

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

In the Matter of)	
)	
Connect America Fund)	WC Docket No. 10-90
)	
Developing a Unified Intercarrier Compensation Regime)	CC Docket No. 01-92
)	
Establishing Just and Reasonable Rates for Local Exchange Carriers)	WC Docket No. 07-135
)	
FairPoint Communications, Inc. Petition for Declaratory Ruling)	

ORDER AND DECLARATORY RULING

Adopted: April 18, 2018

Released: April 19, 2018

By the Commission:

I. INTRODUCTION

1. In this Order and Declaratory Ruling, we address a legacy support issue arising from the ongoing reform and modernization of the universal service fund (USF) and intercarrier compensation (ICC) systems. Specifically, FairPoint Communications, Inc. (FairPoint) asks us to find that the National Exchange Carrier Association (NECA) incorrectly deducted Local Switching Support (LSS) as double recovery in calculating the amount that FairPoint’s rate-of-return affiliates may obtain from the transitional recovery mechanism under the Commission’s rules.¹ We find that Connect America Fund (CAF) Phase II support generally does not include duplicative LSS recovery and, therefore, grant FairPoint’s petition. We also waive on our own motion an additional imputation requirement² of the Commission’s rules to the extent necessary for FairPoint and other similarly situated carriers to obtain the funds they should have received from the recovery mechanism since January 1, 2015.

II. BACKGROUND

2. In the *USF/ICC Transformation Order*, the Commission comprehensively reformed and modernized the USF and ICC systems.³ The existing systems, the Commission explained, were based “on decades-old assumptions that fail[ed] to reflect today’s networks” and were “ill equipped to address the universal service challenges raised by broadband, mobility, and the transition to Internet Protocol (IP) networks.”⁴ Among other reforms, the Commission eliminated several high-cost support mechanisms that had outlived their usefulness and created the Connect America Fund to take their place.

¹ FairPoint Communications, Inc., Petition for Declaratory Ruling, WC Docket No. 10-90 et al., at iii, 22 (filed Dec. 10, 2015) (Petition).

² 47 CFR 51.917(f)(2).

³ *Id.* at 17667, para. 1.

⁴ *Id.* at 17669, para. 6.

3. The underlying petition concerns one of the legacy support mechanisms the Commission decided to terminate. LSS historically allowed incumbent local exchange carriers (LECs) serving 50,000 or fewer access lines to allocate a larger percentage of their switching costs to the interstate jurisdiction and thereby recover those costs through the federal universal service fund.⁵ This mechanism recognized that traditional circuit switches, based on specialized hardware, imposed relatively higher switching costs on smaller carriers than on larger carriers.⁶ The evolution from circuit-switched networks to IP-based networks (which allow less expensive soft switches that can better meet the needs of smaller carriers) undercut the need, however, to maintain LSS as a standalone support mechanism.⁷ Thus, the Commission eliminated LSS effective July 1, 2012.⁸

4. At the same time, the Commission decided that limited recovery of the costs previously covered by LSS would be available, in annually diminishing amounts, through ICC reform for rate-of-return carriers.⁹ Specifically, the *USF/ICC Transformation Order* created a transitional mechanism, CAF ICC transition support, to provide partial recovery for the ICC revenue that the rate-of-return carriers would lose. Within this new recovery mechanism, the amount of “Eligible Recovery” for rate-of-return carriers depends in part on their “2011 interstate switched access revenue requirement,” which included switching costs previously covered by LSS.¹⁰ Once their Eligible Recovery has been determined, rate-of-return carriers can recover some or all of the amount “from their end users through a monthly fixed charge called an ARC” (Access Recovery Charge).¹¹ “[T]o the extent their Eligible Recovery exceeds their permitted ARCs,” carriers may obtain support from CAF ICC.¹²

5. Like rate-of-return carriers, price cap carriers serving 50,000 or fewer access lines also recovered an amount based on their LSS. In the *USF/ICC Transformation Order*, the Commission reformed high-cost support for price cap carriers in two phases.¹³ In CAF Phase I, the Commission froze support under the existing high-cost support mechanisms — including LSS — for price cap carriers and their rate-of-return affiliates.¹⁴ Thus, price cap carriers and their rate-of-return affiliates received legacy LSS as part of CAF Phase I frozen support. In Phase II, the Commission offered these same companies a state-level support amount calculated by the Connect America Cost Model (CAM) in exchange for a commitment to offer voice and broadband service to a set number of locations across the eligible census blocks in each state.¹⁵

6. FairPoint is an incumbent LEC that operates as a price cap carrier in three states and as a rate-of-return carrier in 15 states.¹⁶ FairPoint’s rate-of-return affiliates participate in NECA’s access

⁵ *Id.* at 17758, para. 253.

⁶ *Id.*

⁷ *Id.* at 17758-60, paras. 253-57.

⁸ *Id.* at 17760, para. 257.

⁹ *Id.* at 17760, paras. 256-57.

¹⁰ 47 CFR § 51.917(d)(1); *USF/ICC Transformation Order*, 26 FCC Rcd at 17967, para. 868.

¹¹ *USF/ICC Transformation Order*, 26 FCC Rcd at 17958, para. 852; 47 CFR § 51.917(e).

¹² *USF/ICC Transformation Order*, 26 FCC Rcd at 17961, para. 853; 47 CFR § 51.917(f). Any recovery from CAF ICC support cannot exceed the rate-of-return carrier’s remaining Eligible Recovery after “imput[ing] the maximum charges it could have assessed” upon its end users through ARCs. 47 CFR § 51.917(f)(2).

¹³ *USF/ICC Transformation Order*, 26 FCC Rcd at 17709, para. 116.

¹⁴ *Id.* at 17712, para. 128-29.

¹⁵ *Id.* at 17727, para. 166.

¹⁶ Petition at 3. In Maine, FairPoint has both price cap and rate-of-return affiliates. Petition at 3 n.5. FairPoint has since merged with Consolidated Communications Holdings, Inc. See Consolidated Communications, *Consolidated*

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charge pools, and NECA calculates the Eligible Recovery amounts for FairPoint's participating study areas.¹⁷ All of FairPoint's rate-of-return affiliates received Phase I frozen support (including LSS), and all were further eligible to participate in the ICC recovery mechanism because, as noted above, the Commission determined that rate-of-return affiliates of price cap carriers would be treated as price cap carriers for USF purposes and as rate-of-return carriers for ICC purposes.¹⁸ Thus, these affiliates could possibly recover LSS-based support twice — once through Phase I frozen support and once through the ICC recovery mechanism.

7. To close that loophole, the Commission's rules expressly prohibit double recovery of costs covered by the ICC recovery mechanism: "If a Rate-of-Return Carrier recovers any costs or revenues that are already being recovered as Eligible Recovery . . . from another source, that carrier's ability to recover reduced switched access revenue from Access Recovery Charges or the Connect America Fund shall be reduced to the extent it receives duplicative recovery."¹⁹ The rules further instruct that "[a]ny duplicative recovery shall be reflected as a reduction to a carrier's Eligible Recovery."²⁰

8. Beginning in July 2012, NECA applied these provisions and reduced FairPoint's Eligible Recovery in an amount corresponding to the company's 2011 legacy LSS.²¹ In subsequent years, NECA effected a 5 percent annual reduction to the LSS "offset" to track the Commission-mandated annual reduction in Eligible Recovery.²² FairPoint does not dispute the appropriateness of this reduction for the period when it received CAF Phase I frozen support, conceding that NECA's reduction "made sense" to avoid duplicative recovery.²³

9. FairPoint contends, however, that NECA misapplied the Commission's rules by continuing the LSS-based reductions after its Phase I support ended. FairPoint accepted over \$37 million in annual Phase II model-based support, retroactive to January 1, 2015, in 14 states, so it no longer received Phase I support for those states after 2014.²⁴ In 12 of the 14 states for which FairPoint accepted Phase II model-based support, FairPoint has rate-of-return carrier operations.²⁵ In its petition, FairPoint

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Communications Completes FairPoint Acquisition (July 3, 2017), <https://www.consolidated.com/about-us/news/article-detail/id/556/consolidated-communications-completes-fairpoint-acquisition>.

¹⁷ Comments of the National Exchange Carrier Association, Inc., WC Docket No. 10-90 et al., at 2 (filed Jan. 14, 2016) (NECA Comments).

¹⁸ *USF/ICC Transformation Order*, 26 FCC Rcd at 17712, para. 128-29.

¹⁹ 47 CFR § 51.917(d)(1)(vii).

²⁰ *Id.*

²¹ NECA Comments at 3.

²² See 47 CFR § 51.917(d)(1) (calculating Eligible Recovery by first multiplying the 2011 Base Period Revenue by the Baseline Adjustment Factor, which decreases 5 percent each year, and then subtracting other figures).

²³ Petition at 19.

²⁴ *Wireline Competition Bureau Authorizes FairPoint to Receive Over \$37 Million in Connect America Phase II Support in 14 States*, Public Notice, 30 FCC Rcd 8435 (WCB 2015). FairPoint accepted support in Alabama, Florida, Illinois, Maine, Massachusetts, Missouri, New Hampshire, New York, Ohio, Oklahoma, Pennsylvania, Vermont, Virginia, and Washington. *Id.* FairPoint declined Phase II model-based support in Colorado and Kansas and continues to receive Phase I frozen support in those states. *Id.* at 8435 n.2. In its petition, FairPoint claims to have accepted Phase II support in 15 states, not 14. Petition at 9. However, for purposes of the Phase II model-based support offer, a study area that FairPoint serves that covers part of Georgia is associated with Florida. Petition at Attach. A.

²⁵ See Letter from Karen Brinkmann, Counsel, FairPoint Communications, Inc., to Marlene H. Dortch, Secretary, FCC, Attach. at 3 (filed Mar. 17, 2016) (FairPoint Mar. 17, 2016 *Ex Parte* Letter). These states are Alabama,

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contends that NECA should stop reducing its Eligible Recovery in these states based on double recovery of LSS and alleges that deduction of LSS amounts has reduced its support by approximately \$4.2 million each year.²⁶ FairPoint seeks a declaratory ruling that NECA is not properly compensating it and asks us to direct NECA to correct its Eligible Recovery retroactive to January 1, 2015 and restore the LSS-related amounts that NECA deducted. FairPoint states that “[t]o the extent that CAF Phase II support includes any ‘duplicative’ switching-related support, that amount is *de minimis*,”²⁷ which FairPoint estimates to be approximately \$62,022 per year for all the FairPoint rate-of-return LECs combined.²⁸

10. The Wireline Competition Bureau (Bureau) sought comment on the Petition, and ITTA—The Voice of Mid-Size Communications Companies filed comments supporting FairPoint’s petition and the issuance of a declaratory ruling.²⁹ NECA also filed comments supporting the issuance of a declaratory ruling, claiming that “the rules governing such calculations are less than clear as applied to FairPoint’s particular circumstances.”³⁰ But NECA expressed no opinion on how the issue should be resolved.³¹ No party filed comments opposing FairPoint’s request.

III. DISCUSSION

11. We conclude that there generally is no duplicative recovery of LSS when rate-of-return affiliates of price cap carriers receive both CAF Phase II support and CAF ICC transition support. Accordingly, we grant FairPoint’s petition and direct NECA to correct FairPoint’s Eligible Recovery retroactive to January 1, 2015 and to restore deducted LSS-related amounts as appropriate.

12. CAF Phase II support covers forward-looking costs, not historical costs. In the *USF/ICC Transformation Order*, the Commission stated that rate-of-return affiliates of price cap carriers “in the future will receive support based on a *forward-looking* cost model rather than their embedded costs.”³² The Commission also noted that it was “set[ting] the stage for a full transition to a system where support in price cap territories is determined based on competitive bidding or the *forward-looking* costs of a modern multi-purpose network,”³³ and that it was beginning the process “of transitioning all high-cost support to *forward-looking* costs and market-based mechanisms, which will improve incentives for carriers to invest efficiently.”³⁴

13. Specifically, Phase II’s model-based support “estimate[s] the full average monthly

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Florida, Illinois, Maine, Massachusetts, Missouri, New York, Ohio, Oklahoma, Pennsylvania, Virginia, and Washington. *Id.*

²⁶ Petition at 10.

²⁷ Letter from Karen Brinkmann, Counsel, FairPoint Communications, Inc., to Marlene H. Dortch, Secretary, FCC, WC Docket No. 10-90 et al, at 2 (filed Mar. 3, 2017).

²⁸ Letter from Karen Brinkmann, Counsel, FairPoint Communications, Inc., to Marlene H. Dortch, Secretary, FCC, WC Docket No. 10-90 et al., Attach. at 10 (filed Apr. 22, 2016).

²⁹ *Wireline Competition Bureau Seeks Comment on FairPoint Communications, Inc. Petition for Declaratory Ruling Regarding the Application of Section 51.917 of the Commission’s Rules*, WC Docket No. 10-90 et al., Public Notice, 30 FCC Rcd 14291 (WCB 2015); Comments of ITTA—The Voice of Mid-Size Communications Companies, WC Docket No. 10-90 et al. (filed Jan. 19, 2016) (ITTA Comments).

³⁰ NECA Comments at 4.

³¹ *Id.* at 4-5.

³² *USF/ICC Transformation Order*, 26 FCC Rcd at 17713, para. 129, n.203 (emphasis added).

³³ *Id.* at 17713, para. 129 (emphasis added).

³⁴ *Id.* at 17723, para. 151 (emphasis added).

amount of operating and maintaining an efficient modern network.”³⁵ In designing the CAM, the Bureau decided “to estimate the costs of a FTTP [fiber-to-the-premises] network rather than a twisted copper pair DSL network” because doing so is “the best approach to meet the Commission’s directive that we adopt a forward-looking cost model.”³⁶ “If an efficient carrier were to design a new wireline network today, it would be an all Internet protocol (IP) fiber network, not a circuit switched copper network, because such a network would be cheaper and more scalable over time.”³⁷ Thus, the CAM models costs “based on an IP-based FTTP network of a wireline telecommunications provider.”

14. Crucially, the forward-looking CAM did not include the historical costs associated with LSS because the rationale for providing LSS support had become outdated in light of modern IP-based networks. LSS existed because “traditional circuit switches, which were based on specialized hardware, were relatively expensive for the smallest of carriers because such switches were not easily scaled to the size of the carrier.”³⁸ So when the switch to IP-based networks allowed small rate-of-return carriers to purchase “soft switches and routers which tend to be cheaper and more efficiently scaled to smaller operating sizes,”³⁹ the Commission “conclude[d] that it [wa]s time to end LSS as a stand-alone universal service support mechanism.”⁴⁰

15. We therefore conclude that Phase II support is not directly traceable to either LSS or the historical costs that justified it. In this aspect, Phase II support plainly differs from Phase I frozen support, which expressly included legacy LSS as one revenue source that continued to flow.⁴¹

16. Further, our ruling today is consistent with the Commission’s decision to allow rate-of-return carriers electing to receive Alternative Connect America Cost Model (A-CAM) support to include legacy LSS when calculating their Eligible Recovery. In 2016, the Commission adopted reforms for rate-of-return carriers that are not affiliates of price cap carriers, including giving such carriers the option of electing to receive support calculated using A-CAM in exchange for meeting defined broadband service milestones.⁴² These non-affiliated rate-of-return carriers receive both model-based high-cost support as well as transitional ICC support, without a deduction for legacy LSS from the carriers’ transitional ICC support. We agree with FairPoint that its rate-of-return affiliates should receive the same treatment.

17. Accordingly, we declare that, in states where a rate-of-return affiliate of a price cap carrier is receiving Phase II support, its Eligible Recovery should not be reduced to avoid duplicative recovery stemming from legacy LSS. We direct NECA to stop reducing FairPoint’s and other similarly situated carriers’ Eligible Recovery for this reason going forward.⁴³ To the extent that FairPoint has

³⁵ *Connect America Fund et al.*, Report and Order, 28 FCC Rcd 5301, 5307, para. 11 (WCB 2013).

³⁶ *Id.* at 5314-16, para. 33.

³⁷ *Id.*

³⁸ *USF/ICC Transformation Order*, 26 FCC Rcd at 17758-59, para. 253.

³⁹ *Id.*

⁴⁰ *Id.* at 17760, para. 257.

⁴¹ *Id.* at 17712, para. 128-29.

⁴² *Connect America Fund et al.*, Report and Order et al., 31 FCC Rcd 3087 (2016).

⁴³ The Bureau previously required Consolidated to update its filings to remove LSS from its Eligible Recovery amounts within 45 days of closing on its acquisition of Enventis. See *Connect America Fund et al.*, WC Docket No. 10-90 et al., Order, 29 FCC Rcd 11776, 11777, para. 4 (WCB 2014); *Notice of Non-Streamlined Domestic Section 214 Application Granted*, WC Docket No. 16-150, Public Notice, 31 FCC Rcd 7242 (WCB 2016) (approving transfer of control involving Consolidated, Mutual, and Winnebago); *Connect America Fund; Federal-State Joint Board on Universal Service; Joint Petition for Waiver of the Definition of “Study Area” of the Appendix-Glossary of Part 36 of the Commission’s Rules filed by Mutual Telephone Company of Sioux Center, Iowa d/b/a Premier Communications Winnebago Cooperative Telecom Association*, WC Docket No. 10-90, CC Docket No. 96-45,

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estimated support amounts that may cover duplicative local-switching costs, we direct NECA to reduce FairPoint's support by those amounts.⁴⁴

18. With respect to past years, affected rate-of-return affiliates "cannot charge a higher ARC retroactively" and so would have to recover the restored Eligible Recovery from CAF ICC support.⁴⁵ But simply raising their Eligible Recovery would not suffice to restore all the lost funds because the affiliates "would be required to impute a higher ARC charge in their revised calculations" for CAF ICC support.⁴⁶ Given our conclusion that payment of LSS does not constitute duplicative recovery, we find good cause to waive on our own motion the imputation requirement in section 51.917(f)(2) of the Commission's rules to the extent necessary to permit affected carriers to recover from CAF ICC the LSS amounts deducted beginning January 1, 2015 as appropriate.⁴⁷

19. We prescribe the following procedure for affected carriers to recover additional CAF ICC transition support from the Universal Service Administrative Company (USAC) consistent with our ruling. Any affected carrier shall file with the Commission in the Electronic Tariff Filing System corrected Tariff Review Plan (TRP) worksheets with amended Eligible Recovery amounts, as well as any required certifications. It shall then file a notice of its corrected TRP filing in the Electronic Comment Filing System (ECFS) in WC Docket No. 10-90 and email a copy of the notice to Richard Kwiatkowski, Richard.Kwiatkowski@fcc.gov. Any interested person objecting to the revised data shall file objections in WC Docket No. 10-90 within 21 days after the notice is filed; the Wireline Competition Bureau (Bureau) will then release a Public Notice in WC Docket No. 10-90 directing USAC to withhold payment while the Bureau resolves the objections. If no such Public Notice is released within 45 days of the request, USAC shall proceed to issue payment. We hereby delegate authority to the Bureau to determine and carry out appropriate procedures to resolve any objections.

IV. ORDERING CLAUSES

20. Accordingly, IT IS ORDERED, pursuant to sections 1, 4(i), 201, 202, and 254 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154(i), 201, 202, 254, and to section 1.2 of the Commission's rules, 47 C.F.R. § 1.2, that the petition for declaratory ruling filed by FairPoint Communications, Inc. on December 10, 2015 IS GRANTED to the extent described above.

21. IT IS FURTHER ORDERED, pursuant to section 1.3 of the Commission's rules, 47 C.F.R. § 1.3, that section 51.917(f)(2) of the Commission's rules, 47 C.F.R. § 51.917(f)(2), IS WAIVED to the extent described above.

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Order, 31 FCC Rcd 10683 (WCB 2016) (granting a joint petition from Mutual and Winnebago for waiver of the Commission's study area boundary freeze to accommodate their purchase of a rate-of-return affiliate from Consolidated).

⁴⁴ See *supra* para. 9.

⁴⁵ *Connect America Fund et al.*, Order, 31 FCC Rcd 12021, 12030, para. 25 (2016).

⁴⁶ *Id.*; NECA Comments at 5 n.11.

⁴⁷ Generally, the Commission's rules may be waived for good cause shown. 47 CFR § 1.3. The Commission may exercise its discretion to waive a rule where the particular facts make strict compliance inconsistent with the public interest. *Northeast Cellular Telephone Co. v. FCC*, 897 F.2d 1164, 1166 (D.C. Cir. 1990). In addition, the Commission may take into account considerations of hardship, equity, or more effective implementation of overall policy on an individual basis. *Id.* Waiver of the Commission's rules is appropriate if special circumstances warrant a deviation from the general rule, and such deviation will serve the public interest. *Id.*

22. IT IS FURTHER ORDERED, pursuant to sections 1.2 and 1.103 of the Commission's rules, 47 C.F.R. §§ 1.2, 1.103, that this Order and Declaratory Ruling IS ADOPTED and SHALL BE EFFECTIVE upon release.

FEDERAL COMMUNICATIONS COMMISSION

Marlene H. Dortch
Secretary