban rates. Parties advocating that we use a cost benchmark should explain how it would advance universal service.

⁵³ See *Order on Remand*, 18 FCC Rcd at 22571, para. 22 n.55, 22658-71, App. C; see also *Remand NPRM*, 20 FCC Rcd at 19740, para. 18 n.71.

⁵⁴ *Qwest II*, 398 F.3d at 1236.

⁵⁵ 47 U.S.C. § 254(b)(3).

⁵⁶ *Qwest II*, 398 F.3d at 1237 ("Even if such rural rates are compared against the national urban average, we fail to see how they could be deemed reasonably comparable . . .").

⁵⁷ The court seemed to reject the use of the national average urban rate, which was 149% above the lowest urban rate in 2002, as a benchmark. See *id.*

⁵⁸ *Remand NPRM*, 29 FCC Rcd at 19742-43, paras. 23-26.

⁵⁹ See *supra* para. 9.

⁶⁰ See *supra* para. 10.

⁶¹ The court faulted the Commission for not "empirically demonstrating a relationship between the costs and rates" used in its analysis. *Qwest II*, 398 F.3d at 1237.

B. Definition of Sufficient

17. In *Qwest II*, the court directed the Commission to consider all the section 254(b) principles in addition to reasonable comparability in section 254(b)(3) of the Act in defining the term “sufficient.”⁶² In particular, the court was “troubled by the Commission’s seeming suggestion that other principles, including affordability, do not underlie the federal non-rural support mechanisms.”⁶³ We seek comment on how the Commission should balance all seven principles in section 254(b) of the Act in defining the term “sufficient.” Should the Commission give greater weight to some principles over others? Are some principles more directly related to the specific purposes of non-rural high-cost support than the other principles, and should they be given greater weight than the remaining principles? We note in this regard that, although some commenters in this proceeding discussed all the section 254(b) principles in relationship to the non-rural support mechanism, two principles—reasonable comparability and affordability—received the most attention.

18. We seek comment on whether the Commission should define “affordable rates,” as well as reasonably comparable rates.⁶⁴ Although the Commission has not explicitly linked the goal of ensuring reasonably comparable rural and urban rates to the 254(b)(1) principle of affordability, it has explained that a “major objective of high-cost universal service support is to help ensure affordable access to telecommunications services to consumers living in areas where the cost of providing such services would otherwise be prohibitively high.”⁶⁵ Some commenters in this proceeding argued that the non-rural support mechanism could satisfy the principle of affordability if rural rates are reasonably comparable to urban rates.⁶⁶ On the other hand, some commenters propose that the Commission specifically define an affordability benchmark, for example by using consumer expenditure data and/or household income data.⁶⁷

19. If the Commission determines that it should set an affordability benchmark, should it collect additional rate data? The Commission currently conducts an annual survey of incumbent LEC

⁶² *Id.* at 1234. The court agreed with the petitioners who argued that the Commission’s definition of sufficient is impermissible because it ignores all but one principle enumerated in section 254(b).

⁶³ *Qwest II*, 398 F.3d at 1234.

⁶⁴ Section 254(b)(1) provides that “[q]uality services should be available at just, reasonable, and affordable rates.” 47 U.S.C. § 254(b)(3).

⁶⁵ *Remand NPRM*, 20 FCC Rcd at 19736, para. 9.

⁶⁶ *See, e.g.*, Reply Comments of BellSouth Corporation, CC Docket No. 96-45, WC Docket No. 05-337, 25 (filed May 26, 2006) (BellSouth Reply Comments) (“Reasonable comparability, if achieved and maintained, inherently addresses ‘affordability.’”); Comments of CTIA – The Wireless Association®, CC Docket No. 96-45, WC Docket No. 05-337, 4 (filed Mar. 27, 2006) (CTIA Comments) (“Taking into account the other Section 254(b) principles, a high-cost support mechanism satisfies the ‘affordability’ principle if rural rates are reasonably comparable, but not necessarily the same, with urban rates.”); Reply Comments of the National Association of State Utility Consumer Advocates, CC Docket No. 96-45, WC Docket No. 05-337, 18 (filed May 26, 2006) (NASUCA Reply Comments) (“The key thing is for the Commission to recognize, as argued by NASUCA and others, that reasonably comparable rates will satisfy the affordability principle, so there is no need to focus on affordability.”) (citations omitted); Reply Comments of Nebraska Rural Independent Companies, CC Docket No. 96-45, WC Docket No. 05-337, 6-7 (filed Mar. 27, 2006) (Nebraska Companies Comments) (“Competition in urban areas tends to ensure that rates are generally not priced above cost. This, given the relatively low cost of providing service in urban areas, ensuring that rates in rural areas are reasonably comparable to rates in urban areas, also ensures that those rural rates are affordable.”).

⁶⁷ *See, e.g.*, Comments of AT&T, CC Docket No. 96-45, 23-32 (filed Mar. 27, 2006) (AT&T Comments); Comments of Qwest Communications International, Inc., CC Docket No. 96-45, 22-29 (filed Mar. 27, 2006) (Qwest Comments).

local telephone service rates in 95 urban areas.⁶⁸ Does the Commission need additional rate data to define affordability in today's telecommunications marketplace? Most consumers do not purchase only local service, but purchase bundles of telecommunications services from one or more providers. According to the Commission's most recent data, there are more wireless subscribers than wireline switched access lines.⁶⁹ According to a recent survey released by the Centers for Disease Control and Prevention (CDC), more than one out of every six American homes (17.5 percent) had only wireless telephones during the first half of 2008.⁷⁰ Consumers increasingly are purchasing packages of services that include not only unlimited nationwide calling, but also broadband Internet access and video services. We seek comment on whether the Commission should consider a broader range of rates in determining whether rates are affordable and reasonably comparable. How would the Commission determine the affordability of bundled services that include wireless, broadband Internet access, and/or video services? Should the Commission collect rate data from the broader range of entities that provide these services, including incumbent LECs, ETCs, competitive ETCs, wireless providers, cable operators, others?

20. If the Commission defines affordable rates for purposes of the non-rural support mechanism, should it also consider the burden on universal service contributors when determining whether rates are affordable? The Commission previously found that the principle of sufficiency means that non-rural high-cost support should be "only as large as necessary" to meet the statutory goal.⁷¹ Although the U.S. Court of the Appeals for the Fifth Circuit found that "excessive funding may itself violate the sufficiency requirements of the [1996] Act,"⁷² the Tenth Circuit linked the idea that the amount of support should only be as large as necessary to the principle of affordability, rather than sufficiency.⁷³ The Tenth Circuit explained that "excessive subsidization arguably may affect the affordability of telecommunications services for unsubsidized users, thus violating the principle in [section] 254(b)(1)."⁷⁴ Whether or not we consider the burden on contributors in defining affordability, commenters should address the effect on the universal service fund of any proposal they advocate.

C. Funding Mechanism

21. We seek comment on how "to craft a support mechanism taking into account all the factors that Congress identified in drafting the Act and [the Commission's] statutory obligation to preserve *and* advance universal service," as directed by the court.⁷⁵ We also seek comment on the relationship between the Commission's resolution of the issues in this remand proceeding and more comprehensive reform of the high-cost universal service support system. One approach would be to

⁶⁸ See Reference Book of Rates, Price Indices, and Household Expenditures for Telephone Service, Industry Analysis and Technology Division, Wireline Competition Bureau (2008) (*2008 Reference Book*).

⁶⁹ See Local Telephone Competition: Status as of December 31, 2007, Industry Analysis and Technology Division, Wireline Competition Bureau, at Tables 7, 14 (Sept. 2007). According to the most recent data released by the Commission, there were 129,729,167 wireline end-user switched access lines as of December 31, 2007, and 249,235,715 mobile wireless telephone subscribers. See *id.* In addition, 18 percent of wireline end-user lines are provided by competitive LECs, whose rates are not reflected in the Commission's survey of incumbent LEC rates. See *id.* at Table 7; *2008 Reference Book* at I-2.

⁷⁰ See Stephen J. Blumberg, and Julian V. Luke, Division of Health Interview Statistics, National Center for Health Statistics, CDC, Wireless Substitution: Early Release of Estimates from the National Health Interview Survey, January-June 2008, at <http://www.cdc.gov/nchs/data/nhis/earlyrelease/wireless200812.pdf>.

⁷¹ See *Order on Remand*, 18 FCC Rcd at 22578, para. 30.

⁷² *Alenco v. FCC*, 201 F.3d 608, 620 (5th Cir. 2000).

⁷³ *Qwest II*, 398 F.3d at 1234; see also *Qwest I*, 258 F.3d at 1200.

⁷⁴ *Qwest II*, 398 F.3d at 1234.

⁷⁵ *Id.* (emphasis in original).

modify the existing mechanism for non-rural carriers pending comprehensive reform. Another approach would be to replace the current non-rural mechanism with a new mechanism that could become a basis on which to craft more comprehensive reform. Yet another approach would be to move forward with a more comprehensive reform of high-cost support. We seek comment on which of these approaches or other approaches to be suggested by commenters the Commission should pursue at this time. Our decision here should also be consistent with our longer term goal of developing a comprehensive national broadband plan. We also seek comment on the impact of any increases in non-rural support on the size of the fund and on our ability to achieve reform in other areas. Should the Commission phase-in any increases in non-rural support? We ask parties to suggest options for offsetting any potential increases in non-rural support.

22. In Section III above we seek comment on proposals to modify the existing non-rural mechanism, which take fundamentally different approaches. Some proposals do not change the methodology and underlying assumptions about the federal and state roles in supporting universal service. For example, the Vermont and Maine proposal would lower the benchmark used to calculate support, but continue to compare statewide average costs to the benchmark.⁷⁶ Qwest also proposes a lower benchmark, but it would eliminate statewide averaging and compare wire center costs to the benchmark, which results in considerably higher support levels.⁷⁷ The Commission explained that “[s]tatewide averaging effectively enables the state to support its high-cost wire centers with funds from its low-cost wire centers though implicit or explicit support mechanisms, rather than unnecessarily shifting funds from other states.”⁷⁸ In *Qwest I*, the court rejected the argument that the Commission alone must support the full costs of universal service,⁷⁹ and said that it saw “nothing in [section] 254 requiring the FCC to replace implicit support previously provided by the states with explicit federal support.”⁸⁰ In *Qwest II*, the court rejected the argument that section 254 requires the states to replace implicit subsidies with explicit subsidies, and found that the Commission had not acted unlawfully by failing to ensure that the states transition to an explicit subsidy system.⁸¹ We seek comment on whether the Commission should re-evaluate its conception of the state and federal roles in providing universal service support, and consider whether it should now replace implicit state support with explicit federal support.

23. The court in *Qwest II* found that, in pairing rates with costs in its non-rural high-cost support funding mechanism the Commission had not “empirically demonstrat[ed] a relationship between the costs and rates.”⁸² We seek comment on how best to empirically demonstrate this relationship. Could the Commission use the non-rural cost model to approximate urban and non-urban rates? Should any such estimation of rates take into account the availability of explicit and implicit state-based support mechanisms, such as state universal service funds and intrastate access charge revenue? How should

⁷⁶ See *supra* para. 10. Maine recently suggested adjusting the benchmark to 120 or 125 percent of urban rates, making certain changes to the Commission’s cost model, and adding a screen for payment of additional support, such as density or largest city criterion, or regulatory scrutiny. See Letter from Elisabeth H. Ross, Counsel for Vermont Public Service Board, to Marlene Dortch, Secretary, Federal Communications Commission, WC Docket No. 05-337 (filed Mar. 10, 2009).

⁷⁷ See *supra* para. 9.

⁷⁸ *Order on Remand*, 18 FCC Rcd at 22573, para. 24.

⁷⁹ *Qwest I*, 258 F.3d at 1203.

⁸⁰ *Id.* at 1204.

⁸¹ *Qwest II*, 398 F.3d 1230-33 (“In keeping with the Act, Congress intended that the states retain significant oversight and authority and did not dictate an arbitrary time line for transition from one system to another. ... Nor did Congress expressly foreclose the possibility of the continued existence of state implicit support mechanisms that function effectively to preserve and advance universal service.”) (citation omitted).

⁸² *Id.* at 1237.

urban and non-urban areas be identified?

24. We seek comment on the extent to which we should continue to use the Commission's forward-looking cost model in determining high-cost support for non-rural carriers without updating, changing, or replacing the model. Many of the inputs in the model have not been updated since they were adopted a decade ago.⁸³ The Commission last updated the lines used in the model to estimate costs in 2003 (using year-end 2002 lines), and has been basing non-rural high-cost support on these cost estimates since 2004.⁸⁴ Updating lines in the current model is problematic because the customer location data has not been updated, and the methodology used to estimate special access line costs does not accurately reflect the costs of high-capacity lines. In addition, the Commission's model estimates the costs of constructing and operating a wireline telephone network. Since that time, the Internet and the increasing use of wireless and broadband technologies have transformed the way the world communicates. CostQuest identifies many of the issues that have been raised about the Commission's cost model and describes how the problems could be addressed using a more advanced cost model. Although Embarq proposes using the Commission's cost model to identify relative estimated loop costs, it suggests doing so "one last time" and "using a superior model or some other mechanism" in the future.⁸⁵

25. We ask that parties advocating that the Commission update its cost model propose an efficient, timely, and cost effective process for doing so. As parties involved in the development of the Commission's current model well know, it was an extremely time-consuming process, with several rounds of comments, innumerable *ex parte* meetings, and multiple workshops over many years.

26. If the Commission does not update its cost model, what alternatives could it use to determine high-cost support for non-rural carriers? Would it be appropriate to return to using embedded costs given the Commission's previous statements concerning the use of forward-looking economic costs versus embedded costs? In addition, would it be feasible to use embedded costs in light of the cost allocation relief granted to several of the largest non-rural LECs in forbearance proceedings?⁸⁶

27. Alternatively, could the Commission use a simplified model or algorithm to distribute non-rural high-cost support? Such a model could incorporate the key factors that determine the relative cost of serving various geographic areas as demonstrated by geographic information systems (GIS) technology. Possible factors could include population density, terrain, and climate conditions. The analysis could also include income or other indicators of potential for additional revenue. We specifically seek comment on what inputs—both carrier-specific and non-carrier-specific—should be used, and how the relative weights should be determined. Also, could such a model be used to determine how much non-rural high-cost support should be disbursed, or would its use be limited to distributing a set amount

⁸³ *Federal-State Joint Board on Universal Service, Forward-Looking Mechanism for High-Cost Support for Non-Rural LECs*, CC Docket Nos. 96-45, 97-160, Tenth Report and Order, 14 FCC Rcd 20156 (1999) (selecting input values for the non-rural high-cost support cost model), *aff'd Qwest I*, 258 F.3d at 1206.

⁸⁴ Non-rural carriers file wire center line count data quarterly, and per-line support amounts based on the model's cost estimates are adjusted to reflect updated lines.

⁸⁵ See BCS Plan at 27.

⁸⁶ See *Petition of AT&T Inc. for Forbearance under 47 U.S.C. § 160 from Enforcement of Certain of the Commission's Cost Assignment Rules*, WC Docket Nos. 07-21, 05-342, Memorandum Opinion and Order, 23 FCC Rcd 7302 (2008); *Service Quality, Customer Satisfaction, Infrastructure and Operating Data Gathering*, WC Docket Nos. 08-190, 07-139, 07-204, 07-273, 07-21, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 23 FCC Rcd 13647 (2008); *Petition of Qwest Corporation for Forbearance from Enforcement of the Commission's ARMIS and 492A Reporting Requirements Pursuant to 47 U.S.C. § 160(c)*; *Petition of Verizon for Forbearance Under 47 U.S.C. § 160(c) From Enforcement of Certain of the Commission's Recordkeeping and Reporting Requirements*, WC Docket Nos. 07-204, 07-73, Memorandum Opinion and Order, FCC 08-271 (rel. Dec. 12, 2008).

of universal service support?

28. Finally, we seek comment on the relationship of any modifications to the non-rural high-cost support mechanism to our broadband policies. On March 25, 2009, the Wireline Competition Bureau and the Wireless Telecommunications Bureau issued a public notice seeking comment on Congress's directive in the 2008 Farm Bill that the Chairman of the Commission develop, in consultation with the Secretary of Agriculture, a comprehensive rural broadband strategy.⁸⁷ More recently, Congress required that the Commission develop a comprehensive national broadband plan.⁸⁸ How can the Commission accomplish these broadband initiatives in a manner that is consistent with its directive to craft a revised non-rural high-cost support mechanism?

V. PROCEDURAL MATTERS

A. *Ex Parte* Presentations

29. This proceeding shall be treated as a "permit-but-disclose" proceeding in accordance with the Commission's *ex parte* rules.⁸⁹ Persons making oral *ex parte* presentations are reminded that memoranda summarizing the presentations must contain summaries of the substance of the presentations and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented is generally required.⁹⁰ Other requirements pertaining to oral and written presentations are set forth in section 1.1206(b) of the Commission's rules.⁹¹

B. Comment Filing Procedures

30. Pursuant to sections 1.430, 1.415 and 1.419 of the Commission's rules,⁹² interested parties may file comments and reply comments on or before the dates indicated on the first page of this document. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies.⁹³

- Electronic Filers: Comments may be filed electronically using the Internet by accessing the ECFS: <http://www.fcc.gov/cgb/ecfs/>. Filers should follow the instructions provided on the website for submitting comments.
 - For ECFS filers, if multiple docket or rulemaking numbers appear in the caption of this proceeding, filers must transmit one electronic copy of the comments for each docket or rulemaking number referenced in the caption. In completing the transmittal screen, filers should include their full name, U.S. 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, filers should send an e-mail to ecfs@fcc.gov, and include the following words in the body of the message, "get form." A sample form and directions will be sent in response.

⁸⁷ *Comment Date Established for Report on Rural Broadband Strategy*, GN Docket No. 09-29, Public Notice, DA 09-561 (Wireline Comp. Bur./Wireless Tel. Bur., rel. Mar. 10, 2009); Food, Conservation, and Energy Act of 2008, Pub. L. 110-246, 122 Stat. 1651 (Jun. 18, 2008) (2008 Farm Bill).

⁸⁸ *See id.* at 1; American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115 (2009) (Recovery Act).

⁸⁹ 47 C.F.R. §§ 1.1200-1.1216.

⁹⁰ 47 C.F.R. § 1.1206(b)(2).

⁹¹ 47 C.F.R. § 1.1206(b).

⁹² 47 C.F.R. §§ 1.430, 1.415, 1.419.

⁹³ *See Electronic Filing of Documents in Rulemaking Proceedings*, GC Docket No. 97-115, Report and Order, 13 FCC Red 11322 (1998).

- Paper Filers: 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 appears in the caption of this proceeding, filers must submit two additional copies for each additional docket or rulemaking number.
- Filings can be sent by hand or messenger delivery, by commercial overnight courier, or by first-class or overnight U.S. Postal Service mail (although we continue to experience delays in receiving U.S. Postal Service mail). All filings must be addressed to the Commission's Secretary, Office of the Secretary, Federal Communications Commission.
 - The Commission's contractor will receive hand-delivered or messenger-delivered paper filings for the Commission's Secretary at 236 Massachusetts Avenue, NE, Suite 110, Washington, DC 20002. The filing hours at this location are 8:00 a.m. to 7:00 p.m. All hand deliveries must be held together with rubber bands or fasteners. Any envelopes must be disposed of before entering the building.
 - Commercial overnight mail (other than U.S. Postal Service Express Mail and Priority Mail) must be sent to 9300 East Hampton Drive, Capitol Heights, MD 20743.
 - U.S. Postal Service first-class, Express, and Priority mail should be addressed to 445 12th Street, SW, Washington, DC 20554.

31. In addition, one copy of each pleading must be sent to the Commission's duplicating contractor, Best Copy and Printing, Inc, 445 12th Street, SW, Room CY-B402, Washington, DC 20554; website: www.bcpiweb.com; phone: 1-800-378-3160. Furthermore, one copy of each pleading must be sent to Antoinette Stevens, Telecommunications Access Policy Division, Wireline Competition Bureau, 445 12th Street, SW, Room 5-B521, Washington, DC 20554; e-mail: antoinette.stevens@fcc.gov.

32. Filings and comments are also available for public inspection and copying during regular business hours at the FCC Reference Information Center, Portals II, 445 12th Street, S.W., Room CY-A257, Washington, D.C., 20554. Copies may also be purchased from the Commission's duplicating contractor, BCPI, 445 12th Street, S.W., Room CY-B402, Washington, D.C. 20554. Customers may contact BCPI through its website: www.bcpiweb.com, by e-mail at fcc@bcpiweb.com, by telephone at (202) 488-5300 or (800) 378-3160 (voice), (202) 488-5562 (tty), or by facsimile at (202) 488-5563.

33. To request materials in accessible formats for people with disabilities (Braille, large print, electronic files, audio format), send an e-mail to fcc504@fcc.gov or call the Consumer & Governmental Affairs Bureau at 202-418-0530 (voice) or 202-418-0432 (TTY). Contact the Commission to request reasonable accommodations for filing comments (accessible format documents, sign language interpreters, CART, etc.) by e-mail: FCC504@fcc.gov; phone: (202) 418-0530 or TTY: (202) 418-0432.

34. For further information regarding this proceeding, contact Katie King, Special Counsel, Telecommunications Access Policy Division, Wireline Competition Bureau at (202) 418-7491, or katie.king@fcc.gov, or Ted Burmeister, Attorney Advisor, Telecommunications Access Policy Division, Wireline Competition Bureau at (202) 418-7389, or theodore.burmeister@fcc.gov.

VI. ORDERING CLAUSES

35. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 1, 4(i), 201-205, 214, 254, and 403 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 201-205, 214, 254, and 403, this notice of inquiry IS ADOPTED.

FEDERAL COMMUNICATIONS COMMISSION

Marlene H. Dortch
Secretary

**STATEMENT OF
ACTING CHAIRMAN MICHAEL J. COPPS**

Re: High-Cost Universal Service Support; Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45.

Universal Service policy is built on the principle that all of us benefit when more of us are connected. The principle resides at the core of the Telecommunications Act. And Congress made clear that the Commission must be working to ensure that all Americans—rural, urban and everything in between—have access to reasonably comparable services at reasonably comparable rates. Clearly, at this time, for the future of our country, it is crucial that we strive to preserve and advance Universal Service policy.

Today, we are taking a firm step on a deliberate timeline for considering the High Cost Universal Service mechanism for non-rural providers. Comments elicited from the Notice of Inquiry will refresh the record and bring the matter of non-rural High Cost Universal Service support up-to-date. The Commission will conclude with a final order by the middle of April 2010. By that time, we will have had the benefit of completing the National Broadband Plan, which will further inform us when it comes to advancing universal service. I look forward to reviewing the comments and completing this matter once and for all. Today's action puts us on the road to achieve this.

**STATEMENT OF
COMMISSIONER JONATHAN S. ADELSTEIN**

Re: High-Cost Universal Service Support; Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45.

Universal service has long been at the heart of telecommunications policy. The resulting benefits – economic and social, in health care and education, among many others – accrue to us all, no matter where we live. So I am pleased today to support this Notice of Inquiry that will respond to the Tenth Circuit Court of Appeals review of the high-cost support mechanism for non-rural carriers. I support this broad inquiry into the merits of several plans to modify the existing mechanism and to define key statutory terms that are essential to carrying out Congress' wish that we preserve and advance the fund. By working with all stakeholders - states, carriers, and other agencies – I am confident we will ensure the fund continues to bring the benefits of universal service to us all, no matter where we live. And yet today's action is just one piece of the larger universal service and broadband puzzle. I am pleased that this NOI seeks comment on the effects of high-cost mechanism reform on both the national broadband plan and the 2008 Farm Bill's comprehensive rural broadband strategy. Through these different proceedings, the Commission is taking essential steps to ensure that universal service continues to meet our communications challenges.

**STATEMENT OF
COMMISSIONER ROBERT M. McDOWELL**

Re: High-Cost Universal Service Support; Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45.

The Commission has for too long avoided answering the fundamental questions raised on remand by the United States Court of Appeals for the Tenth Circuit (Tenth Circuit) regarding the high-cost universal service support mechanism for non-rural carriers. I was therefore pleased when the Commission committed to release a notice of inquiry no later than April 8, 2009, issue a further NPRM no later than December 15, 2009, and release a final order that responds to the remand no later than April 16, 2010.

With this Notice of Inquiry we have taken the first step towards fulfilling our commitment. I have consistently stated that, while the Universal Service system has been instrumental in keeping Americans connected and improving their quality of life, this system is in dire need of comprehensive reform. I have maintained that we must follow five principles when considering reforms to the Universal Service Fund. We must: (1) slow the growth of the Fund; (2) permanently broaden the base of contributors; (3) reduce the contribution burden for all, if possible; (4) ensure competitive neutrality; and (5) eliminate waste, fraud and abuse. I will remain mindful of these principles as we consider the record in this proceeding.

I look forward to working with my colleagues to satisfactorily resolve the questions posed to us by the Tenth Circuit and to continuing our work towards fundamental reform of the intercarrier compensation and Universal Service systems.