

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

In the Matter of
Federal-State Joint Board on
Universal Service
Multi-Association Group (MAG) Plan for
Regulation of Interstate Services of
Non-Price Cap Incumbent Local Exchange
Carriers and Interexchange Carriers
CC Docket No. 96-45
CC Docket No. 00-256

FOURTEENTH REPORT AND ORDER, TWENTY-SECOND ORDER ON
RECONSIDERATION, AND FURTHER NOTICE OF PROPOSED RULEMAKING
IN CC DOCKET NO. 96-45, AND REPORT AND ORDER IN CC DOCKET NO. 00-256

Adopted: May 10, 2001

Released: May 23, 2001

Comment Date: 30 days from publication in the Federal Register

Reply Comment Date: 60 days from publication in the Federal Register

By the Commission: Chairman Powell and Commissioner Ness issuing separate statements;
Commissioner Furchtgott-Roth concurring in the result.

TABLE OF CONTENTS

Paragraph

I. Introduction and Overview ..... 1
II. Executive Summary ..... 12
III. Background ..... 13
A. High-Cost Support for Rural Carriers ..... 13
B. The Act ..... 14
C. Prior Joint Board and Commission Actions ..... 15
D. Rural Task Force Recommendation ..... 17
E. Joint Board Recommended Decision ..... 21
IV. Discussion ..... 24
A. Consistency with Principles of the Act ..... 24
B. Modified Embedded Cost Mechanism ..... 31
1. The Indexed Cap on High-Cost Loop Fund and the Rural Growth Factor ..... 31

2.	National Average Loop Cost .....	54
3.	Corporate Operations Expenses.....	60
C.	Support Above the Cap.....	77
1.	Safety Net Additive .....	77
2.	Mergers and Acquisitions Cap and “Safety Valve” Mechanism .....	91
3.	Support in Study Areas with Competitive Eligible Telecommunications Carriers.....	120
D.	Disaggregation and Targeting of Support.....	136
E.	Duration of the Rural Task Force Plan.....	165
F.	Identification of Service Locations .....	178
G.	State Certification Under Section 254(e).....	185
H.	Advanced Services .....	194
I.	Interstate Access Universal Service Support for Rate-of-Return Carriers.....	202
V.	FURTHER NOTICE OF PROPOSED RULEMAKING.....	207
VI.	PROCEDURAL MATTERS .....	212
A.	Final Regulatory Flexibility Analysis .....	212
B.	Paperwork Reduction Act.....	237
C.	Effective Date of Final Rules.....	240
D.	Initial Regulatory Flexibility Analysis .....	241
E.	Initial Paperwork Reduction Act of 1995 Analysis.....	261
F.	Ex Parte.....	262
G.	Comment Filing Procedures.....	263
VII.	ORDERING CLAUSES.....	268

Appendix A – Final Rules

Appendix B – Comments in the Rural Task Force Proceeding

Appendix C – Comments in the MAG Proceeding

Appendix D – Corporate Operations Expense Limitation Chart

## I. INTRODUCTION AND OVERVIEW

1. In this Order, consistent with the recommendation of the Federal-State Joint Board on Universal Service (Joint Board), we modify our rules for providing high-cost universal service support to rural telephone companies for the next five years based upon the proposals made by the Rural Task Force.<sup>1</sup> We find that these modified rules strike a fair and reasonable balance among the universal service principles and goals enumerated in section 254 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996.<sup>2</sup> As the Commission continues to develop a long-term coordinated universal service plan, this five-year plan will provide predictable levels of support so that rural carriers can continue to provide affordable service in rural America, while ensuring that consumers in all areas of the nation, including rural areas, have access to affordable and quality telecommunications services.<sup>3</sup>

2. The Telecommunications Act of 1996 codified the Commission's historical commitment to promote universal service to ensure that all Americans have access to affordable, quality telecommunications services. Specifically, in section 254, Congress instructed the Commission, after consultation with the Joint Board, to establish specific, predictable, and sufficient mechanisms to preserve and advance universal service.<sup>4</sup> Moreover, Congress articulated a national goal that consumers in all regions of the nation, including rural, insular and high cost areas, should have access to telecommunications and information services at rates that are reasonably comparable to rates charged for similar services in urban areas.

3. Consistent with the will of Congress, we have taken numerous steps over the last four years to carry out these statutory directives and goals. Reforming the patchwork system of largely implicit universal subsidies that existed prior to the 1996 Act has not been an easy task. We have proceeded carefully in stages to provide interested stakeholders with an opportunity to express their competing views on how to resolve these vexing public policy issues. Our action today is an important step in completing

---

<sup>1</sup> See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision, FCC 00J-4 (Jt. Bd. rel. Dec. 22, 2000) (*Recommended Decision*); Letter from William R. Gillis, Chair, Rural Task Force, to Magalie Roman Salas, FCC, dated September 29, 2000 (Rural Task Force Recommendation or Recommendation). We also address proposals related to intrastate high-cost support made by the Multi-Association Group (MAG). The MAG plan is a comprehensive proposal for interstate access charge and universal service reform for non-price cap or rate-of-return carriers submitted to the Commission by four associations that represent rural carriers. See *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, CC Docket No. 98-77, *Prescribing the Authorized Rate of Return for Interstate Services of Local Exchange Carriers*, CC Docket No. 98-166, Notice of Proposed Rulemaking, 16 FCC Rcd 460 (2001) (*MAG NPRM*).

<sup>2</sup> Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996) (1996 Act). The 1996 Act amended the Communications Act of 1934. 47 U.S.C. §§ 151, *et seq.* (Communications Act or Act). References to section 254 in this Order refer to the universal service provisions of the 1996 Act, which are codified at 47 U.S.C. § 254 of the Act.

<sup>3</sup> In this Order, the terms "rural carrier" and "rural incumbent local exchange carrier" refer to incumbent local exchange carriers that meet the definition of a rural telephone company set forth in section 153(37) of the Act. 47 U.S.C. § 153(37). Under this definition, rural telephone companies are local exchange carriers that either serve study areas with fewer than 100,000 access lines or meet one of three additional criteria. We note that, "[a]lthough the Commission uses the rural telephone company definition to distinguish between rural and non-rural carriers for purposes of calculating universal service support, there is no statutory requirement that it do so." *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Forward-Looking Mechanism for High Cost Support for Non-Rural LECs*, CC Docket No. 97-160, Tenth Report and Order, 14 FCC Rcd 20156, 20358 para. 458 (1999) (*Tenth Report and Order*).

<sup>4</sup> 47 U.S.C. § 254.

the process begun in 1996 to reform our universal service system so that it is sustainable in an increasingly competitive marketplace. In 1997, the Commission established a comprehensive blueprint for universal service reform.<sup>5</sup> In 1999, we took action to ensure that the rates for supported services provided by non-rural carriers remain reasonably comparable and affordable for all Americans.<sup>6</sup> Today, we take action with respect to rural carriers.

4. In implementing the universal service provisions of the 1996 Act, the Joint Board and the Commission have consistently recognized that rural carriers face diverse circumstances and that “one size does not fit all” in considering universal service support mechanisms that are appropriate for rural carriers. When the Commission determined in May 1997 that universal service support should be based on the forward-looking economic cost of constructing and operating the network facilities and functions used to provide the supported services, it also determined that rural carriers would shift gradually to a forward-looking economic cost methodology.<sup>7</sup> The Commission wanted to allow ample time for rural carriers to adjust to any changes in support calculations. In the meantime, rural carriers would receive support based on the existing embedded cost mechanisms, as modified in the *First Report and Order*.<sup>8</sup>

5. The Commission recognized that the forward-looking cost mechanisms available at that time could not predict the costs of serving rural areas with sufficient accuracy.<sup>9</sup> Because rural carriers generally have higher operating and equipment costs, which are attributable to lower subscriber density, small exchanges, and a lack of economies of scale, the Commission recognized that additional effort would be needed to develop a forward-looking mechanism appropriate for rural carriers. To assist in this challenge, the Commission encouraged the Joint Board to establish a task force representing a broad range of interests.<sup>10</sup> To that end, the Joint Board established the Rural Task Force, which was comprised of individuals representing rural telephone companies, competitive local exchange carriers, interexchange carriers, wireless providers, consumer advocates, and state and federal agencies, to assist it in making its recommendation to the Commission.<sup>11</sup>

6. After exhaustive deliberations and considerable effort, including issuing six white papers, the Rural Task Force submitted its Recommendation to the Joint Board on September 29, 2000.<sup>12</sup> Rather

---

<sup>5</sup> *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776 (1997) (*First Report and Order*) (subsequent history omitted).

<sup>6</sup> See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Ninth Report and Order and Eighteenth Order on Reconsideration, 14 FCC Rcd 20432, 20439 (1999) (*Ninth Report and Order*), *pets. for review pending sub nom., Qwest Corp. v. FCC*, 10<sup>th</sup> Cir. No. 99-9546 and consolidated cases (1999).

<sup>7</sup> *First Report and Order*, 12 FCC Rcd at 8899 para. 224, 8936 para. 294.

<sup>8</sup> *Id.* at 8937-45 paras. 297-313.

<sup>9</sup> *Id.* at 8935 para. 293.

<sup>10</sup> See *id.* at 8917 para. 253.

<sup>11</sup> See *Federal-State Joint Board on Universal Service Announces the Creation of a Rural Task Force*, CC Docket No. 96-45, Public Notice, 12 FCC Rcd 15752 (Jt. Bd. 1997) (*Rural Task Force 1997 Public Notice*); *Federal-State Joint Board on Universal Service Announces Rural Task Force Members*, CC Docket No. 96-45, Public Notice, FCC 98J-1 (Jt. Bd. 1998) (*Rural Task Force 1998 Public Notice*).

<sup>12</sup> See Rural Task Force Recommendation. The Joint Board had requested the Rural Task Force’s recommendations no later than nine months after the implementation of the forward-looking high-cost mechanism for non-rural carriers, which became effective on January 1, 2000. See *Rural Task Force 1997 Public Notice*. As explained *infra*, the Joint Board established the Rural Task Force for the purpose of making recommendations to the Joint Board regarding an appropriate forward-looking high-cost support mechanism for rural carriers. After receiving the Rural Task Force’s recommendation, the Joint Board recommended that we base modifications to the high-cost support mechanism for rural carriers on the Rural Task Force recommendation. We will, for ease, refer to the Rural Task Force’s recommendation interchangeably with the Joint Board’s recommendation.

than attempting to modify the Commission's forward-looking cost mechanism that currently is used to determine non-rural support, the Rural Task Force proposed modifications to the current embedded cost system for a five-year period.<sup>13</sup> The consensus reached by the Rural Task Force members reflects the result of a process in which strongly held opposing views were aired, argued, and eventually accommodated. In recommending a modified embedded cost mechanism, the Rural Task Force attempted to "strike a careful balance between the need to provide a fund that is 'sufficient' under the provisions of the 1996 Act while insuring that the overall size of the fund is reasonable."<sup>14</sup>

7. After reviewing the Rural Task Force's proposal to modify the current embedded cost system for rural carriers, the Joint Board submitted its recommendation to the Commission on December 22, 2000. The Joint Board encouraged the Commission to take advantage of the consensus achieved by the diverse interests represented on the Rural Task Force and use the Rural Task Force Recommendation as a foundation for implementing a universal service plan for rural carriers for the next five years. The Joint Board also recognized that this is an interim plan. To that end, the Joint Board recommended that the Commission undertake a comprehensive review of the high-cost support mechanisms for both rural and non-rural carriers to ensure that both mechanisms function efficiently and in a coordinated fashion. The Joint Board urged the Commission to use this five year period to develop a long-term universal service plan that better targets support to rural carriers serving the highest cost areas.<sup>15</sup>

8. Based on the record before us, we find that adopting a modified embedded cost mechanism for rural carriers for a five-year period strikes a fair and reasonable balance among the goals and principles enumerated in section 254 of the Act. As the Joint Board suggested, we intend to develop over the next few years a long-term universal service plan for rural carriers that is better coordinated with the non-rural mechanism. In particular, we intend to develop a long-term plan that better targets support to carriers serving high-cost areas, while at the same time recognizing the significant differences among rural carriers, and between rural and non-rural carriers.

9. Throughout this proceeding, we have grappled with complex issues and balanced competing interests. We are mindful of the adage "Let not the perfect be the enemy of the good." The 1996 Act charged the Commission with the task of resolving the difficult issues surrounding universal service, consistent with the principles enunciated in section 254. We take action today that is consistent with the statutory requirements, recognizing that views may differ on the best policies to effectuate those requirements. In balancing the competing interests, we draw heavily from the recommendations of the Rural Task Force to the Joint Board, which exhaustively considered the issues before us over a two-year period. We build upon and modify those recommendations only in those areas where we conclude that implementation as proposed may have adverse consequences.

10. We conclude that the plan we adopt today will preserve and advance universal service, consistent with the goals and principles set forth in section 254 of the Act, and encourage competition in high-cost areas, consistent with the competitive goals of the 1996 Act. In particular, we find that adoption of the modified embedded cost mechanism is consistent with our obligation to ensure that the support provided to rural carriers over the next five years is specific, predictable, and sufficient. In addition, we find that the mechanism is consistent with the goals of section 254 to ensure that consumers in rural, insular, and high-cost areas have access to telecommunications services at rates that are affordable and reasonably comparable to rates charged for similar services in urban areas. We find further that the

---

<sup>13</sup> See Rural Task Force Recommendation at 17-19; *Recommended Decision* at para. 13.

<sup>14</sup> Rural Task Force Recommendation at 4.

<sup>15</sup> On January 12, 2001, the Commission sought comment on the Joint Board's Recommended Decision. See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Further Notice of Proposed Rulemaking, FCC 01-8 (rel. Jan. 12, 2001) (*Further Notice*).

flexible plan for disaggregating and targeting support adopted in this Order will facilitate competitive entry into high-cost areas, bringing the benefits of competition to consumers in rural areas.

11. The plan adopted today will provide certainty and stability for rural carriers for the next five years, enabling them to continue to provide supported services at affordable rates to American consumers. While we take an important step today on rural universal service reform, our task is not done. Our universal service rules cannot remain static in a dynamic marketplace. As we move forward, we will continue to refine our policies to preserve and advance universal service, consistent with the mandates in section 254.

## II. EXECUTIVE SUMMARY

12. In this Order, we take the following actions in response to the Rural Task Force's recommended reforms to rural high-cost universal service support and the proposals made by the Multi-Association Group (MAG) relating to this mechanism:

- We adopt the Rural Task Force's recommendation to re-base the high-cost loop support fund for rural telephone companies and retain an indexed cap on the fund. We conclude that re-basing the indexed fund will ensure that rural carriers are able to continue providing supported services at affordable and reasonably comparable rates during the transition to a more permanent high-cost support mechanism for rural carriers.
- We adopt a "rural growth factor" that allows the high-cost loop support fund to grow based on annual changes in the Gross Domestic Product-Chained Price Index (GDP-CPI) and the total number of working loops of rural carriers. We find that allowing the fund to grow in this fashion over the next five years will enable rural carriers to make prudent investments in rural America.
- We adopt the Rural Task Force's recommendation to freeze the national average loop cost at \$240.00. We conclude that freezing the national average loop cost will provide rural carriers with greater certainty as to their eligibility for high-cost loop support.
- We adopt a modified version of the Rural Task Force's proposal as it relates to corporate operations expenses. We revise the corporate operations expense limitation calculation so that the dollar values in the formula are re-based and indexed by the GDP-CPI.
- We also raise the minimum cap in the revised corporate operations expense limitation formula. Specifically, we permit small rural carriers to receive support for corporate operations expenses of up to \$600,000 or amounts derived from the revised corporate operations expense formula, whichever is greater. We find that raising the minimum cap from \$300,000 to \$600,000 will enable small rural carriers to receive more support for corporate operations expenses without having to file for waiver of our rules.
- We adopt a modified version of the Rural Task Force's proposed "safety net additive" so that a carrier will receive support for its incremental expense adjustment associated with new investment, rather than 50 percent of the difference between capped and uncapped support in a given year as proposed by the Rural Task Force. By modifying safety net support in this way, we ensure that carriers that meet the threshold requirement for eligibility will receive support for their incremental investment, but do not recover more than the costs incurred as a result of the additional investment.
- Consistent with the Rural Task Force's recommendation, we retain section 54.305 of the Commission's rules, which provides that a carrier acquiring exchanges from an

unaffiliated carrier shall receive the same per-line levels of high-cost support for which the acquired exchanges were eligible prior to their transfer. We modify the rule, however, to provide a “safety valve” that provides support for additional investment made in the acquired exchanges.

- We decline at this time to adopt the Rural Task Force’s proposal to freeze high-cost loop support upon competitive entry in rural carrier study areas. The proposal may be of limited benefit in serving its intended purpose of preventing excessive fund growth, and in some circumstances might increase high-cost loop support levels. We also conclude that the Rural Task Force’s proposal would be administratively burdensome and may have the unintended consequence of discouraging investment in rural America. In the attached Further Notice of Proposed Rulemaking, we invite comment on possible alternative measures.
- We address the Rural Task Force’s concerns regarding frequency of reporting and the lag in support in study areas with competitive eligible telecommunications carriers. First, we require all eligible telecommunications carriers serving such areas to report updated line counts on a regular quarterly basis. Second, we clarify that competitive eligible telecommunications carriers may submit data and receive high-cost loop support on a regular quarterly basis.
- We adopt, with certain modifications, the three paths for the disaggregation and targeting of high-cost universal service support proposed by the Rural Task Force. We also adopt the general requirements that the Rural Task Force proposed for all disaggregation plans. We find that providing rural carriers flexibility in the methods of disaggregation and targeting is a reasonable approach to address the significant diversity among such carriers and will facilitate competitive entry in rural areas.
- We find that the Rural Task Force’s proposed framework, with certain modifications, shall remain in place for five years and implementation shall begin as of July 1, 2001.
- We adopt the use of a wireless mobile customer’s billing address as the basis for determining the customer’s location for purposes of delivering high-cost universal service support.
- We conclude that states should file annual certifications with the Commission to ensure that eligible telecommunications carriers providing service in the service area of a rural carrier use universal service support “only for the provision, maintenance and upgrading of facilities and services for which the support is intended” consistent with section 254(e) of the Act.
- Consistent with the Rural Task Force’s recommendation, the Joint Board on Universal Service is currently considering the definition of supported services. We agree with the Rural Task Force that our universal service policies should not inadvertently create barriers to the provision of access to advanced services, and believe that our current universal service system does not create such barriers. We commit to further consideration of the Rural Task Force’s proposed “no barriers to advanced services” policy in the future.
- We find the Rural Task Force’s recommended principles for access reform to be reasonable and generally consistent with prior Commission actions to reform the access rate structure of price cap carriers. These principles will aid our consideration of access charge reform issues in the pending MAG proceeding. We recognize the importance of completing access reform for rate-of-return carriers and intend to act expeditiously to resolve issues raised in the MAG proceeding.

### III. BACKGROUND

#### A. High-Cost Support for Rural Carriers

13. The purpose of high-cost universal service support is to help provide access to telecommunications service in areas where the cost of such service otherwise might be prohibitively expensive.<sup>16</sup> Historically, this purpose has been achieved both through explicit monetary payments and implicit support flows to enable carriers to serve high-cost areas at below-cost rates.<sup>17</sup> Currently, three federal universal service mechanisms provide high-cost support for rural carriers. High-cost loop support, with which we are principally concerned here, provides support based on embedded costs averaged over entire study areas.<sup>18</sup> Carriers receive high-cost loop support for a variable percentage of their unseparated loop costs, depending on the number of loops they serve and the degree to which their costs exceed the national average cost per loop.<sup>19</sup> High-cost loop support for rural carriers is subject to an indexed cap, which limits total support to the previous year's total, increased by the rate of annual loop growth for all carriers.<sup>20</sup> Rural carriers also receive federal high-cost support through the Long Term Support (LTS) and Local Switching Support (LSS) mechanisms.<sup>21</sup> These three mechanisms provide approximately \$1.617

---

<sup>16</sup> See *Ninth Report and Order*, 14 FCC Rcd at 20439 para. 12.

<sup>17</sup> See *id.* at 20441 para. 15 (“In contrast to explicit support, some state rate designs and, to a lesser extent, the federal interstate access charge system, have provided implicit high-cost support flowing from (1) urban areas to rural areas; (2) business customers to residential customers; (3) vertical services to basic service; and/or (4) long distance service to local service”).

<sup>18</sup> The term “embedded costs” refers to a carrier’s historic costs, as reflected in its books. A study area is a geographic segment of a carrier’s telephone operations, generally corresponding to its entire service territory within a state. The Commission froze all study area boundaries effective November 15, 1984. See 47 C.F.R. Part 36, Appendix—Glossary.

<sup>19</sup> See 47 C.F.R. §§ 36.601, *et. seq.*; *First Report and Order*, 12 FCC Rcd at 8891-92 paras. 209-11. We define a loop as “the connection between the telephone company’s central office and the customer’s premises[.]” and loop cost as the fixed cost of this connection. *First Report and Order*, 12 FCC Rcd at 8891 nn.523, 525. The term “unseparated” refers to the jurisdictional separations process which divides between the state and federal jurisdictions the costs of those portions of carriers’ telephone plant that are used for intrastate and interstate services. High-cost loop support provides support only for the portion of a carrier’s total costs allocated to the intrastate jurisdiction. Specifically, carriers with 200,000 or fewer working loops receive support equal to 65 percent of the portion of their unseparated loop costs greater than 115 percent but less than or equal to 150 percent of the national average, and 75 percent of the portion of their unseparated loop costs greater than 150 percent. For carriers with over 200,000 working loops, the formula is similar, but with reduced levels of support. For example, a carrier with over 200,000 loops reaches the 75 percent support level only for costs that exceed 250 percent of the national average. The national average is calculated based on the loop costs of both rural and non-rural carriers.

<sup>20</sup> See 47 C.F.R. Part 36, Subpart F; *First Report and Order*, 12 FCC Rcd at 8929-30 paras. 281-82.

<sup>21</sup> LTS provides support for the interstate loop costs of rate-of-return carriers (typically small, rural carriers) that participate in the National Exchange Carrier Association (NECA) common line pool, and LSS (formerly DEM Weighting) is available to support a portion of the switching costs of carriers with 50,000 or fewer lines. 47 C.F.R. §§ 36.125(b), 54.301, 54.303. The Commission removed LTS and LSS from the interstate access charge system in 1998. The LTS and LSS support programs now are funded from collections from all providers of interstate telecommunications services made on an equitable and non-discriminatory basis. See generally *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Fourth Order on Reconsideration, *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge*, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, Report and Order, 13 FCC Rcd 5318, 5343-45 paras. 40-41, 5352-54 paras. 56-58 (1998) (*Fourth Order on Reconsideration*); see also *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Thirteenth Report and Order and Further Notice of Proposed Rulemaking, FCC 00-428 at paras. 6-9 (rel. Dec. 8, 2000).

billion in annual universal service support to over 1,300 rural carriers.<sup>22</sup>

## B. The Act

14. In the 1996 Act, Congress established principles for the preservation and advancement of universal service in a competitive telecommunications environment. In particular, section 254 of the Act provides that consumers in all regions of the nation, including consumers in rural, insular, and high-cost areas, should have access to telecommunications services at rates that are affordable and reasonably comparable.<sup>23</sup> Section 254 also provides that federal universal service support mechanisms should be specific, predictable, and sufficient to preserve and advance universal service.<sup>24</sup> The Commission adopted the additional principle that federal support mechanisms should be competitively neutral, neither unfairly advantaging nor disadvantaging particular service providers or technologies.<sup>25</sup> We have concluded that federal universal service policies should strike a fair and reasonable balance among these principles and goals enumerated in section 254.<sup>26</sup> In so doing, we have held that promotion of any one goal or principle should be tempered by a commitment to ensuring the advancement of each of the principles enumerated above.<sup>27</sup>

## C. Prior Joint Board and Commission Actions

15. With passage of the 1996 Act, particularly section 254, the Commission took a fresh look at its universal service support mechanisms. Based on the recommendations of the Joint Board, the Commission began reforming its high-cost support mechanisms in its *First Report and Order* released on May 8, 1997.<sup>28</sup> Among other things, the Commission concluded that federal universal service support for all carriers should be based on the forward-looking economic cost of constructing and operating the network used to provide the supported services, rather than each carrier's embedded costs.<sup>29</sup> The Commission explained that support based on forward-looking economic costs provides sufficient support without giving carriers an incentive to inflate their costs or to refrain from efficient cost cutting.

16. Although the Commission generally concluded that universal service support should be based on forward-looking economic costs rather than embedded costs, at the request of the Joint Board and rural carriers it proceeded initially with reform of the high-cost support mechanism for non-rural carriers.<sup>30</sup> The new, forward-looking mechanism for non-rural carriers became effective on January 1, 2000.<sup>31</sup> With regard to rural carriers, the Commission agreed with the Joint Board that, compared to the large non-rural carriers, "rural carriers generally serve fewer subscribers, serve more sparsely populated areas, and generally do not benefit as much from economies of scale and scope. For many rural carriers,

---

<sup>22</sup> See Federal Universal Service Support Mechanisms Fund Size Projections and Contribution Base For the Third Quarter 2001, Appendix HC 2 (Universal Service Administrative Company, May 2, 2001).

<sup>23</sup> 47 U.S.C. § 254(b)(3).

<sup>24</sup> *Id.* § 254(b)(5).

<sup>25</sup> *First Report and Order*, 12 FCC Rcd at 8801-03 paras. 46-51; see 47 U.S.C. § 254(b)(7).

<sup>26</sup> *First Report and Order*, 12 FCC Rcd at 8803 para. 52. The 1996 Act also requires the Commission to consult with the Joint Board in implementing section 254. See 47 U.S.C. § 254(a).

<sup>27</sup> *First Report and Order*, 12 FCC Rcd at 8803 para 54.

<sup>28</sup> *Id.* at 8780-81 paras. 1-3.

<sup>29</sup> See *id.* at 8899-901 paras. 224-229.

<sup>30</sup> See *id.* at 8936 para. 294.

<sup>31</sup> See *Ninth Report and Order*, 14 FCC Rcd at 20439 para. 11.

universal service support provides a large share of the carriers' revenues, and thus, any sudden change in the support mechanisms may disproportionately affect rural carriers' operations."<sup>32</sup> Accordingly, the Commission stated that it would not implement a forward-looking high-cost support mechanism for rural carriers before January 1, 2001, and only after selecting an appropriate mechanism based on recommendations from the Joint Board and a task force appointed by the Joint Board.<sup>33</sup> In this regard, the Commission agreed with the state Joint Board members that a task force "should provide valuable assistance in identifying the issues unique to rural carriers and analyzing the appropriateness of proxy cost models for rural carriers."<sup>34</sup>

#### D. Rural Task Force Recommendation

17. The Rural Task Force members were appointed by the Joint Board in July 1998, and deliberated for over two years before presenting their Recommendation to the Joint Board on September 29, 2000.<sup>35</sup> These deliberations included 12 meetings and 28 conference calls, as well as numerous subgroup calls.<sup>36</sup> The foundation for the Recommendation is a series of six white papers addressing, among other things, the differences between rural and non-rural carriers, and the appropriateness of using the Commission's forward-looking economic cost model for non-rural carriers to calculate support for rural carriers.<sup>37</sup> The Recommendation represents the consensus of individual Rural Task Force members, who work for a broad range of interested parties, often with competing interests, including rural telephone companies, competitive local exchange carriers, interexchange carriers, wireless providers, consumer advocates, and state and federal government agencies.<sup>38</sup> The Rural Task Force offered its Recommendation as an integrated package, and asked that it be adopted without modification. It urged that the Recommendation be implemented immediately and remain in place over a five-year period. The Rural Task Force's specific proposals are discussed in detail below. Here, we briefly summarize the Recommendation.

18. The Rural Task Force recommended against use of the Commission's forward-looking high-cost mechanism for non-rural carriers to calculate high-cost support for rural carriers.<sup>39</sup> Instead, it recommended the use over the next five years of a modified version of the current high-cost loop support mechanism used for rural carriers. The Rural Task Force's proposed modifications to the high-cost loop support mechanism include various upward adjustments to current limits on universal service support for rural carriers. Specifically, the Rural Task Force proposed that: (a) the indexed cap on high-cost loop support and the corporate operations expense limitation be recomputed as if they had not been in effect for

---

<sup>32</sup> *First Report and Order*, 12 FCC Rcd at 8936 para. 294.

<sup>33</sup> *Id.* at 8917 para. 252-53; *see also id.* at 8936 para. 294.

<sup>34</sup> *Id.* at 8917 para. 253; *see also id.* at 8918 para. 255; *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Second Recommended Decision, 13 FCC Rcd 24744, 24758 para. 30 (Jt. Bd. 1998).

<sup>35</sup> *See Rural Task Force 1998 Public Notice*; Rural Task Force Recommendation. As stated above, the Joint Board had requested the Rural Task Force's recommendations no later than nine months after the implementation of the forward-looking high-cost mechanism for non-rural carriers, which became effective on January 1, 2000. *See Rural Task Force 1997 Public Notice*.

<sup>36</sup> *See Rural Task Force Recommendation* at Appendix B.

<sup>37</sup> *See id.* at 6. The six Rural Task Force white papers are available on the Rural Task Force's web site at <<http://www.wutc.wa.gov/rtf>>.

<sup>38</sup> *See Rural Task Force Recommendation* at 6 ("This approach is pragmatic, and it is intended to deliver to the Joint Board a package of recommendations with the potential of being implemented promptly and without legal challenge from affected parties.").

<sup>39</sup> *See id.* at 20. The Rural Task Force emphasized that its Recommendation applies only to rural, insular, and high-cost areas served by *rural carriers*, and not to areas served by non-rural carriers. *See id.* at 18.

the calendar year 2000;<sup>40</sup> (b) a “safety net additive” mechanism be created to provide above-the-cap support for carriers with over 14 percent growth in telecommunications plant in service on a per-line basis;<sup>41</sup> and (c) a “safety valve” mechanism be created to provide additional support for “meaningful new investments” in exchanges acquired by rural carriers.<sup>42</sup> The Rural Task Force also recommended that, once a competitive eligible telecommunications carrier initiates service in a study area served by a rural carrier, per-line support within the study area be fixed and subsequently adjusted for growth in lines and inflation rather than changes in cost.<sup>43</sup>

19. In addition, the Rural Task Force recommended the use of a new annual index or “rural growth factor” to adjust the cap on high-cost loop support, the corporate operations expense limitation, and fixed per-line support in competitive study areas on a going-forward basis.<sup>44</sup> The rural growth factor would be the sum of annual line growth for rural carriers and a general inflation factor (Gross Domestic Product-Chained Price Index). Under the Rural Task Force’s proposal, safety net additive support, support for acquired exchanges, and safety valve support, as well as support for competitive eligible telecommunications carriers, would be excluded from the indexed cap on high-cost loop support. The Rural Task Force provided an example of a safety valve mechanism, in which safety valve support would be limited to five percent of the overall indexed cap on high-cost loop support.<sup>45</sup>

20. The Rural Task Force also suggested certain other reforms. It proposed that rural carriers be permitted to elect, within nine months of the effective date of the proposed new rules, whether and how to disaggregate and target universal service support on a per-line basis.<sup>46</sup> It recommended adoption of a “no barriers to advanced services” policy, and identified principles for replacing any implicit support in interstate access charges with explicit universal service support.<sup>47</sup> Furthermore, it recommended that the Commission delegate to the states responsibility for oversight of rural carriers’ compliance with section 254(e) of the 1996 Act, in a manner similar to that adopted for non-rural carriers.<sup>48</sup> Finally, the Rural Task Force recommended that the Commission address a number of issues, such as stranded costs and the interval between the provision of service and receipt of support, regarding which it did not reach agreement or did not formulate specific proposals.<sup>49</sup>

---

<sup>40</sup> *Id.* at 24-25, 27-29. The corporate operations expense limitation limits the amount of such expenses that a rural carrier may recover through high-cost loop support. See 47 C.F.R. § Part 36, Subpart F; *First Report and Order*, 12 FCC Rcd at 8930-32 paras. 283-85.

<sup>41</sup> Rural Task Force Recommendation at 27.

<sup>42</sup> *Id.* at 29-30; see 47 C.F.R. § 54.305 (limiting universal service support for acquired exchanges to the per-line support received by the seller).

<sup>43</sup> Rural Task Force Recommendation at 25-27.

<sup>44</sup> *Id.* at 25, 26, 28.

<sup>45</sup> *Id.* at Appendix D.

<sup>46</sup> *Id.* at 33-36.

<sup>47</sup> *Id.* at 22-23, 30-32. As indicated above, the Commission is now considering the comprehensive MAG proposal for interstate access charge and universal service reform for rate-of-return carriers. See *supra* n.1; see also *infra* paras. 202-205.

<sup>48</sup> Rural Task Force Recommendation at 32-33; see 47 C.F.R. § 54.313; *Ninth Report and Order*, 14 FCC Rcd at 20481-88 paras. 93-110. Section 254(e) provides that carriers shall use universal service support “only for the provision, maintenance, and upgrading of facilities and services for which the support is intended.” 47 U.S.C. § 254(e).

<sup>49</sup> Rural Task Force Recommendation at 38-39.

### E. Joint Board Recommended Decision

21. As noted above, the Rural Task Force presented its Recommendation to the Joint Board on September 29, 2000. The Joint Board issued a public notice requesting written comments from interested parties, and held an *en banc* hearing regarding the Recommendation in November 2000.<sup>50</sup> The Joint Board submitted its *Recommended Decision* to the Commission on December 22, 2000.

22. In its *Recommended Decision*, the Joint Board concluded that the Rural Task Force Recommendation “presents a good foundation for implementing a rural universal service plan.”<sup>51</sup> It stated that the Rural Task Force plan would provide rural carriers with stability for planning their investments over the next several years, while seeking to encourage competition in high-cost areas.<sup>52</sup> It also observed that the Rural Task Force’s proposed upward adjustments to limits on universal service support for rural carriers are “generally designed to provide carriers serving rural areas with increased incentives to invest in new infrastructure and technologies.”<sup>53</sup> The Joint Board remarked that the range of comments it received—from rural carriers that argued the plan would provide too little support to state commissions and other carriers that argued it would provide too much—were “consistent with a recommendation that is a consensus proposal put forth by representatives of disparate interests.”<sup>54</sup> The Joint Board encouraged the Commission “to take advantage of this opportunity to craft a rural universal service plan that enjoys widespread support among diverse interests.”<sup>55</sup>

23. In addition, the Joint Board observed that the Rural Task Force’s proposals to modify the Commission’s rules might raise implementation issues that the Commission would have to address.<sup>56</sup> It highlighted specific issues in connection with the proposals for a safety valve mechanism, fixed per-line support in competitive study areas, and safety net additive support.<sup>57</sup> With regard to access charge reform, the Joint Board recognized that the access charge issues raised by the Rural Task Force and the MAG plan are interstate in nature and, therefore, are properly before the Commission.<sup>58</sup> It urged the Commission, however, to ensure that the Joint Board remains actively involved in review of those aspects of the MAG plan that relate to universal service. Finally, the Joint Board recommended future steps for consideration of an appropriate universal service mechanism to succeed the Rural Task Force plan, urging the Commission “to use the transitional period during which a modified embedded cost mechanism is in place to develop a long-term universal service plan that better targets support to rural companies serving the highest cost areas, while at the same time recognizing the significant distinctions among rural carriers

---

<sup>50</sup> *Federal-State Joint Board on Universal Service To Hold En Banc Hearing November 13, 2000 on the Rural Task Force Recommendation for Universal Service Reform for Rural Carriers*, CC Docket No. 96-45, Public Notice, 15 FCC Rcd 22149 (Jt. Bd. 2000). The *en banc* hearing took place at the National Association of Regulatory Utility Commissioners conference in San Diego, California, where the Joint Board heard testimony from a diverse group of participants including rural and non-rural local exchange carriers, contributors to the federal universal service support mechanisms, consumer groups, and state and federal regulators.

<sup>51</sup> Rural Task Force Recommendation at para. 13.

<sup>52</sup> *See id.* at para. 11. Specifically, the Joint Board stated that the Rural Task Force plan seeks to encourage competitors to enter high-cost areas by proposing a flexible system for disaggregating support to establish the portable per-line support amount available to all eligible telecommunications carriers. *Id.*

<sup>53</sup> *Id.*

<sup>54</sup> *Id.* at para. 12.

<sup>55</sup> *Id.* at para. 10.

<sup>56</sup> *Id.* at para. 14.

<sup>57</sup> *See id.* at paras. 15-19.

<sup>58</sup> *Id.* at para. 20.

and between rural and non-rural carriers.”<sup>59</sup>

#### IV. DISCUSSION

##### A. Consistency with Principles of the Act

24. Based on the record before us, we conclude that the Rural Task Force plan that we adopt today will preserve and advance universal service, consistent with the goals and principles set forth in section 254 of the Act, and encourage efficient competition in high-cost areas, consistent with the competitive goals of the 1996 Act. In particular, we find that adoption of the modified embedded cost mechanism is consistent with our obligation to ensure that the support provided to rural carriers over the next five years is specific, predictable, and sufficient. In addition, we find that this mechanism is consistent with the principles and goals of section 254 to ensure that consumers in rural, insular, and high-cost areas have access to telecommunications services at rates that are affordable and reasonably comparable to rates charged for similar services in urban areas. We find further that the flexible plan for disaggregating and targeting support adopted in this Order will facilitate competitive entry into high-cost areas, bringing the benefits of competition to consumers in rural areas.<sup>60</sup>

25. We find that continuing to base support for rural carriers on embedded cost for the next five years is a reasonable and prudent approach to take in light of the record before us. The present record fails to provide the analysis necessary to permit a transition of rural carriers to a forward-looking high-cost support mechanism.<sup>61</sup> Before we could transition to such a mechanism, it would need to be fully analyzed and considered. Even commenters who urge the Commission to move toward a forward-looking support methodology for rural carriers as soon as possible recognize the need for additional time to develop an appropriate mechanism.<sup>62</sup> In light of the diversity among rural carriers, and based on our experience in developing the forward-looking high-cost support mechanism for non-rural carriers, we find that five years is a reasonable amount of time to maintain the Rural Task Force plan in place, while we consider long-term solutions. In the meantime, providing support based on embedded costs will provide important certainty to rural carriers, which generally receive a greater proportion of their revenues from universal service support mechanisms than non-rural carriers. Accordingly, we conclude that the Rural Task Force plan will provide specific and predictable support to rural carriers over the next five years.

26. In addition, we find that the modified embedded cost mechanism will provide sufficient support for purposes of section 254 of the Act, consistent with the goal of ensuring that consumers in rural, insular, and high-cost areas have access to telecommunications services at rates that are affordable and reasonably comparable to rates charged for similar services in urban areas. The record developed on the sufficiency issue reflects the opposing viewpoints of those receiving support from the fund and those contributing to it. Many commenters representing the interests of rural telephone companies argue that universal service support for rural carriers must be based on embedded costs to be consistent with section 254's sufficiency requirement.<sup>63</sup> Some argue explicitly that the existing and proposed caps on the high-cost loop fund violate this requirement and, by implication, that any mechanism that does not permit full recovery of embedded costs also would violate the Act.<sup>64</sup> Other commenters, namely contributors to the fund and net payor states, oppose any increases in support for rural carriers. They argue that the Rural

---

<sup>59</sup> *Id.* at para. 21.

<sup>60</sup> *See infra* discussion at section IV.D.

<sup>61</sup> *See* Ad Hoc Telecommunications User Committee Comments at 9-10; California Commission Comments at 3.

<sup>62</sup> *See, e.g.,* WorldCom Comments at 3; Ad Hoc Telecommunications User Committee Reply Comments at 5-6.

<sup>63</sup> *See, e.g.,* Alaska Tel. Assn. Comments at 2-3; NECA Reply Comments at 1-2.

<sup>64</sup> *See, e.g.,* Interstate Telecom Group Comments at 6; NTCA Comments at 3.

Task Force has not demonstrated that the current level of rural high-cost support is insufficient, and that sufficiency requires that the universal service support mechanisms provide no more support than is necessary.<sup>65</sup> Notably, although a number of commenters argue generally that the Rural Task Force plan would provide support that is either inadequate or excessive, neither side of the debate has proffered specific evidence supporting their positions.<sup>66</sup>

27. Determining whether support is “sufficient” for purposes of the Act is not a precise exercise: there is a range of funding levels that may be deemed sufficient. As the Fifth Circuit has observed, section 254(e) is ambiguous as to what constitutes “sufficient” support.<sup>67</sup> Thus, the Commission must use its expertise and informed judgement to make a reasonable determination as to what constitutes “sufficient” support. The Fifth Circuit has provided guidance, however. Rejecting challenges by rural telephone companies that, among other things, the continued imposition of the overall cap on high-cost loop support and the corporate operations expenses limitation violated the Act, the court stated that “[s]o long as there is sufficient and competitively-neutral funding to enable all customers to receive basic telecommunications services, the FCC has satisfied the Act and is not further required to ensure sufficient funding of every local telephone company.”<sup>68</sup> The court also cautioned that “excessive funding may itself violate the sufficiency requirements of the Act.”<sup>69</sup> Thus, in crafting universal service policies and programs, the Commission must strike a fair and reasonable balance among the goals and principles of the Act, and consider both the adequacy of support and the burden on contributors.<sup>70</sup>

28. We find that the modified embedded cost mechanism that we adopt in this Order strikes the appropriate balance at this time. In reaching this conclusion, we reject the contention that no increase in current high-cost loop support levels is warranted. In 1997, when the Commission decided to continue using an embedded cost mechanism to determine high-cost loop support for rural carriers pending permanent reform, it declined to adopt a Joint Board recommendation to freeze support for rural carriers at then-current levels.<sup>71</sup> In addition, the Commission did not anticipate that the embedded cost mechanism

---

<sup>65</sup> See, e.g., NYDPS at 4-5; WorldCom Comments at 2; Ad Hoc Telecommunications User Committee Reply Comments at 12-13. Some commenters also argue that support based on embedded costs may include costs associated with advanced services and other services that are not included in the Commission’s definition of universal service. See, e.g., California Commission Comments at 6; Illinois Commission Comments at 5; WorldCom Comments at 3.

<sup>66</sup> We note that the Maine and Vermont Commissions offer anecdotal evidence that specific carriers receive too little and/or too much support. See Maine and Vermont Commissions Comments at 6, 9, 13. As discussed below, their arguments are geared primarily towards better harmonization of the high-cost support mechanisms for rural and non-rural carriers, and the Commission will consider their arguments in the context of its comprehensive review of the rural and non-rural high-cost support mechanisms.

<sup>67</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393, 425-26 (5<sup>th</sup> Cir. 1999); *Alenco Communications, Inc. v. FCC*, 201 F.3d 608, 620 (5<sup>th</sup> Cir. 2000).

<sup>68</sup> *Alenco Communications, Inc. v. FCC*, 201 F.3d at 619 (“[P]etitioners’ sufficiency challenge fundamentally misses the goal of the Act. The Act does *not* guarantee all local telephone service providers a sufficient return on investment; quite to the contrary, it is intended to introduce competition into the market. Competition necessarily brings the risk that some telephone service providers will be unable to compete. The Act only promises universal service, and that is a goal that requires sufficient funding of *customers*, not *providers*.”)

<sup>69</sup> *Id.* (“Because universal service is funded by a general pool subsidized by all telecommunications providers – and thus indirectly by customers – excess subsidization in some cases may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market.”).

<sup>70</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d at 412; *Alenco Communications, Inc. v. FCC*, 201 F.3d at 620.

<sup>71</sup> *First Report and Order*, 12 FCC Rcd at 8939 para. 300. The Commission agreed with the state members of the Joint Board that “rural carriers may require a greater amount of support than fixed support mechanisms would (continued....)

for rural carriers would be in place for this long. As stated above, there is a range of funding levels that could be deemed sufficient for purposes of the Act, and the Rural Task Force proposal is the product of the consensus of divergent interests. At this time, we find that it is reasonable to modify the high-cost loop support levels for rural carriers established in 1997 to account for changes in costs and technology, and to ensure that rural carriers can maintain existing facilities and make prudent facility upgrades until such time as a long-term rural plan is adopted. Based on the estimates provided by the Rural Task Force and the Joint Board, we estimate that the modified embedded cost mechanism will result in an increase in rural carrier support of approximately \$1.26 billion over the five-year period.<sup>72</sup> We anticipate that any increases in the universal service contribution factor as a result of such increases will be modest, ranging from two-tenths to four-tenths of one percent.<sup>73</sup>

29. We also reject the assertions of several commenters, notably state commissions, that any universal service support mechanism should provide each area no more than the amount of support needed to enable the relevant state to ensure reasonably comparable rates among states.<sup>74</sup> These commenters argue, either expressly or implicitly, that because support under the modified embedded cost mechanism will be determined at the study-area level, and not at the state level consistent with the approach of the forward-looking mechanism for non-rural carriers adopted in the *Ninth Report and Order*, the modified embedded cost mechanism will provide excessive support to states that have low costs on average but contain high-cost study areas. The approach adopted in the *Ninth Report and Order*, however, depends on the ability to determine a statewide average forward-looking cost. In the *Ninth Report and Order* we found that, as a policy matter, federal high-cost support should be sufficient to enable reasonably comparable rates among states, while leaving states with sufficient resources to set rates for intrastate services that are reasonably comparable to rates charged for similar services within their borders.<sup>75</sup> To that end, we adopted a mechanism to calculate support for non-rural carriers by comparing the forward-looking costs of providing the supported services, averaged at the statewide level, to a national benchmark.<sup>76</sup> We found that statewide averaging, together with the other components of the forward-looking methodology adopted for non-rural carriers, is consistent with the division of federal-state

(Continued from previous page)

provide, ... [i]n order to maintain existing facilities and make prudent facility upgrades until such time as . . . forward-looking support mechanisms are in place.” *Id.*

<sup>72</sup> See Letter from William R. Gillis, Chair, Rural Task Force, to Magalie Roman Salas, FCC, dated November 10, 2000, at Attachment 2; *Recommended Decision* at para. 11 & n.32.

<sup>73</sup> The contribution factor for the second quarter of 2001 was approximately 6.88 percent. See *Proposed Second Quarter 2001 Universal Service Contribution Factor*, CC Docket No. 96-45, Public Notice, DA 01-614 (rel. Mar. 9, 2001). Future changes in the overall amount of federal universal service support and changes in the contribution revenue base may impact these projections. For example, the Commission recently sought comment on proposals to streamline and reform the manner in which the Commission assesses contributions to the federal universal service mechanisms. See *Federal-State Joint Board on Universal Service, 1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms, Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans With Disabilities Act of 1990, Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size, Number Resource Optimization, Telephone Number Portability*, CC Docket Nos. 96-45, 98-171, 90-571, 92-237, 99-200, 95-116, Notice of Proposed Rulemaking, FCC 01-145 (rel. May 7, 2001).

<sup>74</sup> See, e.g., California Commission Comments at 5; Florida Commission Comments at 4; Illinois Commission Comments at 13; NYDPS Comments at 4; Texas Commission Comments at 1, 2.

<sup>75</sup> *Ninth Report and Order* at 20453-54 para. 38.

<sup>76</sup> By averaging costs at the statewide level, the federal mechanism compares the relative costs of providing supported services in different states. The mechanism provides support to carriers in those states with average costs that exceed the national average cost benchmark.

responsibility for achieving reasonably comparable rates for customers of non-rural carriers.<sup>77</sup> When we adopted the forward-looking methodology for non-rural carriers, we noted that our decision did not necessarily mean that we would adopt a similar approach for rural carriers.<sup>78</sup> As explained above, we will continue to refine our rules as we develop a long-term universal service support mechanism for rural carriers. During the duration of the plan, which we are adopting for the interim, we will continue to consider a forward-looking methodology for rural carriers. Meanwhile, we will rely on the modified embedded cost mechanism to calculate support for rural carriers.

30. In sum, we find that the modified embedded cost mechanism we adopt will provide rural carriers with specific, predictable, and sufficient support over the next five years, consistent with the goals and principles set forth in section 254 of the Act. As a result, rural carriers will be able to continue to provide affordable service in rural America.

## **B. Modified Embedded Cost Mechanism**

### **1. The Indexed Cap on High-Cost Loop Fund and the Rural Growth Factor**

#### **a. Background**

31. The high-cost loop support fund currently is subject to an indexed cap, originally adopted in 1993,<sup>79</sup> which limits the maximum growth in the total amount of support available from the high-cost loop support fund to the previous year's support amount, increased by an index factor that is equal to the rate of growth in the total number of working loops nationwide for the calendar year preceding the annual data filing.<sup>80</sup> For example, in 1998, the total number of working loops grew 3.43 percent. Thus, the amount of high-cost loop support available in 2000 was the 1999 support amount (\$864.2 million) increased by 3.43 percent, which equals \$893.8 million.

32. The Commission originally adopted the indexed cap on the high-cost loop fund in order to limit fund growth and moderate annual fluctuations in the size of the fund pending the Commission's consideration of permanent changes to the high-cost assistance mechanisms.<sup>81</sup> Prior to the adoption of the indexed cap, the high-cost loop fund had grown by approximately 60 percent in eight years, with annual rates of growth ranging from one percent to more than 19 percent.<sup>82</sup> The Commission reasoned that moderating the growth of the high-cost loop fund would provide carriers with certainty regarding overall support levels and would facilitate the Commission's ability to revise the universal service mechanisms, if necessary, without jeopardizing the continued availability of local telephone service at reasonable rates.<sup>83</sup>

33. After passage of the 1996 Act, the Commission reassessed the operation of the indexed cap and decided to retain the indexed cap until all carriers receive high-cost support based on a forward-

---

<sup>77</sup> *Ninth Report and Order*, 14 FCC Rcd at 20453-54 para 38.

<sup>78</sup> *Id.* at 20453-54 para 45 n.136.

<sup>79</sup> *See Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Report and Order, 9 FCC Rcd 303 (1993) (*Fund Cap Order*); *see also Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Report and Order, 11 FCC Rcd 2538 (1996); *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 11 FCC Rcd 7920 (1996) (*Fund Cap Extension Order*).

<sup>80</sup> *See* 47 C.F.R. § 36.601(c). *See supra* para. 13 describing the operation of the high-cost loop support mechanism.

<sup>81</sup> *See Fund Cap Order*, 9 FCC Rcd at 305 paras. 17-20.

<sup>82</sup> *See id.* at 306 para. 22.

<sup>83</sup> *See id.* at 305 paras. 18-19.

looking economic cost mechanism.<sup>84</sup> The Commission reasoned that the indexed cap would prevent excessive growth in the existing high-cost loop fund during the period preceding the implementation of a forward-looking support mechanism.<sup>85</sup> According to the Commission, rapid growth in high-cost loop support would make the transition to a forward-looking mechanism more difficult for rural carriers if the new system provided for significantly different levels of support.<sup>86</sup> In short, the Commission concluded that the indexed cap effectively limits overall growth of the fund, while protecting individual carriers from experiencing extreme reductions in support.<sup>87</sup>

34. In the *Fourth Reconsideration Order*, the Commission concluded that the indexed cap is a reasonable means of limiting the overall growth of the high-cost loop fund, and thus protects contributors from excess universal service contribution requirements, while allowing the high-cost loop fund to grow to support the growth in lines served by carriers in high-cost areas.<sup>88</sup> In the absence of evidence showing that the indexed cap will result in insufficient support, the Commission also concluded that the indexed cap is consistent with the goal of section 254(b)(5) to ensure that universal service support is sufficient.<sup>89</sup>

35. Against this backdrop, the Rural Task Force recommended that the Commission retain an indexed cap on the high-cost loop support mechanism, but increase the size of the rural carrier portion of the high-cost loop support fund to reflect increased costs for rural carriers and tie the annual rate of growth of the rural carrier portion of the fund to an index that reflects increased costs and lines over time. In particular, the Rural Task Force recommended that the Commission recompute or “re-base” the indexed cap on the rural incumbent local exchange carrier portion of the high-cost loop support fund as if the indexed high-cost loop fund cap and a limitation on support for corporate operations expenses had not been in effect for the calendar year 2000.<sup>90</sup> The Rural Task Force also recommended that the Commission annually increase the re-based rural incumbent local exchange carrier portion of the high-cost loop support fund by an annual “rural growth factor” representing the sum of rural line growth and changes in a general inflation factor -- the United States Department of Commerce’s Gross Domestic Product-Chained Price Index (GDP-CPI).<sup>91</sup> The Rural Task Force further recommended that the Commission resize the indexed cap whenever the definition of supported services is changed.<sup>92</sup> Under the Rural Task Force’s proposal, “safety net additive” support,<sup>93</sup> support for acquired exchanges and “safety

---

<sup>84</sup> See *First Report and Order*, 12 FCC Rcd at 8940 para. 302, *Fourth Order on Reconsideration*, 13 FCC Rcd at 5340 para. 34.

<sup>85</sup> *First Report and Order*, 12 FCC Rcd at 8940 para. 302.

<sup>86</sup> *Id.*

<sup>87</sup> *Id.*

<sup>88</sup> See *Fourth Order on Reconsideration*, 13 FCC Rcd at 5343 para. 39.

<sup>89</sup> *Id.* at 5341-42 para. 36. See also 47 U.S.C. § 254(d) (requiring “[e]very telecommunications carrier that provides interstate services [to] contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service”).

<sup>90</sup> See Rural Task Force Recommendation at 24. According to the Rural Task Force, re-basing will result in an initial \$118.5 million increase in the high-cost loop support fund, representing \$83.9 million from removing the overall cap on high-cost loop support and \$34.6 million from removing the corporate operations expense limitation, used when calculating high-cost loop support. See *id.* at 20-21. The corporate operations expense limitation is discussed in greater detail in section IV.B.3. *infra*.

<sup>91</sup> See Rural Task Force Recommendation at 24-25.

<sup>92</sup> *Id.* at 27.

<sup>93</sup> *Id.*; see *infra* discussion at paras. 77-90.

valve” support,<sup>94</sup> and support for competitive eligible telecommunications carriers<sup>95</sup> would be calculated without regard to the re-based cap on high-cost loop support. In other words, these forms of support would be “uncapped.”

36. The Joint Board observed that the modifications to the caps and limitations on high-cost loop support proposed by the Rural Task Force, including the modifications to the cap on the high-cost loop fund, are “generally designed to provide carriers with increased incentives to invest in new infrastructure and technologies.”<sup>96</sup> The Joint Board concluded that the Rural Task Force Recommendation presents a good foundation for implementing a rural universal service plan.<sup>97</sup>

### b. Discussion

37. As discussed in greater detail below, we adopt the Rural Task Force’s recommendation to re-base the high-cost loop support fund for rural telephone companies and retain an indexed cap on the fund. Rural carriers shall receive re-based high-cost loop support effective July 1, 2001. We believe that an indexed cap balances the various goals enunciated in section 254 of the Act.<sup>98</sup> These goals include, among others, keeping the fund specific, predictable, and competitively neutral, as well as the need to achieve service and rate comparability.<sup>99</sup> Moreover, the indexed cap will ensure that the fund is within the range of sufficiency, and will minimize burdens on carriers to contribute to the universal service mechanisms.<sup>100</sup>

38. We agree with the Rural Task Force that “safety net additive” support and support for acquired exchanges and “safety valve” support should be excluded from the re-based cap on high-cost loop support. We believe that the exclusion of such support from the re-based cap on high-cost loop support is consistent with the universal service goals enunciated in section 254 of the Act. By providing carriers above-the-cap support for new investments in their existing networks and acquired exchanges, we introduce an element of predictability that has not been present under the current high-cost universal service mechanism.

39. In addition, we adopt the Rural Task Force’s proposal to increase the portion of the high-cost loop support fund that is distributed to rural incumbent local exchange carrier study areas by a rural growth factor equal to annual increases in the GDP-CPI and growth in the total number of working loops of rural incumbent local exchange carriers. As discussed in greater detail below, by reforming the growth factor in this way, we make high-cost support more specific to the needs of rural carriers. We also agree with the proposal included in the Rural Task Force’s example of a safety valve mechanism in Appendix D

---

<sup>94</sup> Rural Task Force Recommendation at 30. The Rural Task Force’s example of a “safety valve” mechanism for transferred exchanges includes a proposal to exclude loops transferred to rural telephone companies from the rural growth factor calculation. *Id.* at Appendix D. *See infra* discussion at paras. 91-119.

<sup>95</sup> Rural Task Force Recommendation at 25; *see infra* discussion at paras. 97-119.

<sup>96</sup> *Recommended Decision* at para. 11.

<sup>97</sup> *See id.* at para. 13.

<sup>98</sup> *See* 47 U.S.C. § 254.

<sup>99</sup> *See* 47 U.S.C. § 254(b)(3), (5). In addition to the universal service principles specified in the 1996 Act, Congress directed that the Joint Board and the Commission be guided by such other principles as they determine to be consistent with the Act, and necessary and appropriate for the protection of the public interest, convenience, and necessity. 47 U.S.C. § 254(b)(7). As recommended by the Joint Board, the Commission adopted competitive neutrality as an additional principle for universal service. *See First Report and Order*, 12 FCC Rcd at 8801-02 paras. 46-48, 8932-34 paras. 286-90.

<sup>100</sup> *See* 47 U.S.C. § 254(b)(4), (d).

of its Recommendation that all access lines transferred to rural carriers should be excluded from the rural growth factor.<sup>101</sup> We conclude that the Rural Task Force's proposal, as modified herein, represents a reasonable compromise between disparate interests. We also conclude that the Rural Task Force's proposal is consistent with the universal service goals enunciated in section 254 of the Act. Specifically, the Rural Task Force's proposal will ensure that rural telephone companies receive sufficient, specific, and predictable high-cost universal service support during this transition period, while minimizing the burden on carriers to contribute to the universal service mechanisms.

40. *Indexed Cap on the High-Cost Loop Fund.* We agree with the Rural Task Force and commenters that the indexed cap on the rural incumbent local exchange carrier portion of the high-cost loop fund should be recomputed or "re-based" as if the indexed fund cap and the corporate operations expense limitation had not been in effect for the calendar year 2000.<sup>102</sup> Effective July 1, 2001, rural carriers shall receive increased high-cost loop support based on uncapped support amounts for the calendar year 2000, plus a rural growth factor equal to the sum of annual changes in the total number of working loops for rural carriers and the GDP-CPI.<sup>103</sup> In reaching this conclusion, we are mindful that the Rural Task Force's recommendation represents the consensus of the Rural Task Force members, a diverse group representing all points of view affected by a change in the high-cost loop fund.<sup>104</sup> The need for such a consensus is evidenced by the widely differing comments received regarding the Rural Task Force's proposal to re-base the high-cost loop fund. The MAG and some commenters support removal of the indexed cap on the high-cost fund in its entirety,<sup>105</sup> while certain other commenters argue that the high-cost loop fund should not be re-based at this time.<sup>106</sup> Most commenters, however, support the Rural Task Force's proposal to re-base the rural carrier portion of the high-cost loop fund as an acceptable compromise between disparate interests.<sup>107</sup>

41. In the *First Report and Order*, the Commission concluded, in part, that rural carriers may require a greater amount of support than fixed support mechanisms would provide in order to maintain existing facilities and make prudent facilities upgrades until such time as a forward-looking support

---

<sup>101</sup> See Rural Task Force Recommendation at Appendix D; see also *infra* discussion at para. 53.

<sup>102</sup> See Rural Task Force Recommendation at 24; see also, e.g., Arizona LEC Assn. Comments at 2; AT&T Comments at 12; CUSC Comments App. A at 22; GVNW Consulting Comments at 3; NECA Comments at 7; NTCA Comments at 3-4; Virgin Islands Commission Comments at 6; Sprint Comments at 1-2; Western Alliance Comments at 11; WorldCom Reply Comments at 8.

<sup>103</sup> See *infra* discussion at paras. 48-53.

<sup>104</sup> The Rural Task Force was made up of individuals representing rural carriers, competitive local exchange carriers, interexchange carriers, wireless providers, consumers advocates, and state and federal interests.

<sup>105</sup> See *MAG NPRM*, 16 FCC Rcd at 464 para. 11; Arizona LEC Assn. Comments at 2; Interstate Telecom Group Comments at 6; John Staurulaukis, Inc. Comments at 6-8; NECA Comments at 5-7; NRTA, OPASTCO, & USTA Reply Comments at 5; NTCA Comments at 3-4; Western Alliance Comments at 11; see also Alabama Rural LECs Comments in CC Docket No. 00-256 at 2; MAG Reply Comments in CC Docket No. 00-256 at 14-15; Rate-of-Return Coalition Comments in CC Docket No. 00-256 at 6-7; Summit Tel. Co. Comments in CC Docket No. 00-256 at 3; Telecom Consulting Associates Comments in CC Docket No. 00-256 at 6; Wisconsin Commission Comments in CC Docket No. 00-256 at 6-7.

<sup>106</sup> See California Commission Comments at 8; Florida Commission Comments at 4; Illinois Commission Comments at 4-7; NYDPS Comments at 4; Texas Commission Comments at 3; Qwest Reply Comments at 3; WorldCom Comments at 3; see also AT&T Comments in CC Docket No. 00-256 at 9; CUSC Comments in CC Docket No. 00-256 at 18-19; Global Crossing Comments in CC Docket No. 00-256 at 11-12; Illinois Commission Comments in CC Docket No. 00-256 at 11; WorldCom Comments in CC Docket No. 00-256 at 16-17.

<sup>107</sup> See, e.g., Arizona LEC Assn. Comments at 2; AT&T Comments at 12; CUSC Comments App. A at 22; GVNW Consulting Comments at 3; NECA Comments at 7; NTCA Comments at 3-4; Virgin Islands Commission Comments at 6; Sprint Comments at 1-2; Western Alliance Comments at 11; WorldCom Reply Comments at 8.

mechanism is in place.<sup>108</sup> On the other hand, the Commission concluded that the indexed cap on high-cost loop support would moderate growth in the high-cost loop fund until final rules implementing the universal service provisions of the 1996 Act take effect.<sup>109</sup> More than seven years have passed since the Commission originally implemented the indexed cap on the high-cost loop support fund. We observe that the weighted average unseparated per-line loop cost for rural carriers increased by an annual average of approximately one percent per year from 1995 to 1999. The weighted average unseparated per-line loop cost for non-rural carriers decreased by an annual average of approximately 1.2 percent over the same period. Increases in the weighted average unseparated per-line loop cost for rural carriers currently are not reflected in the indexed cap on the high-cost loop fund, which is based on the rate of growth in the total number of rural and non-rural working loops nationwide for the preceding calendar year.<sup>110</sup> Therefore, the indexed cap on the high-cost loop fund increasingly has limited the amount of high-cost loop support for rural carriers. According to the Rural Task Force, without the indexed cap, the portion of the high-cost loop fund that is distributed to rural telephone company study areas would have been \$83.9 million higher in calendar year 2000.<sup>111</sup> The Rural Task Force has responded, in part, by recommending that the Commission recompute or “re-base” the indexed cap on the rural carrier portion of the high-cost loop fund as if the indexed cap was not in effect for the calendar year 2000. As discussed above, this proposal represents a compromise of competing interests.<sup>112</sup>

42. Based on the record before us, we find it reasonable to reevaluate and re-base the high-cost loop support fund to ensure that rural telephone companies have incentives to maintain existing facilities and make prudent investments in facility upgrades. At the same time, the record does not reflect a specific point at which support should be set. Indeed, we believe that there is no one specific such point. Rather, establishing sufficient support requires a balancing of goals such as providing incentives for prudent investment and preventing excessive support to the detriment of carriers contributing to the fund.<sup>113</sup> In light of these goals, we believe it is reasonable to re-base the rural incumbent local exchange carrier portion of the high-cost loop fund as if the indexed cap and the corporate operations expense limitation were not in effect for the calendar year 2000. Although this approach may appear more generous to rural carriers than the current mechanism, we believe it is a reasonable approach to accomplishing the sufficiency balance here because we do not want to stifle prudent investment while we continue to transition rural carriers to a support mechanism based on forward-looking economic costs. The adjustments to the indexed cap we adopt today will prevent excessive and erratic growth in the high-cost loop fund, while ensuring that rural telephone companies are able to provide supported services at affordable and reasonably comparable rates.

43. We therefore adopt the Rural Task Force’s proposal to re-base the rural carrier portion of the high-cost loop fund as if the indexed cap and the corporate operations expense limitation had not been effect for calendar year 2000. We concur with the Joint Board’s observation that the modifications to the caps and limitations on high-cost loop support proposed by the Rural Task Force are “generally designed to provide carriers with increased incentives to invest in new infrastructure and technologies.”<sup>114</sup> We

<sup>108</sup> See *First Report and Order*, 12 FCC Rcd at 8939 para. 300 (rejecting a proposal to base support, on a going-forward basis, on costs reported in 1995).

<sup>109</sup> See *First Report and Order*, 12 FCC Rcd at 8940 para. 302; *Fund Cap Order*, 9 FCC Rcd at 305 para. 17; *Fund Cap Extension Order*, 11 FCC Rcd at 7923-24 paras. 7-9.

<sup>110</sup> See *supra* at para. 31.

<sup>111</sup> See Rural Task Force Recommendation at 20-21. The Rural Task Force also notes that the removal of corporate operations expense limitation would increase the fund for rural carriers by \$34.6 million.

<sup>112</sup> See *supra* at para. 35.

<sup>113</sup> See *supra* paras. 26-28.

<sup>114</sup> See *Joint Board Recommended Decision* at para. 12.

conclude that re-basing the indexed fund will ensure that eligible rural telephone companies are able to continue making prudent investments in rural facilities for the next five years, while we develop a more targeted high-cost support mechanism for rural telephone companies.

44. We also agree with the Rural Task Force that safety net additive support, support for acquired exchanges, and safety valve support should be excluded from the re-based cap on high-cost loop support.<sup>115</sup> As discussed in greater detail below, we believe that the exclusion of such support from the re-based cap on high-cost loop support is consistent with the universal service goals enunciated in section 254 of the Act. The availability of uncapped safety net additive support will ensure that rural carriers that make significant investments in telecommunications plant in service receive sufficient, specific, and predictable support for the incremental costs associated with new investment, while minimizing the burden on carriers that contribute to the universal service mechanisms.<sup>116</sup> Support for acquired exchanges in the form of safety valve support will be subject to a cap of five percent of the portion of the annual indexed cap on the high-cost loop fund that is distributed to rural incumbent local exchange carrier study areas.<sup>117</sup> We believe that a five percent cap will ensure that sufficient support is available for acquired exchanges and will protect contributors from excessive universal service contributions.

45. We clarify, however, that, because support for acquired exchanges and safety valve support will be provided outside the cap, the overall size of the rural high-cost loop fund should be reduced to reflect the removal of support for access lines transferred from rural carriers to non-rural carriers or to other rural carriers. The reduction shall equal the amount of the expense adjustment available to the transferred access lines at the time of the transfer and shall be effective in the next calendar quarter after the access lines are transferred. Without such an exclusion from the rural incumbent local exchange carrier portion of the high-cost loop fund, the remaining access lines might receive increased per-line support when access lines are transferred from a rural incumbent local exchange carrier study area to a non-rural carrier or to another rural incumbent local exchange carrier.<sup>118</sup> Under such a scenario, the lines included in the rural incumbent local exchange carrier portion of the high-cost loop fund would decrease, without a corresponding decrease in the overall rural incumbent local exchange carrier portion of the high-cost loop fund. Over time, per-line support for the remaining access lines would increase to the extent that more exchanges are transferred from rural incumbent local exchange carrier study areas. Such a result would be inconsistent with the statutory goal of providing no more support than is sufficient and would not prevent excessive growth in the high-cost loop fund.<sup>119</sup> We expect that the exclusion of support for transferred access lines from the rural incumbent local exchange carrier portion of the indexed high-cost loop fund will maintain the relationship between the size of the high-cost loop fund and the number of supported lines.

46. We disagree with commenters and the MAG that the Commission should remove the indexed cap on the high-cost loop fund in its entirety.<sup>120</sup> We find that the MAG proposal to remove the indexed cap on the high-cost fund is incompatible with the modified high-cost loop support mechanism

---

<sup>115</sup> See Rural Task Force Recommendation at 30.

<sup>116</sup> See *infra* discussion at para. 79.

<sup>117</sup> See *infra* discussion at paras. 107-109.

<sup>118</sup> Assume, for example, that a total of 10 rural carrier lines receive \$1 per line or a total of \$10 in high-cost loop support. If one line is sold to a non-rural carrier, then the remaining nine lines would be eligible for approximately \$1.11 per line in high-cost loop support, representing an 11 percent increase in per-line support. If, however, there is a corresponding \$1 reduction in the total amount of available high-cost loop support to reflect the sale of one line to a non-rural carrier, then the remaining lines would not receive increased per-line support.

<sup>119</sup> See *First Report and Order*, 12 FCC Rcd at 8940 para. 302.

<sup>120</sup> See *supra* n.105.

recommended by the Joint Board and adopted in this Order. Based on the record before us, we specifically disagree that an indexed cap on the high-cost loop fund will prevent rural carriers from receiving adequate universal service support.<sup>121</sup> The indexed cap we adopt today will result in an immediate increase in the high-cost loop support available to rural telephone companies and will grow by the rural growth factor, which includes an inflation adjustment – an additional growth element that is not part of our existing cap. In addition, several mechanisms we adopt today, such as safety net additive support<sup>122</sup> and safety valve support<sup>123</sup> will provide carriers with additional support. We also continue to believe that an indexed cap is a reasonable means of limiting the overall growth of the high-cost loop fund, and thus protects contributors from excessive universal service obligations.<sup>124</sup> As discussed above, we also believe that an indexed cap balances the universal service goals, such as sufficiency, specificity, and predictability, enunciated in section 254 of the Act.<sup>125</sup>

47. The Rural Task Force also recommended that the indexed cap be resized whenever the definition of supported services is changed.<sup>126</sup> We note that, in accordance with section 254(c)(2) of the Act,<sup>127</sup> the Commission recently requested that the Joint Board review the definition of services eligible for high-cost and low-income universal service support.<sup>128</sup> The Commission specifically asked the Joint Board to address the implications of any proposed modifications to the list of supported services.<sup>129</sup> We therefore will await the Joint Board's recommendations regarding the definition of supported services prior to considering whether the indexed cap should be resized to reflect any modifications to the list of supported services.

48. *Rural Growth Factor.* We adopt the Rural Task Force's proposal to grow the portion of the high-cost loop support mechanism that is distributed to rural incumbent local exchange carrier study areas by a rural growth factor equal to the sum of annual changes in the total number of working loops of rural incumbent local exchange carriers and the GDP-CPI, not the rate of growth for all rural and non-rural working loops.<sup>130</sup> The rural growth factor shall be based on the GDP-CPI for the year in which costs are incurred and the difference between the total number of rural incumbent local exchange carrier working loops for the cost year and the preceding calendar year. For example, for support disbursed in the year 2001, the rural growth factor shall be based on the percentage change in the GDP-CPI for calendar year 1999 and the percentage change in the total number of rural incumbent local exchange carrier working loops between calendar years 1998 and 1999.

---

<sup>121</sup> See, e.g., Interstate Telecom Group Comments at 6; John Staurulaukis, Inc. Comments at 6-7; NRTA, OPASTCO, & USTA Comments at 5-7.

<sup>122</sup> See *infra* discussion at paras. 77-90.

<sup>123</sup> See *infra* discussion at paras. 91-119.

<sup>124</sup> See *Fourth Order on Reconsideration*, 13 FCC Rcd at 5343 para. 39. As the Commission concluded in the *First Report and Order*, excessive growth in high-cost loop support may make the transition to other support mechanisms more difficult for rural carriers, especially if those support mechanisms provide significantly different levels of support. See *First Report and Order*, 12 FCC Rcd at 8940 para. 302.

<sup>125</sup> See *supra* discussion at para. 42.

<sup>126</sup> Rural Task Force Recommendation at 27.

<sup>127</sup> Section 254(c)(2) provides that “[t]he Joint Board may, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms.” 47 U.S.C. § 254(c)(2).

<sup>128</sup> See *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Order, 15 FCC Rcd 25257 (rel. Dec. 21, 2000) (*Referral Order*).

<sup>129</sup> *Id.* at para. 3.

<sup>130</sup> See Rural Task Force Recommendation at 25.

49. We note that growth in rural working loops nationwide recently has been higher than growth in non-rural working loops nationwide.<sup>131</sup> We therefore believe that it is appropriate to limit growth in the rural incumbent local exchange carrier portion of the high-cost loop fund based on the growth in the total number of working loops of rural incumbent local exchange carriers. Using a rural growth factor will more accurately reflect changes in the number of rural lines over time. We disagree with commenters who argue that the Commission should retain the current index factor, which reflects both rural and non-rural line growth, instead of adopting the Rural Task Force's proposal for a rural growth factor.<sup>132</sup> These parties do not suggest that the high-cost loop fund should remain stagnant, rather they disagree with the factor to be used to grow the fund.

50. We also note that the current index factor does not account for varying costs that are unrelated to the increase in working loops. When the Commission extended the indexed cap in the *First Report and Order*, it expected to move rural carriers to a universal service support mechanism based on forward-looking economic costs more quickly than will actually occur.<sup>133</sup> Because the timeframe for moving to a forward-looking economic cost mechanism is now extended for rural carriers, we believe that it is reasonable to acknowledge, in the portion of the high-cost loop support mechanism that is distributed to rural incumbent local exchange carrier study areas, that costs may vary for reasons unrelated to the growth in working loops. For the duration of this plan, we therefore adopt the Rural Task Force's recommendation to use the GDP-CPI as a proxy for cost changes.

51. We reject proposals to include a rural telephone company or telecommunications industry productivity factor in the rural growth factor.<sup>134</sup> Although it appears that rural carrier costs recently have grown at a slightly slower annual rate than growth in the GDP price index (indicating that rural carriers have experienced modest productivity gains over time), at this time, we do not have a reliable methodology for measuring productivity gains for rural telephone companies.<sup>135</sup> Moreover, parties have not submitted a methodology that specifically measures the productivity gains of rural carriers.<sup>136</sup> We note that the high-cost loop fund will be subject to an indexed cap for the life of the plan, thus ensuring that rural carriers do not receive excessive support. We therefore adopt the consensus recommendation of the Rural Task Force to include an inflation factor, the GDP-CPI, in the rural growth factor without also including a productivity factor.

52. We conclude that the rural growth factor proposed by the Rural Task Force will further the universal service goals, such as sufficiency, specificity, and predictability, enunciated in section 254 of

---

<sup>131</sup> For example, the annual rate of growth in the total number of rural and non-rural working loops nationwide, which was 2.86 percent in 1999, is considerably less than the annual rate of growth in the total number of rural working loops nationwide, which was 4.26 percent in 1999. See NECA Universal Service Fund 2000 Submission of 1999 Study Results, filed October 1, 2000; NECA Universal Service Fund 1999 Submission of 1998 Study Results, filed October 1, 1999.

<sup>132</sup> See, e.g., California Commission Comments at 9; SBC Reply Comments at 6.

<sup>133</sup> See *supra* discussion at para. 41.

<sup>134</sup> See Ad Hoc Telecommunications User Committee Comments at 17; Texas Commission Comments at 4; *but see* Innovative Telephone Reply Comments at 5-7.

<sup>135</sup> For example, the weighted average unseparated per-line loop cost for rural carriers increased by an average of approximately one percent per year from 1995 to 1999, while the GDP price index increased by 1.75 percent per year during that same period. See *supra* discussion at para. 41; AT&T Comments in CC Docket No. 00-256 at Table 1. Moreover, AT&T states that average growth in the common line revenue requirement from 1995-1999 was 5.99 percent per year, while average annual growth in the GDP price index plus access lines was 7.19 percent during that same period. *Id.*

<sup>136</sup> See, e.g., Ad Hoc Telecommunications User Committee Comments at 17 (proposing that the Commission use the productivity factor currently applied to price cap LEC rates).

the Act.<sup>137</sup> Because the rural growth factor will ensure that the portion of the high-cost loop support mechanism that is distributed to rural incumbent local exchange carrier study areas better reflects growth in rural lines and changed costs over time, we conclude that the rural growth factor will provide rural incumbent local exchange carriers with sufficient support. The rural growth factor also will provide rural incumbent local exchange carriers with specific and predictable growth in the high-cost loop support mechanism over time.

53. In addition, we adopt the proposal, included in the Rural Task Force's example of a safety valve mechanism, to exclude all access lines transferred to rural carriers from the rural growth factor calculation.<sup>138</sup> This conclusion is consistent with our reasons for excluding support for access lines transferred to rural incumbent local exchange carrier study areas from the rural incumbent local exchange carrier portion of the indexed cap on the high-cost loop fund.<sup>139</sup> Including access lines transferred to rural incumbent local exchange carriers in the rural growth factor, but not in the portion of the indexed high-cost loop fund that is distributed to rural incumbent local exchange carrier study areas, would result in growth in the indexed high-cost loop fund that reflects neither growth in lines eligible to receive support from the indexed high-cost loop fund nor growth in the GDP-CPI for those lines. If transferred loops were included in the rural growth factor, but not in the rural incumbent local exchange carrier portion of the indexed high-cost loop fund, the remaining access lines would receive increased per-line support whenever access lines are transferred to a rural carrier study area. Over time, per-line support for the remaining access lines would increase as more loops are transferred to rural carrier study areas. Such a result would be inconsistent with the goal, enunciated in the *First Report and Order*, of preventing excessive growth in the high-cost loop fund.<sup>140</sup> Consistent with the exclusion of support for competitive eligible telecommunications carriers from the indexed cap, we also will exclude lines operated by competitive eligible telecommunications carriers from the rural growth factor.<sup>141</sup>

## 2. National Average Loop Cost

### a. Background

54. The Rural Task Force's recommendation to re-base the high-cost loop fund includes a proposal to freeze the national average loop cost at \$240.00 for the life of the plan, which, according to the Rural Task Force, approximates the actual national average loop cost for year 2000 support (based on 1998 cost data).<sup>142</sup> Under the Commission's existing rules, a rural carrier is eligible for high-cost loop support if its embedded loop costs for a particular study area exceed 115 percent of the national average loop cost.<sup>143</sup> According to section 36.622 of the Commission's rules, the national average loop cost is the greater of: (1) the sum of loop costs nationwide divided by the total number of working loops nationwide; or (2) an amount calculated to maintain the indexed cap on the high-cost loop support fund.<sup>144</sup> If the sum of actual high-cost loop support nationwide exceeds the indexed cap on the high-cost loop support fund (in essence, the indexed cap on the high-cost loop support fund is triggered), the national average loop cost is increased in order to ensure that the total amount of high-cost loop support disbursed does not exceed the

---

<sup>137</sup> See 47 U.S.C. § 254(b)(5).

<sup>138</sup> See Rural Task Force Recommendation at Appendix D.

<sup>139</sup> See *supra* para. 45.

<sup>140</sup> See *First Report and Order*, 12 FCC Rcd at 8940 para. 302.

<sup>141</sup> See *infra* discussion at para. 125.

<sup>142</sup> See Rural Task Force Recommendation at 24.

<sup>143</sup> See 47 C.F.R. §§ 36.601-36.631.

<sup>144</sup> See 47 C.F.R. § 36.622.

indexed cap.

**b. Discussion**

55. We adopt the Rural Task Force's recommendation to freeze the national average loop cost at \$240.00 for purposes of calculating rural high-cost loop support.<sup>145</sup> We conclude that freezing the national average loop cost for the duration of this plan will provide rural carriers with greater certainty as to their eligibility for high-cost loop support.<sup>146</sup> Because the national average loop cost will be frozen at \$240.00, carriers will know in advance whether they may be eligible for high-cost loop support. Such certainty will assist carriers in short- and long-term planning for infrastructure investment, consistent with the goals of specificity and predictability in section 254 of the Act.<sup>147</sup> Because freezing the national average loop cost for rural carriers at \$240.00 will provide carriers with greater predictability as to their eligibility for high-cost loop support, carriers also will be better able to achieve rate and service comparability, another goal of section 254 of the Act.<sup>148</sup>

56. At this time and based on the record, we do not believe that freezing the national average loop cost at \$240.00 will result in significant numbers of carriers with higher than average loop costs being denied support and carriers with lower than average loop costs being awarded support. If in a given year the actual national average loop cost is significantly above \$240.00, support may be directed to certain rural carriers that otherwise would not be eligible for high-cost loop support. If, on the other hand, the actual national average loop cost falls below \$240.00, support may be withheld from rural carriers that otherwise would be eligible for high-cost loop support under our current rules.

57. In support of this conclusion, we note that the national average loop cost has experienced only minor fluctuations over the past four years. For example, the national average loop cost (with the corporate operations expense limitation in effect) for high-cost loop support disbursed in 1998 was \$247.34, while the national average loop cost (with the corporate operations expense limitation in effect) for high-cost loop support disbursed in 2001 is \$239.86.<sup>149</sup> This represents only an approximately three percent reduction in the national average loop cost in four years. We therefore do not anticipate a dramatic increase or decrease in the actual national average loop cost in the near future such that large numbers of carriers with lower than average loop costs will inappropriately receive high-cost loop support or that carriers with higher than average loop costs will inappropriately be denied high-cost loop support. In light of this relatively small percentage change, we believe that the specificity and predictability provided by a frozen national average loop cost outweighs any potential distortions that might occur with a freeze for the limited five-year duration of the plan we adopt today.<sup>150</sup>

58. We also note that, as provided by section 36.622 of the Commission's rules, if the sum of the actual high-cost loop support nationwide exceeds the indexed cap on the high-cost loop support fund, NECA increases the amount of the national average loop cost in order to ensure that the total amount of

---

<sup>145</sup> See Rural Task Force Recommendation at 24; *see also* NTCA Comments at 4; Verizon Comments at 3; Sprint Reply Comments at 3; *but see* Texas Commission Comments at 4.

<sup>146</sup> See 47 U.S.C. §§ 254(b)(5), (e).

<sup>147</sup> See 47 U.S.C. § 254(b)(5).

<sup>148</sup> See 47 U.S.C. § 254(b)(3).

<sup>149</sup> See NECA Universal Service Fund 1997 Submission of 1996 Study Results, filed October 1, 1997; NECA Universal Service Fund 2000 Submission of 1999 Study Results, filed October 1, 2000.

<sup>150</sup> See 47 U.S.C. § 254(b)(5).

high-cost loop support disbursed does not exceed the indexed cap.<sup>151</sup> Thus, certain carriers with average loop costs slightly above the proposed frozen national average loop cost would not receive support. To the extent that the frozen national average loop cost is increased to accommodate the indexed cap on the high-cost loop fund, carriers with average loop costs below the actual national average loop cost but above the proposed frozen national average loop cost would not receive high-cost loop support. Although we adopt a national average loop cost of \$240.00 for the duration of this plan, if the actual national average loop cost experiences significant increases or reductions, we may consider appropriate actions at that time.<sup>152</sup>

59. Under section 36.612 of our rules, every non-rural telephone company is required to submit loop cost data and loop counts on a quarterly basis.<sup>153</sup> Under section 36.611 of our rules, all incumbent local exchange carriers are required to submit loop cost data and loop counts on an annual basis.<sup>154</sup> Because the national average loop cost is based on embedded loop cost data for both rural and non-rural study areas, non-rural carriers currently are required to file such data with the fund administrator even though non-rural carriers now receive high-cost support based on a forward-looking methodology.<sup>155</sup> If we freeze the national average loop cost at \$240.00, it will no longer be necessary for NECA to calculate the national average loop cost on a quarterly basis, and, thus, it is unnecessary for non-rural carriers to file loop cost data on a quarterly basis. Nor is there any other reason to require non-rural carriers to file this quarterly loop cost data.<sup>156</sup> Because NECA will no longer make such calculations, it is unnecessary to require submission of that information. We therefore will no longer require non-rural carriers to submit the loop cost data listed in section 36.611 of our rules to NECA on a quarterly basis. In order to enable the Commission to accurately evaluate the operation of the frozen national average loop cost over time, we will continue to require non-rural carriers to submit loop cost data on an annual basis and loop counts on a quarterly basis. Such information is necessary for NECA and USAC to determine the amount of high-cost support available to non-rural carriers.

### **3. Corporate Operations Expenses**

#### **a. Background**

60. The high-cost loop support fund provides support for a portion of the corporate operations expenses incurred by rural carriers in providing supported services. Corporate operations expenses consist of total company costs associated with the following activities: formulating corporate policy and providing overall administration and management; long-range planning; providing accounting and financial services; maintaining relations with government, regulators, other companies, and the general public; performing personnel administration activities; operating general purpose computers; providing legal services; procuring material and supplies; developing new products; and performing other general administrative activities.<sup>157</sup> Prior to 1998, the amount of corporate operations expenses that was supported

---

<sup>151</sup> 47 C.F.R. § 36.622. The Rural Task Force did not propose to change this aspect of section 36.622 of the Commission's rules.

<sup>152</sup> *See infra* paras. 167-177.

<sup>153</sup> *See* 47 C.F.R. § 36.612.

<sup>154</sup> *See* 47 C.F.R. § 36.611.

<sup>155</sup> *See* 47 C.F.R. §§ 36.621, 36.622.

<sup>156</sup> *See* Verizon Comments at 1, 3; Sprint Reply Comments at 2-3.

<sup>157</sup> Corporate operations expenses include all of the expenses listed in sections 32.6710 through 32.6712 and sections 32.6720 through 32.6728 of the Commission's rules. 47 C.F.R. §§ 32.6710-32.6712; 47 C.F.R. §§ 32.6720-32.6728. Those categories of expenses include: executive; planning; general; administrative; accounting; finance; external relations; human resources; information management; legal; procurement; research and development; and other general and administrative expenses. *Id.*

through our universal service mechanisms was determined by multiplying the total corporate operations expense by the ratio of loop investment to total plant in service. As explained below, in the *First Report and Order* the Commission concluded that a carrier's ability to receive universal service support for corporate operations support should not be unlimited.

61. The corporate operations expense limitation, adopted by the Commission in the *First Report and Order*, limits the amount of corporate operations expenses that a carrier may include in the high-cost loop support mechanism.<sup>158</sup> Under the current mechanism, a carrier compares its actual corporate operations expenses with the expenses calculated by the existing corporate operations expense limitation formula and the lesser amount is used to calculate the carrier's high-cost loop support. The formula was developed to "ensure that carriers use universal service support only to offer better service to their customers through prudent facility investment and maintenance consistent with their obligations under section 254(k)."<sup>159</sup> The Commission agreed with commenters that corporate operations expenses do not appear to be costs inherent in providing telecommunications services, but rather may result from managerial priorities and discretionary spending.<sup>160</sup> The Commission decided to "limit universal service support for corporate operations expense to a reasonable per-line amount," but recognized that "small study areas . . . may experience greater amounts of corporate operations expense per line than larger study areas."<sup>161</sup> The formula allows a greater amount of corporate expense per line for smaller study areas than larger ones because statistical analysis of carrier data show that study areas with fewer loops have more corporate operations expense per loop.

62. In the *First Reconsideration Order* and the *Fourth Reconsideration Order*, the Commission made further refinements to the corporate operations expense cap formula specifically to recognize problems of smaller carriers.<sup>162</sup> On its own motion, the Commission established a floor (or minimum cap) on the corporate operations expense cap to allow carriers with relatively few lines to receive sufficient support to recover initial or fixed corporate operations expenses.<sup>163</sup> Subsequently, the Commission reconsidered, to a limited extent, the dollar amount of the minimum cap on allowable corporate operations expenses for small carriers.<sup>164</sup>

63. In response to requests by small carriers to reconsider its decision to place a limit on the support available for corporate operations expenses, the Commission explained more fully in the *Fourth Reconsideration Order* its reasons for limiting the amount of corporate operations expenses that a carrier could include in the high-cost loop support mechanism.<sup>165</sup> The Commission explained that carrier expenditures for corporate operations expenses may be discretionary in many instances, in contrast to

<sup>158</sup> *First Report and Order*, 12 FCC Rcd at 8930-32 paras. 283-85, 8942 para. 307.

<sup>159</sup> *See id.* at 8930-31 para. 283.

<sup>160</sup> *Id.* at 8931 para. 283.

<sup>161</sup> *Id.*

<sup>162</sup> *See Federal-State Joint Board on Universal Service*, CC Docket 96-45, Order on Reconsideration, 12 FCC Rcd 10102-10105 paras. 17-24 (1997) (*First Reconsideration Order*); *Fourth Order on Reconsideration*, 13 FCC Rcd at 5376-77 paras. 94-95.

<sup>163</sup> *First Reconsideration Order*, 12 FCC Rcd at 10103 para. 19. Under the original formula, carriers with very few lines may have been unable to recover portions of corporate operations expense that do not vary with the number of lines, because allowable corporate operations expenses were determined by a factor that is multiplied by the number of lines. *Id.* The Commission also modified the formula to ensure that the cap on allowable corporate operations expense does not decrease as the number of lines increases. *Id.*; *see also Fourth Order on Reconsideration*, 13 FCC Rcd at 5377 para. 96.

<sup>164</sup> *See id.* at 5376-77 paras. 94-95.

<sup>165</sup> *See id.* at 5369-70 para. 87 & nn.230-231, 5374-76 paras. 92-93.

expenditures for maintaining plant and equipment.<sup>166</sup> Corporate operations expenses include, for example, travel, lodging, and other expenses associated with attending industry conventions and corporate meetings. While participation in such activities may be prudent, the levels of these expenditures are subject to managerial discretion. The Commission also noted that carriers with 200,000 or fewer working loops had little incentive to minimize these expenses because the previous rules allowed carriers to recover a large percentage of their corporate operations expenses from federal universal service support mechanisms.<sup>167</sup>

64. Although the Commission retained the limitation on support for corporate operations expenses, the Commission raised the minimum cap so that the need for the smallest carriers to seek a waiver would be reduced.<sup>168</sup> Specifically, the Commission adjusted the maximum allowable corporate operations expense formula by permitting carriers with 6,000 or fewer working loops to include in the high-cost loop support mechanism corporate operations expenses of up to \$300,000 or amounts derived from the corporate operations expense formulas, whichever is greater, provided that the amount is not greater than a carrier's actual corporate operations expenses.<sup>169</sup> The Commission concluded that "imposing a cap that is relatively generous to small carriers, but still imposes a limitation, is a reasonable method of encouraging carriers to assign corporate operations expenses to the proper accounts and discouraging carriers from incurring excessive expenditures."<sup>170</sup>

65. The Rural Task Force proposed modifying the existing corporate operations expense limitation formula by re-basing and indexing the dollar values in the formula.<sup>171</sup> Since this cap was imposed, the Rural Task Force estimated that the number of rural carriers affected by it -- 205 rural study areas in 2000 -- has increased by 15 percent.<sup>172</sup> To reflect increased work requirements, labor, and other costs since the formula was put in place, the Rural Task Force proposed increasing the dollar values in the formula by the rural growth factor for each year since the cap was adopted. In subsequent years, the

---

<sup>166</sup> See *id.* at 5374 para. 92.

<sup>167</sup> See *id.* at 5374 para. 92. Under the Commission's Part 36 rules, carriers with 200,000 or fewer working loops recover 65 percent of loop costs that exceed 115 percent of the national average loop cost and 75 percent of loop costs that exceed 150 percent of the national average. Thus, prior to adoption of the corporate operations expense limitation, carriers with 200,000 or fewer working loops could recover a substantial portion of their operation expenses from the federal universal service support mechanism. See 47 C.F.R. § 36.631. By comparison, for example, a carrier with more than 200,000 working loops recovers 10 percent of loop costs that exceed 115 percent of the national average loop cost, 30 percent of loop costs that exceed 160 percent of the national average, 60 percent of loop costs that exceed 200 percent of the national average, and 75 percent of loop costs that exceed 250 percent of the national average. See 47 C.F.R. § 36.631.

<sup>168</sup> *Fourth Order on Reconsideration*, 13 FCC Rcd at 5374 para. 92. The Commission recognized, however, that certain carriers, such as those serving Alaska or insular territories, may have unusually high corporate operations expenses, and invited such carriers to file for a waiver "to demonstrate the necessity of these expenses for the provision of the supported services." *Id.*

<sup>169</sup> See *id.* at 5376-77 paras. 94-95. The minimum cap under the previous formula was \$114,071. *Id.* In no event may a carrier include in the expense adjustment calculation more than its actual corporate operations expenses. See 47 C.F.R. § 36.621(a)(4).

<sup>170</sup> See *Fourth Order on Reconsideration*, 13 FCC Rcd at 5374 para. 92.

<sup>171</sup> As discussed above, the Rural Task Force also recommended that the Commission re-base the indexed cap on the high-cost loop support fund as if both the indexed cap and the corporate operations expense limitation had not been in effect for the calendar year 2000. The Rural Task Force estimated that re-basing the fund would result in a \$118.5 million increase in high-cost loop support, representing \$83.9 million from removing the overall cap on high-cost loop support and \$34.6 million from removing the corporate operations expense limitation. Rural Task Force Recommendation at 24. Note that removing the corporate operations expenses limitation without also removing the overall cap would not increase total support, but would only redistribute support among carriers.

<sup>172</sup> This is based on information provided by NECA. See Rural Task Force Recommendation at 27 n.53.

dollar values in the formula would be increased each year by the rural growth factor. The Rural Task Force estimated that the number of rural carriers affected by the corporate operations expense cap would have decreased, rather than increasing by 15 percent, if the dollar limitations derived from the formula had been increased annually by five percent.<sup>173</sup> Rather than \$34.6 million being excluded by operation of the corporate operations expense limitation in 2000, the Rural Task Force estimated that only \$15.1 million would have been excluded.<sup>174</sup>

66. The Rural Task Force also proposed an additional calculation that carriers could use to determine the maximum amount of corporate operations expenses that could be included in the high-cost loop support mechanism. The Rural Task Force noted that some companies consistently have corporate operations expenses above the existing limitation and acknowledged that the waiver process can be economically infeasible for some rural carriers.<sup>175</sup> In order to provide an option other than the waiver process for carriers that would continue to have corporate operations expenses above the section 36.621(a)(4) limitation, even after the dollar amounts in the formula are re-based and indexed, the Rural Task Force proposed an alternative calculation based on uncapped corporate operations expenses for the year 2000. The new alternative formula begins with the uncapped corporate operations expense per line for the year 2000, increases this amount each year by the rural growth factor, and multiplies this amount by the number of lines for the year in question.<sup>176</sup>

67. Under the Rural Task Force proposal, the carrier first compares the amount calculated by the re-based and indexed corporate operations expense limitation formula with the amount calculated under the proposed alternative formula.<sup>177</sup> If the alternative amount based on year 2000 actual expenses is greater than the amount calculated by the re-based and indexed corporate operations expense limitation formula, this is the amount compared with a carrier's actual corporate operations expenses for the year in question and the lesser amount is included in the high-cost loop support mechanism.

68. The Joint Board observed that the modifications to the caps and limitations on high-cost loop support proposed by the Rural Task Force are "generally designed to provide carriers with increased incentives to invest in new infrastructure and technologies."<sup>178</sup> The Joint Board concluded that the Rural Task Force Recommendation presents a good foundation for implementing a rural universal service plan, but did not address the corporate operations expense limitation in specific detail.<sup>179</sup>

## **b. Discussion**

69. We generally agree with the Rural Task Force that modifications to the existing corporate operations expense limitation are appropriate to reflect changes in costs since the limitation was imposed in 1998. Accordingly, as discussed below, we adopt a revised formula to reflect these changes. We also agree with the Rural Task Force's goal of reducing the need for carriers to request waivers due to the operation of section 36.621(a)(4) of our rules.<sup>180</sup> We decline, however, to adopt the Rural Task Force's proposed alternative calculation. Instead, as explained below, in order to reduce the need for the smallest

---

<sup>173</sup> *Id.* at 28 n.55.

<sup>174</sup> *Id.*

<sup>175</sup> *Id.* at 29.

<sup>176</sup> *Id.*

<sup>177</sup> *Id.*

<sup>178</sup> *Recommended Decision* at para. 12.

<sup>179</sup> *See id.* at para. 14.

<sup>180</sup> 47 C.F.R. §36.621(a)(4).

carriers to seek a waiver of section 36.621(a)(4), we raise the minimum cap on allowable corporate operations expenses supported by universal service to \$600,000.

70. We disagree with the MAG and other commenters who argue that the Commission should remove the limitation on support for corporate operations expenses entirely.<sup>181</sup> Because expenditures for corporate operations expenses are discretionary in many instances, and carriers with 200,000 or fewer loops have little incentive -- absent the limitation -- to minimize these expenses, we continue to believe that some limitation on the universal service support available for these expenses is reasonable and appropriate. We also disagree with those commenters who argue that no adjustment to the corporate operations cap is justified.<sup>182</sup> As discussed below, we find that it is reasonable to make certain adjustments to the corporate operations expense limitation formula.

71. We share the Rural Task Force's concern that the number of rural carriers impacted by the corporate operations expense limitation has increased by 15 percent, affecting 205 rural study areas, in the two years since this limitation was imposed and, therefore, believe that the formula should be revised.<sup>183</sup> The limitation is intended to encourage carriers to assign corporate operations expenses to the proper accounts and to discourage carriers from incurring excessive expenditures. The Rural Task Force suggested that the reason more carriers have been affected by the corporate operations expense limitation is due to "increased work requirements, labor, and other costs."<sup>184</sup> Analysis of carrier data over this period shows that, on average, corporate operations expenses per line have remained essentially constant.<sup>185</sup> For some carriers, however, corporate operations expenses clearly have increased since the limitation was imposed. Without adjustment, the number of rural carriers affected by the cap in 2001 would be 215 -- an increase of almost 21 percent since the cap was imposed. We therefore conclude that it is reasonable to revise the formula by increasing the dollar values in the formula.

72. We decline, however, to increase the limitation by the rural growth factor, as suggested by the Rural Task Force. Instead, we adopt a revised corporate operations expense limitation formula in which the dollar values in the formula are re-based and indexed by the Gross Domestic Product-Chained

---

<sup>181</sup> See, e.g., *MAG NPRM*, 16 FCC Rcd at 464 para. 11; Wisconsin Commission Comments at 7. Most commenters who oppose caps do not specifically discuss the corporate operations expense limitation, but argue generally against any caps or limitations on high-cost loop support. See, e.g., John Staurulaukis, Inc. Comments at 6; NTCA Comments at 3.

<sup>182</sup> See, e.g., California Commission Comments at 10. Most commenters who oppose increases in support for rural carriers do not specifically discuss the corporate operations expense limitation, but argue generally against re-basing the high-cost loop fund. See, e.g., Ad Hoc Telecommunications User Committee Comments at 15-16; NYDPS Comments at 3-5. AT&T points out that any increased support that results from revising the corporate operations expense limitation is subject to the new indexed cap on the high-cost loop fund. See AT&T Comments at 12.

<sup>183</sup> See Rural Task Force Recommendation at 27 n.53.

<sup>184</sup> See *id.* at 28.

<sup>185</sup> Using publicly available data, Commission staff compared growth in corporate operations expenses from 1997 to 1999. Weighted by 1997 loops, the annual growth rate was 0.10 percent. Weighted by 1999 loops, the annual growth rate declined by 0.39 percent. The source of the data is the NECA Universal Service Fund 2000 Submission of 1999 Study Results, filed October 29, 2000. This data set includes data for the years 1995 to 1999. The sample included 773 rural cost companies. For each of the 773 companies staff listed: USF Loops, Account #6710 -- Executive and planning expense; Account #6720 -- General and administrative expense; and their sum, which is total corporate operations expense. From these factors staff calculated the monthly cost per loop for 1997 and 1999 for each of the 773 companies. For each of the companies, staff calculated the increase of 1999 expenses over 1997 expenses. This increase for each company was weighted by both the 1997 loops and the 1999 loops and two weighted averages were calculated as follows: using 1997 loops:  $1.001009221 - 1 = .001009221$  or 0.10 percent; using 1999 loops:  $.99612603 - 1 = -.00387397$  or -0.38 percent.

Price Index (GDP-CPI). The Rural Task Force proposed that the dollar values in the corporate operations expense limitation formula be re-based and indexed by the rural growth factor, which is the sum of the GDP-CPI and total annual line growth for rural carriers.<sup>186</sup> We find that it is more appropriate to re-base and index the formula only by the GDP-CPI, without including annual rural line growth. Because the corporate operations expense limitation is calculated as a per-line amount, which is then multiplied by lines to determine the total amount of corporate operations expenses that is used to determine support, the formula already accounts for a carrier's line growth. Multiplying the amount by another line growth factor – the rural line growth – would result in double counting of line growth.

73. In re-basing the dollar values in the formula, we will increase the dollar values for each of four years. We believe that this is more consistent with the Rural Task Force's proposal to increase the dollar values in the formula for each year since the cap was implemented, than the two years referenced in the Recommendation.<sup>187</sup> Although the corporate operations expense cap was implemented in 1998, the formula was based on 1995 cost data.<sup>188</sup> Because support in year 2001 is based on 1999 cost data, we will increase the dollar values in the formula to reflect increases in GDP-CPI from 1995 to 1999. In subsequent years, the per-line allowable expense amount shall be adjusted annually by GDP-CPI. We find that these modifications to the corporate operations expense limitation will adequately account for increases in corporate operations expenses since the cap originally was adopted.

74. We recognize that smaller carriers in particular may be affected by the current corporate operations expense limit and agree with the Rural Task Force that the waiver process can be a very expensive option for small carriers.<sup>189</sup> To reduce the need for small carriers to seek a waiver, the Commission previously raised the minimum cap in the corporate operations expense limitation formula to \$300,000.<sup>190</sup> We adopt further protections for small carriers by raising the minimum cap in the revised formula. Specifically, we permit carriers with 6,000 or fewer loops to receive support for corporate operations expenses of up to \$600,000 or amounts derived from the revised corporate operations expense formulas, whichever is greater.<sup>191</sup> We find that by raising the minimum cap from \$300,000 to \$600,000 an increased number of small carriers will have expenses that fall within the revised limitation. Consistent with current rules, we propose that if a carrier's actual corporate operations expenses are less than \$600,000 then the carrier would recover high-cost loop support based on its actual corporate operations expenses.

75. We find that raising the minimum cap in the corporate operations expense limitation formula to address the needs of smaller carriers is preferable to the alternative proposed by the Rural Task Force. The Rural Task Force's proposed alternative calculation would essentially eliminate the corporate operations expense limitation currently in effect. We note that the corporate operations expense limitation was adopted, in part, to prevent carriers from recovering from the high-cost loop support mechanism excessive expenditures unrelated to the provision of supported services.<sup>192</sup> The limitation is designed to allow carriers to receive support for corporate operations expenses based on typical expenses for companies of comparable size. As demonstrated by the graph in Appendix D, some carriers are

---

<sup>186</sup> See Rural Task Force Recommendation at 26.

<sup>187</sup> See *id.* at 28 & n.55.

<sup>188</sup> See *supra* n.158.

<sup>189</sup> See Rural Task Force Recommendation at 28-29. The Rural Task Force noted that one Alaska carrier received a waiver, but only for one year.

<sup>190</sup> See *supra* para. 62.

<sup>191</sup> See 47 C.F.R. § 36.621.

<sup>192</sup> See *Fourth Order on Reconsideration*, 13 FCC Red at 5374 para. 92.

extreme outliers and have corporate operations expenses that far exceed the average range of expenses for companies of comparable size. The Rural Task Force's proposal would permit these outliers to receive support for these uncapped expenses as if the corporate operations expense limitation had never been adopted.<sup>193</sup> For example, under the Rural Task Force proposal, these outliers could include in the high-cost loop support mechanism either their actual corporate operations expenses in 2001 or their actual per-line expenses in the year 2000, increased by the rural growth factor and the number of lines served in 2001. The latter would be more than 2001 actual expenses if a carrier's per line actual expenses increase by more than the rural growth factor. A carrier would only receive less than the adjusted, uncapped 2000 amount in future years if its actual corporate operations expenses were lower in those years. The Rural Task Force's proposal therefore would provide no incentive for carriers to limit their corporate operations expenses.

76. By imposing a reasonable limit on the universal service support available for carriers' corporate operations expenses, we are not precluding carriers that incur unusually high corporate operations expenses from receiving support for such expenses. To the extent that individual companies continue to incur corporate operations expenses that exceed the limitation, they may ask the Commission to waive these rules on a case-by-case basis.<sup>194</sup>

### **C. Support Above the Cap**

#### **1. Safety Net Additive**

##### **a. Background**

77. In addition to the existing support provided by the high-cost loop fund, the Rural Task Force proposed a "safety net additive," which would provide additional support to carriers "who make significant investment in rural infrastructure."<sup>195</sup> Safety net additive support would only be available in years in which support levels would otherwise exceed the new indexed cap on the high-cost loop support fund.<sup>196</sup> To receive such support in a particular study area, a carrier would need to show that growth in telecommunications plant in service (TPIS)<sup>197</sup> per line is at least 14 percent greater than the study area's TPIS per line in the prior year, or the "base year."<sup>198</sup> As proposed, safety net additive support would allow a carrier to recover 50 percent of the difference between the capped and uncapped expense adjustment

---

<sup>193</sup> See Texas Commission Comments at 4 (suggesting that the Commission consider raising the corporate operations cap for very small rural carriers "rather than eliminating the limitation in its entirety").

<sup>194</sup> We clarify that the Commission's rules do not preclude a multi-year waiver. See California Commission Comments at 11 ("California supports a change to the waiver process that would allow a multi-year waiver if a petitioner supports the need for a waiver for more than one year."). The Rural Task Force stated that the waiver process "has yielded petitioners only a one-year waiver" and cited an example in which this was the case. Rural Task Force Recommendation at 28 & n.55. The Commission's rules do not require a carrier to seek a waiver every year if a waiver is granted for a longer period of time.

<sup>195</sup> See *Joint Board Recommended Decision* at para. 19; see also Rural Task Force Recommendation at 27.

<sup>196</sup> Rural Task Force Recommendation at 27. In years when the cap is not triggered, rural carriers would receive support in an amount that would cover the added expense associated with the new investment, and thus it is unnecessary to provide safety net additive support in those years.

<sup>197</sup> TPIS is an accounting category used by the Commission and carriers to classify certain elements of their operation. TPIS includes, for example, the carrier's cable and wire facilities, poles, central office switching facilities, public telephone terminal equipment, and customer premises wiring. It also includes general support facilities such as buildings, office equipment, and general purpose computers. 47 C.F.R. §32.2001.

<sup>198</sup> Rural Task Force Recommendation at 27. The Rural Task Force stated in its recommendation that the 14 percent figure represents an estimate of two times the average rural growth factor in recent years.

for the qualifying year.<sup>199</sup> Any study area that initially qualifies for safety net additive support would also qualify for such support in each of the four succeeding years if the cap is again triggered, regardless of whether the study area meets the 14 percent criterion in the succeeding years.<sup>200</sup>

78. In the *Further Notice*, the Commission sought comment on issues relating to implementation of the safety net additive mechanism. Specifically, the Commission asked whether the safety net additive mechanism would allow carriers to recover more than 100 percent reimbursement of their incremental loop investment and on any other implementation issues raised by the Rural Task Force's plan.<sup>201</sup>

## b. Discussion

79. We agree with the Joint Board, the Rural Task Force, and several commenters that we should adopt some form of safety net additive that will provide additional support to those rural carriers that have made significant investment in years in which the fund is capped.<sup>202</sup> We believe that providing this additional support will provide rural carriers with appropriate incentives to invest in the network infrastructure serving their communities. As the Rural Task Force stated in *White Paper 3*, which reviewed alternatives to the current embedded cost mechanism, no mechanism for universal service support is without weaknesses.<sup>203</sup> The Rural Task Force, however, also recognized that a mechanism could be designed so that it mitigates specific weaknesses.<sup>204</sup> One of the identified weaknesses of an embedded cost mechanism that incorporate an overall cap is that it may hinder the ability of rural carriers to invest in infrastructure.<sup>205</sup>

80. While we make modifications to the operation of the safety net additive mechanism proposed by the Rural Task Force, we find that the implementation of a safety net mechanism is a reasonable consensus approach arrived at by competing interests to mitigate the potential negative effects of a cap, and provide rural carriers with the predictability to make investments in their communities.<sup>206</sup> As detailed below, we modify the safety net additive so that a carrier will receive support for its incremental, or additional, expense adjustment associated with new investment, as opposed to 50 percent of the difference between the study area's capped and uncapped support in a given year.<sup>207</sup> By tying the amount of additional support to a carrier's incremental expense adjustment associated with new investments, we ensure that carriers do not receive additional support for more than the costs incurred as a result of the additional investment. We also address below certain implementation issues regarding the safety net

---

<sup>199</sup> *Id.* The "qualifying year" is the first year in which the study area meets the criterion for receiving support.

<sup>200</sup> *Id.* Safety net additive support would only be available in years in which the cap is triggered because, in years when the cap is not triggered, carriers would already receive 100 percent of their expense adjustment.

<sup>201</sup> See *Further Notice* at para. 7.

<sup>202</sup> See *Joint Board Recommended Decision* at para. 19; see also Rural Task Force Recommendation at 27; AT&T Comments at 15; NRTA, OPASTCO, & USTA Comments at 6; Texas Commission Comments at 5; Telecom Consulting Associates Comments at 11.

<sup>203</sup> *Alternative Mechanisms for Sizing a Universal Service Fund for Rural Telephone Companies: Rural Task Force White Paper 3* (Aug. 2000) (visited May 2, 2001) <<http://www.wutc.wa.gov/rtf>> at 29 (*White Paper 3*).

<sup>204</sup> *Id.* at 29.

<sup>205</sup> *Id.* at n.10.

<sup>206</sup> *White Paper 3* at 29.

<sup>207</sup> The expense adjustment calculated pursuant to section 36.621 of our rules is the amount of high-cost loop support a carrier is eligible to receive. This support amount is based on a carrier's unseparated loop costs in relation to the national average loop cost. See *infra* n.19.

additive. We believe that by modifying the safety net additive mechanism in this way, we provide carriers with predictability in investing in infrastructure, while minimizing the potential burden such a mechanism could have on contributors.

81. We find that a 14 percent increase in a carrier's TPIS per line investment, as proposed by the Rural Task Force, provides a reasonable method for assessing whether the carrier has made significant investment to qualify its study area for safety net additive support. We find that growth in TPIS is a reasonable benchmark for triggering the safety net additive mechanism because increases in TPIS reflect the carrier's overall increases in investment over the past year.<sup>208</sup> While we recognize that not all TPIS investments are supported through the high-cost loop fund, we find that using TPIS as a benchmark for the safety net additive is a reasonable proxy for defining rural infrastructure investment requirements. We note in this regard that investments made in categories other than those supported by high-cost loop support may allow a carrier to qualify for safety net support, but the investment itself would not qualify for additional support under the safety net additive mechanism. Unless the incremental costs associated with new investment are in the categories eligible for support under section 36.621 of our rules, the carrier's incremental costs, for purposes of high-cost loop support, appear unchanged and therefore the carrier would realize no additional support from the safety net additive.<sup>209</sup> Carriers are thus provided with the appropriate incentive to make investments in those categories that affect supported services to the end user, which is the underlying goal of the safety net additive.

82. Moreover, we find that 14 percent growth in TPIS is a reasonable trigger given historical TPIS per-line investment trends. In order to determine which wire centers and study areas are entitled to an expense adjustment, the Commission requires the National Exchange Carrier Association (NECA) to collect data from all incumbent local exchange carriers.<sup>210</sup> Based on the information reported by those carriers, NECA calculates the national and study area average cost per loop.<sup>211</sup> A comparison of the 1999 NECA cost study results to 1998 cost study results shows that, in approximately five percent of cost-study areas, TPIS per-line investment increased by 14 percent or more, while only nine cost-study areas had TPIS per-line investment over 40 percent. The average increase was approximately two percent. While we realize that prospectively this pattern may be altered by inclusion of the safety net additive, our concern and those expressed by commenters regarding the potential for gaming by rural carriers is mitigated because the types of investments the safety net additive supports require time and extensive planning.<sup>212</sup>

83. Accordingly, we conclude that the Rural Task Force has proposed a reasonable figure for what constitutes significant investment and thus we set the safety net trigger at 14 percent. We therefore disagree with those commenters who claim that setting the threshold as high as 14 percent effectively denies the neediest of rural carriers access to the additional support under this new mechanism.<sup>213</sup> In doing so, we ensure that carriers that make significant investment will receive additional support in years in

---

<sup>208</sup> *But cf.* Maine and Vermont Commissions Comments at 11 (arguing that we should “restrict the trigger for the safety net by excluding loop costs.”).

<sup>209</sup> 47 C.F.R. § 36.621. These categories include investment in cable and wire facilities that are “subscriber of common lines that are jointly used for local exchange service and exchange access for state and interstate interexchange services” and exchange line circuits. 47 C.F.R. § 36.154 (a); 36.126 (b)(1)(iii).

<sup>210</sup> 47 C.F.R. § 36.611.

<sup>211</sup> 47 C.F.R. §§ 36.621, 36.622, 36.631.

<sup>212</sup> CUSC Comments at 8 (asserting that carriers would have an incentive to defer investment only to later make large investments to qualify for support). *See also* California Commission Comments at 9.

<sup>213</sup> *See* NTCA Comments at 17; SDITC Comments at 6; Telecom Consulting Associates Comments at 11.

which the cap is reached.<sup>214</sup>

84. While we agree that study areas with at least 14 percent increase in TPIS should qualify for safety net additive support, we conclude that the Rural Task Force's proposed safety net mechanism should be modified to ensure that carriers do not receive support in excess of the incremental costs associated with new investment. We note that, with the modification we adopt below, any carrier that makes the requisite investment will receive support for the incremental expense adjustment associated with that investment as if the fund had not been capped.<sup>215</sup>

85. As proposed, the safety net additive support mechanism would allow carriers to recover "50 percent of the difference between the capped expense adjustment and the uncapped amount for the study area" in each year that the cap is implicated.<sup>216</sup> A carrier could recover more than 100 percent of the incremental expenses associated with new investment because under the Rural Task Force's proposal the safety net additive mechanism fails to isolate only the additional investment. Instead, safety net additive support would be calculated based on a carrier's total expense adjustment in the year in which the carrier qualifies for safety net additive (qualifying year), which includes the base year expense adjustment as well as the additional expense adjustment resulting from the additional investment. For example, assume that a carrier's overall expenses would make it eligible to receive support for 65 percent of its study area's average unseparated loop cost that is above 115 percent of the national average loop cost.<sup>217</sup> Further assume that in the base year the carrier receives \$1000, and that capped support is \$950. Also assume that, in the year in which the carrier qualifies for the safety net additive, the carrier's uncapped support would be \$1200, while the capped support would be \$1140. As proposed by the Rural Task Force, the carrier would receive its capped support of \$1140, plus 50 percent of the difference between the capped support and the uncapped support in the qualifying year, or \$30  $((\$1200 - \$1140 \div 2))$ . The incremental expense adjustment support not received as a result of the cap, however, is \$10  $((\$1200 - \$1000) - (\$1140 - \$950) \text{ or } (\$200) - (\$190))$ . In this example, the \$200 increase in expenses in the qualifying year is the amount that should be isolated because it represents the additional investment causing an increase in the carrier's expense adjustment. This amount should then be compared to the amount that the carrier's capped support has grown, or \$190, because that is the additional amount that the cap is already supporting without safety net additive.

86. Because the safety net additive is intended to provide support to eligible carriers that incur costs associated with additional investment, we find that safety net additive should be based on the additional expense adjustment resulting from the additional investment only.<sup>218</sup> We therefore modify the safety net additive so that, in the qualifying year, safety net additive will be determined by subtracting from the carrier's expense adjustment in the qualifying year its expense adjustment in the base year, and then subtracting from that amount the difference between the capped support in the qualifying year and the capped support in the base year. This amount will be in addition to the capped support it receives in that

---

<sup>214</sup> As discussed *infra*, section 254(e) of the Act requires that all carriers, rural and non-rural, that are certified as eligible telecommunications carriers use universal service support only for the "provision, maintenance, and upgrading of facilities and services for which the support is intended." See *infra* section IV.G; 47 U.S.C. § 254(e). As discussed in section IV.G of this Order, we have adopted a provision that requires the states to certify that the eligible telecommunications carriers operating within their jurisdiction will use universal service funds in a manner that is consistent with 254(e). See *infra* section IV.G.

<sup>215</sup> See 47 C.F.R. § 36.631.

<sup>216</sup> See Rural Task Force Recommendation at 27.

<sup>217</sup> 47 C.F.R. § 36.631.

<sup>218</sup> See Maine and Vermont Commissions Comments at 10-11 (Arguing that the mechanism as proposed by the Rural Task Force produces "support in excess of 100 percent of incremental cost").

year.<sup>219</sup> In no event shall a carrier that is eligible for safety net additive receive less support than it would normally receive under the cap. We believe that, by allowing carriers to receive the same level of support they would have received had the cap not been in effect, we encourage new investment by making support predictable while ensuring that carriers do not receive support for more than their incremental costs. Consistent with the principle of competitive neutrality, we conclude that safety net additive shall be available to competitive eligible telecommunications carriers in an amount equal to that received by the incumbent.<sup>220</sup>

87. We clarify that, if our safety additive net formula results in a negative amount, the carrier will not be eligible for safety net additive in that year. For example, it is possible that the incremental increase in expense adjustment incurred by a carrier when compared to the incremental support received by the carrier through the indexed fund may result in a negative amount. Such a result would indicate that the carrier actually received support for the incremental expense adjustment available under the safety net mechanism through operation of the cap.<sup>221</sup>

88. We adopt the Rural Task Force's proposal that, once a study area qualifies for safety net additive, the study area will receive such support in any of the remaining years of this plan in which the cap is triggered, whether or not the study area meets the 14 percent TPIS trigger in those years. Providing support in the years succeeding the qualifying year is consistent with the manner in which carriers depreciate capital costs associated with new investments. Such costs generally are not recovered in one year; rather they are recovered over multiple years. Thus, by providing carriers with support over multiple years, we give them an opportunity to receive support for more of the expenses associated with their investments. In any of the succeeding four years in which the cap is again triggered, the carrier will be eligible for the lesser of the sum of capped support and the safety net additive received in the qualifying year or uncapped support. Therefore, qualifying carriers will receive safety net additive in each year that the cap is triggered under the five-year plan we adopt in this order.

89. We find that carriers shall be required to provide written notice to the Commission and USAC in conjunction with their annual or quarterly submissions to NECA indicating that a study area meets the 14 percent TPIS trigger.<sup>222</sup> If a carrier should fail to provide written notification to the Commission and USAC, the study area that otherwise would have qualified for safety net additive will not be eligible.<sup>223</sup> By requiring written notification from the carrier, we minimize the administrative burden placed on USAC and will help control the costs associated with implementing this mechanism. To require USAC to determine eligibility would require it to monitor TPIS investment for all 873 cost study areas.

90. In the context of the modifications to the high-cost support mechanism that we adopt in this Order, we believe that safety net additive support is a reasonable means of ensuring that rural carriers that make significant investments receive adequate but not excessive support for such investments. By limiting safety net additive support to those carriers who have TPIS per-line investment increases of 14

---

<sup>219</sup> Safety net additive support = (Uncapped support in the qualifying year – Uncapped support in the base year) – (Capped support in the qualifying year – Actual support in the base year). See 47 C.F.R. § 36.631.

<sup>220</sup> See *First Report and Order*, 12 FCC Rcd at 8801-02 paras. 46-48, 8932-34 paras. 286-90.

<sup>221</sup> For example, assume that a qualifying carrier's uncapped expense adjustment in the base year is \$1000 and capped support is \$930. Further assume that in the qualifying year the carrier's uncapped expense adjustment is \$1200 and capped support is \$1164. The resulting amount of support would be a negative \$34 ((1200 – 1000) – (1164 – 930) or (200) – (234)).

<sup>222</sup> 47 C.F.R. §§ 36.611; 36.612. Rural carriers are required to make annual cost study submissions, whereas, quarterly updates are voluntary unless a competitor enters one of their disaggregation zones. See *infra* n.330.

<sup>223</sup> Once a carrier misses the filing requirement, it would need to make the requisite 14 percent TPIS investment in a subsequent year for the study area to again be eligible.

percent or more in a given year, support is tailored to those carriers who make extraordinary investment. In addition, by ensuring that carriers have a mechanism that provides support outside the cap for new investment, we encourage carriers to make these needed investments in their communities.<sup>224</sup> By crafting the mechanism to provide support based on incremental costs associated with new investments, we control for the possible overcompensation that would have occurred under the Rural Task Force's proposal.<sup>225</sup>

## 2. Mergers and Acquisitions Cap and "Safety Valve" Mechanism

### a. Background

91. Section 54.305 of our rules provides that a carrier acquiring exchanges from an unaffiliated carrier shall receive the same per-line levels of high-cost universal service support for which the acquired exchanges were eligible prior to their transfer.<sup>226</sup> Section 54.305 was adopted in the *First Report and Order* as a temporary measure aimed at discouraging carriers from transferring exchanges merely to increase their share of high-cost universal service support during the Commission's transition to universal service support mechanisms that provide support to carriers based on the forward-looking economic cost of operating a given exchange.<sup>227</sup> The Commission was concerned that, until support for all carriers is based on a forward-looking economic costs methodology, potential universal service payments may unduly influence a carrier's decision to purchase exchanges from other carriers.<sup>228</sup>

92. Under section 54.305 of the Commission's rules, if a rural carrier purchases an exchange from a non-rural carrier that receives support based on the Commission's new universal service support mechanism for non-rural carriers,<sup>229</sup> the loops of the acquired exchange receive the same per-line support as calculated at the time of the transfer under the new non-rural mechanism, regardless of the rural carrier's cost characteristics or the support the rural carrier purchasing the exchange may receive for any other exchanges.<sup>230</sup> High-cost support mechanisms that are subject to the limitations in section 54.305 include non-rural carrier forward-looking high-cost support,<sup>231</sup> interim hold-harmless support for non-rural carriers,<sup>232</sup> rural carrier high-cost loop support, local switching support,<sup>233</sup> and Long Term Support (LTS).<sup>234</sup>

---

<sup>224</sup> *But cf.* California Commission Comments at 9; CUSC Comments at 8.

<sup>225</sup> Consistent with the 254(e) certification requirements we adopt today, state commissions shall certify that a carrier's use of safety net support is consistent with section 254(e). *See infra* para. 187.

<sup>226</sup> 47 C.F.R. § 54.305.

<sup>227</sup> *See First Report and Order*, 12 FCC Rcd at 8942-43 para. 308.

<sup>228</sup> *Id.*

<sup>229</sup> *See supra* description of non-rural high-cost support mechanism at para. 15.

<sup>230</sup> *See First Report and Order*, 12 FCC Rcd at 8942-43 para. 308.

<sup>231</sup> *See* 47 C.F.R. § 54.309.

<sup>232</sup> In the event that support provided to a non-rural carrier in a given state is less under the forward-looking methodology, the carrier is eligible for interim hold-harmless support, which is equal to the amount of support for which the non-rural carrier would have been eligible under the Commission's existing high-cost support mechanism. *See* 47 C.F.R. § 54.311. The Commission recently adopted the recommendations of the Joint Board for phasing down the interim hold-harmless support for non-rural carriers. *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Thirteenth Report and Order and Further Notice of Proposed Rulemaking, FCC 00-428 (rel. Dec. 8, 2000). The Commission adopted measures to phase down interim hold-harmless support, excluding LTS, through \$1.00 reductions in average monthly, per-line support beginning January 1, 2001, and every year thereafter until there is no more interim hold-harmless support. *Id.* at para. 1. The Commission also adopted the Joint Board's recommendation not to phase down interim hold-harmless support for eligible exchanges transferred to rural carriers until the Commission reexamines section 54.305 or until rural high-cost reform is complete. *Id.* at para. 21. Interim hold-harmless support for exchanges transferred to non-rural carrier will be (continued....)

To the extent that a carrier acquires exchanges receiving any of these forms of support, the acquiring carrier will receive the same per-line levels of support for which the acquired exchanges were eligible prior to their transfer.

93. The Rural Task Force outlined principles for providing universal service support to exchanges acquired by rural carriers. The Rural Task Force acknowledged the valid policy considerations underlying section 54.305 of our rules, while recognizing that the operation of section 54.305 may discourage carriers from acquiring high-cost exchanges that currently are eligible for limited amounts of universal service support.<sup>235</sup> According to the Rural Task Force, customers in high-cost rural exchanges involving transfers should not be “doomed” to poor service because the selling carrier has limited access to universal service support funds.<sup>236</sup> The Rural Task Force also stated that universal service support should “provide incentives for new investment in rural America.”<sup>237</sup> On the other hand, the Rural Task Force asserted that a mere transfer of ownership should not result in increased support for acquired lines. The Rural Task Force stated that “universal service support also should not artificially inflate the price on sale/transfer transactions.”<sup>238</sup>

94. The Rural Task Force therefore recommended that the Commission establish an appropriate “safety valve” mechanism, which would enable rural carriers acquiring access lines to receive additional support over a period of five years reflecting “post-transaction investment made to enhance the infrastructure of and improve the service in these exchanges.”<sup>239</sup> The Rural Task Force also stated that any transferred support or additional support under the safety valve mechanism should be excluded from the re-based cap on high-cost loop support.<sup>240</sup> Finally, the Rural Task Force stated that the safety valve mechanism should be capped at some appropriate level.

95. The Rural Task Force provided an example of a safety valve mechanism in Appendix D of its Recommendation.<sup>241</sup> The Rural Task Force noted, however, that the safety valve example was used illustratively (*i.e.*, it does not represent a consensus of the Rural Task Force members).<sup>242</sup> In Appendix D, the Rural Task Force proposed that safety valve support should be based on the difference between an “index year expense adjustment” calculated for the acquired exchanges in accordance with section 36.631 of the Commission’s rules and subsequent year expense adjustments.<sup>243</sup> The “expense adjustment” formulas included in section 36.631 of the Commission’s rules are used to calculate high-cost loop support for rural carriers. A carrier’s expense adjustment is based on the relationship between a carrier’s study

(Continued from previous page) \_\_\_\_\_  
phased down over the same time period as the seller’s support would have been phased down. *Id.* at para. 22. The Commission also sought comment on whether to continue applying section 54.305 to transfers of telephone exchanges between non-rural carriers following phase-down. *Id.* at paras. 23-24.

<sup>233</sup> See *supra* discussion at n.21.

<sup>234</sup> See *supra* discussion at n.21.

<sup>235</sup> See Rural Task Force Recommendation at 29-30.

<sup>236</sup> See *id.*

<sup>237</sup> *Id.*

<sup>238</sup> *Id.*

<sup>239</sup> See *id.* at 29.

<sup>240</sup> See *id.*; see also *supra* discussion at para. 45.

<sup>241</sup> See Rural Task Force Recommendation at Appendix D.

<sup>242</sup> See Rural Task Force Comments at 6-7.

<sup>243</sup> See Rural Task Force Recommendation at Appendix D-1.

area average unseparated loop cost per working loop and the national average cost per loop.<sup>244</sup> The index year expense adjustment would be the study area's high-cost loop support expense adjustment calculated at the end of the acquiring company's first year of operations.<sup>245</sup> Fifty percent of any positive difference between subsequent year expense adjustments and the index year expense adjustment would be designated as safety valve support and would be provided in addition to transferred support amounts available under section 54.305. The Rural Task Force's example also limited the total safety valve support available to all eligible study areas to no more than five percent of the indexed high-cost loop fund cap for rural carriers.<sup>246</sup> Moreover, the Rural Task Force's example created a new study area for each transfer of exchanges and excluded transferred exchanges from the rural growth factor.<sup>247</sup> The Rural Task Force's example also made per-loop transferred support portable to competitive eligible telecommunications carriers.<sup>248</sup>

96. The Joint Board generally supported the Rural Task Force's proposal for providing additional support to rural carriers that acquire high-cost exchanges and make post-transaction investments to enhance the network infrastructure, but urged the Commission to address issues relating to the implementation of the safety valve mechanism.<sup>249</sup> First, the Joint Board urged the Commission to consider how to distribute safety valve support if the total amount of eligible safety valve support exceeds the cap of five percent of the rural carrier portion of the indexed high-cost loop support fund.<sup>250</sup> Next, the Joint Board asked the Commission to examine whether it would be more appropriate to define the index year expense adjustment for purposes of calculating safety valve support as the year prior to the subsequent year expense adjustment.<sup>251</sup> In addition, the Joint Board urged the Commission to address whether a carrier's safety valve support should transfer to a different carrier as a result of a subsequent transfer of exchanges. Finally, the Joint Board requested that the Commission consider whether safety valve support is frozen when a competitive eligible telecommunications carrier enters the study area.<sup>252</sup>

## b. Discussion

97. We agree with the Rural Task Force, the Joint Board, and several commenters that we should provide additional support to rural carriers that acquire high-cost exchanges and make post-transaction investments to enhance network infrastructure.<sup>253</sup> We continue to believe that section 54.305 serves the important purpose of discouraging carriers from transferring exchanges merely to increase their share of high-cost universal service support during the Commission's transition to universal service support mechanisms that provide support to all carriers based on the forward-looking economic cost of operating a given exchange.<sup>254</sup> On other hand, we recognize that the section 54.305 of our rules may have some

---

<sup>244</sup> See 47 C.F.R. § 36.631.

<sup>245</sup> See Rural Task Force Recommendation at Appendix D.

<sup>246</sup> See *id.*

<sup>247</sup> See *id.*

<sup>248</sup> See *id.*

<sup>249</sup> See *Joint Board Recommended Decision* at para. 16.

<sup>250</sup> See *id.*

<sup>251</sup> See *id.* at para. 16 n.47. As currently proposed, the index year expense adjustment is the study area's high-cost loop support expense adjustment calculated at the end of the acquiring company's first year of operations.

<sup>252</sup> *Id.*

<sup>253</sup> See *id.* at para. 16. See, e.g., Alaska Rural Coalition Reply Comments at 2-3; Innovative Telephone Comments 24; Interstate Telecom Group Comments at 9.

<sup>254</sup> See *First Report and Order*, 12 FCC Rcd at 8942-43 para. 308.

unintended consequences. Specifically, the operation of section 54.305 may discourage rural carriers from acquiring high-cost exchanges from carriers with low average costs and may prevent rural carriers from receiving support for new investments in recently-acquired high-cost exchanges. As a result, we do not agree with commenters that support retaining section 54.305 without any modifications.<sup>255</sup> We conclude that section 54.305 should be retained, but modified to provide additional support to rural carriers that make substantial investment after acquiring exchanges.<sup>256</sup> In reaching this conclusion, we are mindful that the Rural Task Force's principles for providing additional support for significant post-transaction investments in the infrastructure of acquired exchanges represent a consensus of the Rural Task Force members. We therefore agree with commenters that oppose outright elimination of section 54.305 of our rules,<sup>257</sup> and do not agree with the MAG and certain commenters that we should entirely eliminate section 54.305.<sup>258</sup>

98. As discussed in greater detail below, we adopt certain aspects of the Rural Task Force's example of a safety valve mechanism. We conclude that a safety valve mechanism, as clarified herein, will provide appropriate incentives for rural carriers operating recently-acquired exchanges to invest in rural infrastructure. We conclude that safety valve support should be provided for up to 50 percent of any positive difference between the rural incumbent local exchange carrier's index year expense adjustment for the acquired exchanges and subsequent year expense adjustments. We agree with the Rural Task Force's example and conclude that the total safety valve support available to all eligible study areas should be limited to no more than five percent of rural incumbent local exchange carrier support available from the annual high-cost loop fund, as set forth in the Rural Task Force's example.<sup>259</sup> We do not agree with the Rural Task Force's example that a new study area should be created for each transfer of exchanges.<sup>260</sup> We agree that per-loop transferred support should be transferable to competitive eligible telecommunications carriers.<sup>261</sup> In addition, consistent with the Rural Task Force's principles for providing universal service support to acquired or transferred exchanges, we conclude that safety valve support

---

<sup>255</sup> See, e.g., Ad Hoc Telecommunications User Committee Reply Comments at 16-17; WorldCom Reply Comments at 9-10. See also, e.g., ASCENT Comments in CC Docket No. 00-256 at 6; AT&T Comments in CC Docket No. 00-256 at 18-19; California Commission Comments in CC Docket No. 00-256 at 25-26; CUSC Comments in CC Docket No. 00-256 at 19; Florida Comments in CC Docket No. 00-256 at 5; WorldCom Comments in CC Docket No. 00-256 at 17-18.

<sup>256</sup> See, e.g., CenturyTel Comments at 3-8; GVNW Consulting Comments at 1-2; Innovative Telephone Comments at 24; NECA Comments at 9; Texas Commission Comments at 6; SDITC Comments at 7-8; Sprint Comments at 4; Telecom Consulting Associates Comments at 12; Western Alliance Comments at 8.

<sup>257</sup> See, e.g., Ad Hoc Telecommunications User Committee Reply Comments at 16-17; California Commission Comments at 13; WorldCom Reply Comments at 9-10; See also AT&T Comments in CC Docket No. 00-256 at 18-19; California Commission Comments in CC Docket No. 00-256 at 25; WorldCom Comments in CC Docket No. 00-256 at 17-18.

<sup>258</sup> See MAG Comments in CC Docket No. 00-256 at 29-30; see also Letter of William F. Maher, Jr. to Magalie Roman Salas, FCC, dated November 21, 2000 ("The plan is intended to propose the deletion of current section 54.305 . . . from the Commission's rules."). See also, e.g., CenturyTel Comments at 5; Fred Williamson & Assoc. Comments at 11; GVNW Consulting Comments at 1; Iowa Telecom Reply Comments at 2-3; NECA Comments at 9; NRTA, OPASTCO, & USTA Comments at 4; NTCA Comments at 4-5; Telecom Consulting Associates Comments at 12; see also Alaska Rural Coalition Comments in CC Docket No. 00-256 at 3-4; Innovative Telephone Comments in CC Docket No. 00-256 at 11-13; MAG Comments in CC Docket No. 00-256 at 29-30; Summit Tel. Co. Comments in CC Docket No. 00-256 at 3; Wisconsin Commission Comments in CC Docket No. 00-256 at 4-5.

<sup>259</sup> As discussed in section IV.C.1.b, we agree that exchanges transferred to rural telephone companies should be excluded from the rural incumbent local exchange carrier portion of the high-cost loop fund and from the rural growth factor. See *supra* discussion at paras. 45, 53.

<sup>260</sup> See *infra* discussion at para. 110.

<sup>261</sup> See *infra* discussion at para. 113.

should not be frozen whenever a competitor enters a study area eligible for such support.<sup>262</sup>

99. *Index Year Expense Adjustment.* We agree with the Rural Task Force's example that, for purposes of determining a rural carrier's safety valve support for acquired exchanges, the index year expense adjustment shall be defined as the high-cost loop support expense adjustment for the acquired exchanges calculated at the end of the company's first year operating the exchanges.<sup>263</sup> Acquiring carriers will establish an index year expense adjustment for the acquired exchange through cost data submitted in accordance with section 36.611 or section 36.612 of our rules.<sup>264</sup> Under section 36.611 of the Commission's rules, all incumbent local exchange carriers, including rural carriers, submit loop cost data to NECA on an annual basis.<sup>265</sup> Under section 36.612 of our rules, rural carriers have the option of submitting loop cost data to NECA on a quarterly basis.<sup>266</sup> NECA compiles and analyzes these data to determine an incumbent local exchange carrier's study area expense adjustment, which is based, in part, on the relationship between a carrier's study area average unseparated loop cost per working loop and the national average cost per loop.<sup>267</sup> For carriers establishing an index year for acquired exchanges pursuant to section 36.611, the index year for the acquired exchange(s) shall commence at the beginning of the next calendar year after the transfer of said exchanges. For carriers establishing an index year for acquired exchanges pursuant to section 36.612, the index year for the acquired exchange(s) shall commence at the beginning of the next calendar quarter after the transfer of said exchanges. An acquiring carrier's expense adjustment for the acquired exchanges in subsequent years shall end on the same calendar quarter. By submitting loop cost data for acquired exchanges on a quarterly, as opposed to annual, basis, a carrier could establish its index year expense adjustment earlier and therefore potentially could begin receiving safety valve support earlier. In order to assist USAC in the administration of the safety valve mechanism, rural carriers shall provide written notice to USAC of when their index year has been established for purposes of calculating eligibility for safety valve support.

100. We conclude that basing safety valve support on the difference between an acquiring carrier's expense adjustment at the end of its first year of operations and subsequent year expense adjustments reasonably approximates a carrier's new investments in the acquired exchanges. We therefore believe that the safety valve mechanism will provide acquiring rural carriers with support for new investments that is within the range of sufficiency envisioned by the principles espoused in section 254(b)(5) of the Act. We also believe that calculating safety valve support on this basis will provide acquiring carriers with predictability as to whether they will qualify for safety valve support in a given year.<sup>268</sup> In particular, because we freeze the national average loop cost at \$240.00, as long as an acquiring rural carrier's study area average unseparated loop cost per working loop is more in the current year than

---

<sup>262</sup> See *infra* discussion at paras. 114-115. We note that the Competitive Universal Service Coalition (CUSC) requests that the Commission clarify that exchange sales or transfers to smaller incumbent LECs will not affect preexisting designations of competitive eligible telecommunications carriers. See CUSC Comments App. A at 17-18. In particular, CUSC requests that the Commission clarify that existing competitive eligible telecommunications carriers should not be required to return to the designating commission for a public interest finding or serve additional areas if the exchanges they serve are sold to a carrier that satisfies the definition of "rural telephone company." See *id.* Because this issue does not directly relate to the implementation of the safety valve mechanism or any other aspect of the Rural Task Force Recommendation, we do not address it in this order.

<sup>263</sup> See Rural Task Force Recommendation at Appendix D.

<sup>264</sup> See 47 C.F.R. §§ 36.611, 36.612.

<sup>265</sup> See 47 C.F.R. § 36.611.

<sup>266</sup> See 47 C.F.R. § 36.612.

<sup>267</sup> See 47 C.F.R. § 36.631.

<sup>268</sup> *Id.*

in the index year, the carrier likely will qualify for safety valve support.<sup>269</sup> As discussed above, a carrier's expense adjustment is based on the relationship between the carrier's study area average unseparated loop cost per working loop and the national average cost per loop.<sup>270</sup>

101. Consistent with section 254(d) of the Act, we also conclude that the proposed methodology for calculating safety valve support based on the difference between the acquired exchange's index year expense adjustment and subsequent year expense adjustments will minimize burdens on carriers to contribute to the universal service mechanisms.<sup>271</sup> The Rural Task Force's proposal will ensure that acquiring rural carriers receive no more than 50 percent of the difference between their acquired exchange expense adjustment for the first full year of operation of the acquired exchange and subsequent year expense adjustments. In this manner, acquiring carriers will only receive safety valve support for new investments in rural infrastructure.

102. We decline to modify the Rural Task Force's proposal by defining the index year expense adjustment, for purposes of determining the annual safety valve support amounts in a particular year, as the year immediately prior to that particular year's expense adjustment.<sup>272</sup> This modified proposal would prevent an acquiring carrier from receiving safety valve support if the carrier's expense adjustment does not increase in a given year. For example, if a carrier depreciates an investment made in year one equally over the subsequent four years, the carrier would not be able to receive support for amounts depreciated in each of those four years if the index year expense adjustment is defined as the year prior to that particular year's expense adjustment. Under this scenario, the carrier would only be eligible for safety valve support in the first year. Because there would be no year-to-year increase in the carrier's expense adjustment after the first year, the carrier would be ineligible for safety valve support in subsequent years. This modified proposal also may create incentives for a carrier to include all of its investment in one year's expense adjustment in order to maximize receipt of safety valve support. Similarly, this proposal may simply discourage carriers from making post transaction investments in acquired exchanges because they would be unable to recover costs associated with such investment. We therefore decline to define the index year expense adjustment as the year prior to the subsequent year expense adjustment.

103. We also decline to define the index year expense adjustment as prior to the end of an acquiring carrier's first year of operations of the acquired exchange.<sup>273</sup> Because rural carriers most often acquire high-cost exchanges from non-rural carriers operating in large study areas with lower average costs,<sup>274</sup> we conclude that it would be inappropriate for acquiring carriers to rely on the cost data of selling carriers in establishing the index year expense adjustment. We also conclude that carriers should not be permitted to rely on projected expenses when establishing their index year expense adjustment. Such a proposal would provide acquiring carriers with incentives to underestimate their expenses in the index year

---

<sup>269</sup> See *supra* discussion at paras. 55 to 59. We note, however, that if the sum of the actual high-cost loop support nationwide exceeds the indexed cap on the high-cost loop support fund, NECA increases the amount of the national average loop cost in order to ensure that the total amount of high-cost loop support disbursed does not exceed the indexed cap. See *supra* para. 58.

<sup>270</sup> See *supra* discussion at para. 95.

<sup>271</sup> See 47 U.S.C. § 254(d).

<sup>272</sup> See *Joint Board Recommended Decision* at para. 16 n.47.

<sup>273</sup> See CenturyTel Comments at 5-7; Interstate Telecom Group Comments at 11; NECA Comments at 9; NTCA Comments at 7-9.

<sup>274</sup> Even though non-rural carriers currently receive high-cost support based on forward-looking economic costs, non-rural carriers are required to report their study area average costs to NECA on an annual and quarterly basis in accordance with sections 36.611 and 36.612 of our rules. See 47 C.F.R. §§ 36.611, 36.612. Such costs are used in determining the national average loop cost. See 47 C.F.R. §§ 36.621, 36.622.

in order to maximize future safety valve support. Establishing the index year expense adjustment prior to the end of acquiring carriers' first year of operations also would result in additional filing requirements beyond those included in sections 36.611 and 36.612 of our rules.<sup>275</sup> We therefore decline to adopt proposals to define the index year expense adjustment prior to the end of an acquiring carrier's first year of operations.

104. We also conclude that certain clarifications are necessary to ensure that the safety valve mechanism does not enable carriers to receive excessive amounts of high-cost universal service support for acquired exchanges. We clarify that in no event shall a rural carrier's acquired exchanges receive more through the transfer of high-cost support and the safety valve mechanism than it would receive in uncapped high-cost loop support. That is, a study area's safety valve loop cost expense adjustment cannot exceed the difference between the acquired exchanges' uncapped annual study area loop cost expense adjustment calculated pursuant to section 36.631 of our rules and transferred support amounts available under section 54.305(a) of our rules. Without this limitation, a rural carrier, for example, could acquire exchanges eligible for \$50 per loop in targeted interim hold-harmless support and an additional \$25 per loop in safety valve support, while only being eligible for \$60 per loop in uncapped high-cost loop support for the acquired exchanges. This would equal a \$15 per-loop over-recovery.

105. As proposed, the Rural Task Force's example would enable carriers with acquired exchanges that are not eligible for high-cost loop support to receive safety valve support.<sup>276</sup> We clarify that safety valve support only will be available to rural carriers that would otherwise qualify for high-cost loop support for the acquired exchanges under section 36.631 of our rules.<sup>277</sup> Consistent with the Commission's reasons for adopting section 54.305 of our rules, these clarifications will ensure that the potential for safety valve support does not unduly influence a rural carrier's decision to purchase exchanges from another carrier.<sup>278</sup>

106. We also clarify that acquiring rural carriers shall not be permitted to qualify for safety net additive support for acquired exchanges that are subject to section 54.305 of our rules. As discussed above, both safety net additive support and safety valve support enable rural carriers to recover above-the-cap support for new investments.<sup>279</sup> Safety net additive applies to new investments in existing exchanges while safety valve support applies to new investments in acquired exchanges. Permitting carriers to recover both safety net additive and safety valve support for investments in the same exchanges could result in the double recovery of costs. We therefore clarify that acquiring carriers shall not be permitted to qualify for safety net additive support for acquired exchanges and by application of this same analysis, we also conclude that safety net additive support shall not transfer with acquired exchanges.<sup>280</sup>

107. *Five Percent Cap on Safety Valve Support.* We agree with the Rural Task Force's example that the total amount of safety valve support available to all eligible study areas should be limited to no more than five percent of rural incumbent local exchange carrier support available from the annual

---

<sup>275</sup> See 47 C.F.R. §§ 36.611, 36.612.

<sup>276</sup> Because the benchmark or index year expense adjustment used in determining safety valve support is based on the carrier's own costs, a carrier potentially could qualify for safety valve support without also qualifying for high-cost loop support.

<sup>277</sup> See 47 C.F.R. § 36.631.

<sup>278</sup> See *First Report and Order*, 12 FCC Rcd at 8942-43 para. 308.

<sup>279</sup> See *supra* discussion at paras. 79-84, 99-101.

<sup>280</sup> See *infra* discussion at para. 113.

high-cost loop fund.<sup>281</sup> To the extent that rural carriers receive less than the indexed cap on the high-cost loop fund, the five percent cap on the safety valve mechanism shall be based on the lesser amount. Just as the indexed cap is a reasonable means of limiting the overall growth of the portion of the high-cost loop fund that is distributed to rural incumbent local exchange carrier study areas,<sup>282</sup> we believe that a five percent cap on the safety valve mechanism will prevent uncontrollable growth. A five percent cap also will help minimize the burden on contributors to the universal service support mechanisms, while allowing the safety valve mechanism to grow at a rate that will encourage investment in rural areas.<sup>283</sup>

108. We further conclude that a five percent cap on the safety valve mechanism will ensure the availability of specific and predictable support for new investment in acquired exchanges while at the same time not encouraging speculative purchases of exchanges for more than their book value.<sup>284</sup> Based on estimates of growth in the rural carrier portion of the modified high-cost loop fund provided by the Rural Task Force, we project that the five percent cap on the safety valve mechanism will reach approximately \$63 million annually by June 30, 2006.<sup>285</sup> It is unlikely that annual demand for safety valve support will exceed the proposed five percent cap. This conclusion is based on an analysis of projected transfers to rural carriers and annual increases in per line high-cost loop support for rural carriers, taking into account increases in the transfer of lines to rural carriers over time and the fact that rural carriers may have higher than average increases in annual expense adjustments for acquired exchanges. We therefore do not agree with commenters that no cap, or a higher cap, should be placed on the safety valve mechanism.<sup>286</sup>

109. As discussed above, the Joint Board urges the Commission to consider the distribution of safety valve support if the total amount of eligible safety valve support exceeds the cap of five percent of the rural carrier portion of the indexed high-cost loop support fund.<sup>287</sup> We agree with commenters that, if the total amount of eligible safety valve support in a given year exceeds the cap of five percent of the rural carrier portion of the indexed high-cost loop support fund, the percentage used to calculate the safety valve loop cost expense adjustment will be reduced until all safety valve support fits under the five percent cap.<sup>288</sup> In such years, carriers eligible for safety valve support will receive less than 50 percent of the positive difference between the subsequent year expense adjustment and the index year expense adjustment.<sup>289</sup> We believe that such a *pro rata* reduction will ensure that all carriers eligible for safety

---

<sup>281</sup> See Rural Task Force Recommendation at Appendix D. We note that the five percent cap was included in the Rural Task Force's example of a safety valve mechanism for illustrative purposes only. See Rural Task Force Comments at 6.

<sup>282</sup> See *Fourth Order on Reconsideration*, 13 FCC Rcd at 5343 para. 39.

<sup>283</sup> The five percent cap on safety valve support will grow as the indexed cap on the high-cost loop fund grows by the rural growth factor, discussed *supra* at paras. 48-53.

<sup>284</sup> See 47 U.S.C. § 254(b)(5).

<sup>285</sup> See Letter from William R. Gillis, Chair, Rural Task Force, to Magalie Roman Salas, FCC, dated November 10, 2000, at Attachment 2. This estimate assumes that the indexed cap on the high-cost loop fund will be triggered in 2006. To the extent that rural carriers are eligible for less high-cost loop support than is available from the indexed cap, the amount of available safety valve support would be based on the lesser amount.

<sup>286</sup> See NTCA Comments at 9-10; SDITC Comments at 8; *but see* California Commission Comments at 13.

<sup>287</sup> See *Joint Board Recommended Decision* at para. 16.

<sup>288</sup> See AT&T Comments at 13; CUSC Comments at 5; Innovative Telephone Comments at 25; NECA Comments at 9; Western Alliance Comments at 7-8.

<sup>289</sup> In contrast, under section 36.622 of our rules, if the sum of loop costs nationwide exceeds the indexed cap on the high-cost support fund, certain carriers with above average loop costs would not receive high-cost loop support. See *supra* discussion at para. 31. The national average loop cost would be increased in order to ensure that the total amount of high-cost loop support disbursed does not exceed the indexed cap.

valve support continue to receive explicit and predictable support for new investments in infrastructure.

110. *Creation of New Study Areas.* We decline to adopt the proposal in the Rural Task Force safety valve example to create a new study area for each transfer of exchanges.<sup>290</sup> The Commission froze all study area boundaries effective November 15, 1984, and an incumbent local exchange carrier must apply to the Commission for a waiver of the study area boundary freeze if it wishes to sell or purchase additional exchanges and the transaction requires the alteration of a study area boundary.<sup>291</sup>

111. We are concerned that the creation of a new study area for each transfer of exchanges would enable carriers to gain an unfair advantage from the high-cost support mechanisms. For example, under the safety valve, an acquiring carrier could take advantage of the high-cost support mechanisms by structuring a transaction to create separate study areas that satisfy the definition of rural telephone company,<sup>292</sup> and, therefore, qualify for rural high-cost support, including safety valve support. An acquiring carrier also could structure its transaction so that higher-cost exchanges are isolated into a separate study area.<sup>293</sup> Such a result would undermine the goals the Commission sought to achieve when it froze all study area boundaries. The study area freeze is intended to prevent carriers from setting up high-cost exchanges within their existing service territory as separate study areas to maximize high-cost support.<sup>294</sup> As a result, the Commission consistently has rejected requests to create multiple study areas in connection with acquisitions requiring study area waivers.<sup>295</sup> The Commission specifically has concluded that, where an incumbent local exchange carrier is acquiring exchanges in a state in which it already operates, the creation of an additional study area is unwarranted.<sup>296</sup> We therefore do not adopt the proposal in the Rural Task Force safety valve example to automatically create a new study area with each new transfer of

---

<sup>290</sup> See 47 C.F.R. § 36 Appendix-Glossary (defining "study area").

<sup>291</sup> See *MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board*, CC Docket Nos. 78-72, 80-286, Recommended Decision and Order, 49 Fed. Reg. 48325 (1984) (*1984 Joint Board Recommended Decision*); Decision and Order, 50 Fed. Reg. 939 (1985) (*Order Adopting Recommendation*); see also *Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board*, CC Docket No. 80-286, Notice of Proposed Rulemaking, 5 FCC Rcd 5974 (1990).

<sup>292</sup> See 47 C.F.R. § 51.5.

<sup>293</sup> We also note that in the absence of section 54.305 of our rules, the isolation of higher-cost exchanges into a separate study area would enable an acquiring carrier to take advantage of the high-cost loop support mechanism by reporting average loop costs in the higher-cost study area further above the national average loop cost than would be possible if the exchanges remained consolidated in a single study area with lower-cost exchanges. See 47 C.F.R. §§ 36.631, 54.305. In the absence of 54.305, the isolation of higher-cost exchanges into a separate study area also would enable an acquiring carrier to gain an unfair advantage under local switching support, which permits carriers operating in study areas with less than 50,000 access lines to assign a greater portion of local switching costs to the interstate jurisdiction. See 47 C.F.R. §§ 54.301, 54.305.

<sup>294</sup> See *1984 Joint Board Recommended Decision*, 49 Fed. Reg. 48325 at para. 66; *Order Adopting Recommendation*, 50 Fed. Reg. 939 at para. 1.

<sup>295</sup> See, e.g., *Petition for Waivers Filed by Columbine Telephone Company, Inc., Silver Star Telephone Company, Inc., and U S WEST Communications, Inc., Concerning Section 61.41(c)(2) and 69.3(e)(11) and the Definition of "Study Area" Contained in the Part 36 Appendix-Glossary of the Commission's Rules*, AAD 96-169, Memorandum Opinion and Order, 12 FCC Rcd 3622, 3627-28 para. 12 (Acc. Aud. Div. 1997) (*Columbine Telephone Company*); *US West Communications, Inc. and Nemont Cooperative, Inc., Project Telephone Company, and Valley Telecommunications, Inc., Joint Petition for Waiver of the Definition of "Study Area" contained in Part 36, Appendix-Glossary of the Commission's Rules and Petition for Waiver of Sections 61.41(c) and 69.3(e)(11) of the Commission's Rules*, AAD 93-87, Memorandum Opinion and Order, 9 FCC Rcd 721, 723 paras. 14-15 (Com. Car. Bur. 1994).

<sup>296</sup> See, e.g., *Columbine Telephone Company*, 12 FCC Rcd at 3628 para. 12.

exchanges.

112. For similar reasons, we also decline to adopt a proposal in the MAG plan to permit rate-of-return carriers to alter the boundaries of their study areas without obtaining a waiver of the study area definition.<sup>297</sup> As discussed above, the study area freeze is intended to prevent carriers from setting up high-cost exchanges within their existing service territories as separate companies to maximize high-cost support. The MAG proposal would enable rate-of-return carriers to alter the boundaries of study areas in order to maximize high-cost loop support, potentially to the detriment of other carriers receiving support because of the indexed cap on the high-cost loop fund.<sup>298</sup> The MAG proposal particularly would enable carriers to maximize their eligibility for safety valve support. We therefore decline to adopt the MAG proposal to permit rate-of-return carriers to alter study area boundaries without obtaining a waiver of the study area definition.

113. *Transfer of Above-the-Cap Support with Acquired Exchanges.* We conclude that above-the-cap support, such as safety valve support or safety net additive support, should not transfer with acquired exchanges.<sup>299</sup> Rather, subsequent acquiring carriers will have an opportunity to qualify for safety valve support based on their own costs for the acquired exchanges.<sup>300</sup> The subsequent acquiring rural carrier will be permitted to receive safety valve support representing up to 50 percent of any positive difference between the rural carrier's index year expense adjustment and subsequent year expense adjustments. To allow otherwise would be to relieve the subsequent acquiring rural carrier of the requirement that they make new investments in rural infrastructure in order to receive safety valve support.<sup>301</sup> This conclusion also is consistent with our decision not to permit rural carriers to qualify for safety net additive support for acquired exchanges.<sup>302</sup>

114. *Safety Valve Support for Competitive Study Areas.* We agree with the Rural Task Force's example that per-loop equivalent amounts of safety valve support should be portable to competitive eligible telecommunications carriers. According to the principle of competitive neutrality adopted by the Commission and recommended by the Joint Board, universal service support mechanisms and rules should neither unfairly advantage nor disadvantage one provider over another.<sup>303</sup> Consistent with this principle, the Commission implemented the universal service principles in section 254 of the Act to ensure that universal service support is "portable," in essence, available to all competing eligible telecommunications carriers.<sup>304</sup> We therefore conclude that per-loop equivalents of safety valve support should be portable to competitive eligible telecommunications carriers.

115. Consistent with our decision in section IV.C.3. below, we also conclude that safety valve support should not be "frozen" when a competitive eligible telecommunications carrier enters a study area. In its *Recommended Decision*, the Joint Board asks the Commission to consider whether safety valve support is frozen when a competitive eligible telecommunications carrier enters the study area, just as high-cost loop support would be frozen when a competitive eligible telecommunications carrier enters the

---

<sup>297</sup> See *MAG NPRM*, 16 FCC Rcd at 464 para. 12.

<sup>298</sup> See *ASCENT Comments* in CC Docket No. 00-256 at 6; *WorldCom Comments* in CC Docket No. 00-256 at 17-18.

<sup>299</sup> See *Joint Board Recommended Decision* at para. 16.

<sup>300</sup> See, e.g., *CUSC Comments* at 6; *NECA Comments* at 10.

<sup>301</sup> See *Rural Task Force Recommendation* at 29-30.

<sup>302</sup> See *supra* discussion at para. 106.

<sup>303</sup> See *First Report and Order*, 12 FCC Rcd at 8801-02 paras. 46-48, 8932-34 paras. 286-90.

<sup>304</sup> See 47 C.F.R. § 54.307; see also *First Report and Order*, 12 FCC Rcd at 8932, para. 287.

incumbent's service area.<sup>305</sup> We believe that such an approach, which would freeze per-line safety valve support upon competitive entry in a study area, would unduly dissuade investment in new infrastructure. Under such an approach, the rural incumbent local exchange carrier would receive the same fixed amount of per-line safety valve support regardless of how much it invests in its telecommunications infrastructure. In this regard, affected carriers would be relieved of the requirement that they demonstrate that they have made new investment in rural infrastructure. We believe that such concerns outweigh the potential that per-line support amounts might escalate over time as incumbent carriers lose lines to competitors.<sup>306</sup>

116. *Reporting Requirements for Carriers with Transferred Exchanges.* In order to ensure that rural carriers receive the appropriate amount of high-cost support for acquired and existing exchanges, companies incorporating acquired exchanges into existing study areas consistently have been required to submit, as part of their universal service data submission in accordance with section 36.611 of our rules, a schedule showing their methodology for excluding the costs associated with the acquired exchanges from the costs associated with their pre-acquisitions study areas.<sup>307</sup> To receive safety valve support, rural telephone companies also will need to segregate costs associated with the operation of acquired and existing exchanges in order for USAC to ultimately determine an acquiring carrier's eligibility for such support. We therefore clarify that rural telephone companies that incorporate acquired exchanges into existing study areas should exclude the costs associated with the acquired exchanges from the costs associated with the pre-acquisition study areas in annual universal service data submissions used to determine eligibility for high-cost loop support. Acquiring rural carriers shall separately provide the information listed in section 36.611 of our rules for both acquired and existing exchanges, as if these two categories of exchanges constitute separate study areas.

117. Consistent with the Rural Task Force's proposal, we also clarify that, once relevant regulatory approvals are obtained and the transaction is closed, the rural carrier shall provide written notice to USAC that they have acquired access lines that may become eligible for safety valve support.<sup>308</sup> Rural carriers also shall provide written notice to USAC of when their index year has been established for purposes of calculating eligibility for safety valve support. Such notifications will assist USAC in the administration of the safety valve mechanism.

118. USAC will then determine whether acquired exchanges qualify for safety valve support based on expense adjustments calculated by NECA in accordance with section 36.631 of the Commission's rules.<sup>309</sup> Once USAC determines that an acquired exchange does indeed satisfy the requirements for safety valve support, the amount of support in the qualifying year will be up to 50 percent of any positive difference between the rural carrier's index year expense adjustment and subsequent year expense adjustments, subject to the limitations described above.

119. *Retroactive Application of Safety Valve.* We decline to apply the safety valve mechanism retroactively to all carriers currently operating exchanges subject to section 54.305 of our

---

<sup>305</sup> See *Joint Board Recommended Decision* at para. 16.

<sup>306</sup> See *infra* discussion at para. 129.

<sup>307</sup> See, e.g., *ATEAC, Inc., Alaska Telephone Company, Arctic Slope Telephone Association Cooperative, Inc., Interior Telephone Company, Inc., Mukluk Telephone Company, Inc., and United-KUC, Inc., Petition for Waiver of the Definition of "Study Area" Contained in Part 36, Appendix-Glossary of the Commission's Rules*, DA 01-101, at para. 8 (Acc. Pol. Div. rel. Jan. 17, 2001).

<sup>308</sup> Consistent with the 254(e) certification requirements we adopt today, state commissions shall certify that a carrier's use of safety valve support is consistent with section 254(e). See *infra* para. 187.

<sup>309</sup> See 47 C.F.R. § 36.631.

rules.<sup>310</sup> The retroactive application of the safety valve mechanism would provide additional support for rural carriers with acquired exchanges, with no assurance that such support would be used to increase investment in rural infrastructure or reduce customer rates. We also note that the retroactive application of the safety valve mechanism was not included in the Rural Task Force's principles for providing support to exchanges acquired by rural carriers or in the Rural Task Force's example of a safety valve mechanism. We therefore will not apply the safety valve mechanism retroactively. We will, however, permit carriers currently operating exchanges subject to section 54.305 of our rules to receive safety valve support on a going-forward basis for new investments in the acquired exchanges. Carriers currently operating exchanges subject to section 54.305 of our rules may qualify for safety valve support for acquired exchanges in accordance with the procedures described above.<sup>311</sup> For example, a carrier that will operate acquired exchanges subject to section 54.305 for a full year by June 30, 2001, would establish its index year expense adjustment by filing a quarterly update on December 30, 2001, in accordance with section 36.612 of our rules with cost data for the first six months of 2001 and the last six months of 2000. This conclusion is consistent with our decision to provide safety valve support to other rural carriers acquiring exchanges from unaffiliated carriers.

### **3. Support in Study Areas with Competitive Eligible Telecommunications Carriers**

#### **a. Background**

120. The Rural Task Force proposed that high-cost loop support be frozen on a per-line basis in rural carrier study areas where a competitive eligible telecommunications carrier initiates service.<sup>312</sup> As discussed below, the purpose of this proposal is to prevent excessive fund growth following competitive entry.<sup>313</sup> Under the Rural Task Force's recommended approach, frozen per-line support would be calculated based on the incumbent rural carrier's cost and line count data for the 12-month period prior to competitive entry. The incumbent and the competitive carrier would receive the same frozen support amount for each line served within the study area, subject to the disaggregation plan established for the study area, if any. Frozen per-line support would be adjusted annually by the rural growth factor, rather than for changes in costs. It would be subject to the indexed cap on high-cost loop support. In addition, incumbent rural carriers could request additional support to recover the costs of catastrophic events affecting their ability to provide supported services. Any adjustments to the frozen per-line support amount would apply equally to competitive carriers.

121. The Joint Board stated that, although it agreed with this proposal, "it is unclear how the high-cost loop fund cap would account for frozen carrier support."<sup>314</sup> The Joint Board also stated that "[t]he Commission should seek further input on the impact of 'catastrophic' support provided by other sources such as insurance, Rural Utilities Service loans, and federal or state emergency management relief."<sup>315</sup>

122. The Rural Task Force also raised concerns about frequency of reporting and the interval

---

<sup>310</sup> See, e.g., CenturyTel Comments at 6; Iowa Telecom Reply Comments at 4; NTCA Comments at 6; *but see* WorldCom Reply Comments at 12.

<sup>311</sup> See *supra* discussion at paras. 99-105.

<sup>312</sup> Rural Task Force Recommendation at 25-26. This proposal does not apply to LTS, LSS, or other forms of federal universal service support. *Id.*

<sup>313</sup> See *infra* para. 125.

<sup>314</sup> *Recommended Decision* at para. 17.

<sup>315</sup> *Id.*

between the provision of service and receipt of support in competitive study areas.<sup>316</sup> The Rural Task Force recommended that this interval “should be as short as technically and administratively feasible to ensure provision of universal service.”<sup>317</sup> To ensure that carrier data is “sufficiently sensitive to mid-period competitive activity[,]” it also proposed that support be distributed based on line count data for “the average of the quarter (*i.e.*, beginning of quarter plus end of quarter divided by two).”<sup>318</sup>

## b. Discussion

123. *Proposal to Freeze High-Cost Loop Support.* Based on consideration of the record in this proceeding, we decline at this time to adopt the Rural Task Force’s proposal to freeze high-cost loop support upon competitive entry in rural carrier study areas. As discussed below, the purpose of this proposal is to prevent excessive growth in the universal service fund as a result of an incumbent carrier’s loss of lines to a competitive eligible telecommunications carrier. The likelihood of this harm occurring in the immediate future is speculative, however, and in some instances the proposal may increase support levels. Moreover, the proposal has significant drawbacks, including administrative complexity and disincentives to infrastructure investment by rural carriers. We conclude, therefore, that adoption of the Rural Task Force’s proposal is not warranted at this time.

124. We recognize, however, that, as competition develops in high-cost areas and rural incumbent carriers lose lines to competitors, excessive fund growth may occur. We therefore seek comment in the attached Further Notice on possible alternative measures to address this potential issue.<sup>319</sup> During this proceeding, we intend to closely monitor the impact on the fund of competitive entry in rural carrier study areas to ensure that the fund remains specific, predictable, and sufficient consistent with section 254.<sup>320</sup>

125. In its comments, the Rural Task Force explains that the purpose of this proposal is to prevent excessive fund growth following competitive entry.<sup>321</sup> Due to the nature of telecommunications as an industry with high fixed costs, an incumbent carrier’s loss of subscriber lines to a competitive eligible telecommunications carrier is unlikely to be offset by a corresponding reduction in its total embedded cost of service.<sup>322</sup> If the incumbent’s lines decreased while its fixed costs remained roughly the same, its per-

---

<sup>316</sup> Rural Task Force Recommendation at 38; *see Competition and Universal Service: Rural Task Force White Paper 5* (Sept. 2000) (visited May 2, 2001) <<http://www.wutc.wa.gov/rtf>> at 21-22 (*White Paper 5*).

<sup>317</sup> Rural Task Force Recommendation at 38.

<sup>318</sup> *Id.* (“continuing support for the [incumbent] for a whole period when it is not serving the customer for the whole period, coupled with the failure to compensate the [competitor] for the portion of the period that it is providing service may constitute a barrier to entry for the [competitor]”). Under the current rules, carriers report lines served as of the end of the relevant reporting period. *See* 47 C.F.R. §§ 36.612, 54.307.

<sup>319</sup> *See infra* paras. 209-211.

<sup>320</sup> To facilitate such monitoring and prevent overpayment of support, as well as to address Rural Task Force concerns about frequency of reporting, we also adopt a requirement that eligible telecommunications carriers in competitive study areas file updated line counts on a regular quarterly basis. *See infra* paras. 132-133.

<sup>321</sup> *See* Rural Task Force Comments at 7-8; *see also* AT&T Comments at 14-15; NTCA Comments at 11, 13-14; John Staurulaukis, Inc. Comments at 9-10; Telecom Consulting Associates Comments at 6. The Rural Task Force Recommendation did not explain the purpose of its proposal to freeze high-cost loop support in the Recommendation. The Rural Task Force addressed the purpose in its Comments, however, and discussed related issues in its *White Paper 5*, which was incorporated by reference into the Recommendation. *See White Paper 5* at 19, 21, n.35.

<sup>322</sup> *See id.* We express no opinion on the issue of stranded costs, regarding which the Rural Task Force did not reach agreement. *See* Rural Task Force Recommendation at 39. As stated below, few competitive carriers currently (continued....)

line costs would increase. Consequently, the incumbent would be entitled to higher support per line.<sup>323</sup> Because the higher per-line support amount would be available to both the incumbent and the competitor for each line served under our portability rules, the size of the fund could grow significantly as competition increases, particularly if there is a net increase in the total number of lines served in the study area.<sup>324</sup> The indexed cap on high-cost loop support would not check this growth fully, because support received by competitive carriers currently is not included within the cap. Thus, by recommending that support be frozen on a per-line basis after competitive entry, and subsequently adjusted by a predetermined growth factor, the Rural Task Force sought to prevent excessive fund growth.

126. We are not convinced, however, that it is necessary to adopt the Rural Task Force's proposal at this time. The proposal may be of limited benefit in serving its intended purpose, and under some circumstances may contribute to fund growth rather than limiting it. First, the possibility of excessive fund growth is speculative. The harm the Rural Task Force sought to avoid arises only if a competitive eligible telecommunications carrier captures subscriber lines from an incumbent, not if it adds new lines. In addition, the competitive carrier presumably must capture a meaningful percentage of lines from the incumbent within the study area,<sup>325</sup> but it is unclear what this threshold is, or how often it is likely to be reached during the five-year period in which the Rural Task Force plan is in effect.<sup>326</sup> Second, the indexed cap on the high-cost loop fund will operate as a check on excessive fund growth to a certain extent. The support received by incumbent rural carriers is subject to the cap, and a competitive carrier will receive no more support on a per-line basis than the incumbent receives.<sup>327</sup> Moreover, in years the cap is not triggered, frozen per-line support, as proposed by the Rural Task Force, actually might exceed the support that carriers would receive based on the incumbent's embedded costs. Embedded costs per line generally decrease with line growth, but frozen per-line support would increase annually by the rural growth factor. Thus, if the incumbent's lines increase and the cap is not triggered, it may recover more frozen support

(Continued from previous page) \_\_\_\_\_

receive high-cost loop support for service to rural carrier study areas, and there is no evidence in the record before us projecting specific levels of competitive entry in the future. *See infra* n.326.

<sup>323</sup> *See* 47 C.F.R. §§ 36.601, *et. seq.*

<sup>324</sup> *See White Paper 5* at 21, n.35 ("For example, . . . if an ILEC served 1,000 lines and received \$1,000 in monthly universal service support, this would equate to \$1 of support per line. This amount would be available to any CETC that captured a line from the ILEC. If the ILEC lost 500 lines to competitors, but the ILEC's support based on embedded costs still amounted to \$1,000 per month, the per line support available to the ILEC and CETC would double to \$2 per line to the ILEC and CETC."). Under the Commission's portability rules, a competitive carrier receives the same support for each line served that the incumbent carrier would receive, based on the incumbent's embedded costs. 47 C.F.R. § 54.307. Two commenters argue that these rules should be modified to provide support to competitive carriers based on their own costs. *See* NTCA Comments at 12, Fred Williamson & Assoc. Comments at 6-7. The Commission previously rejected this argument, and we decline to reconsider it at this time. *See First Report and Order*, 12 FCC Rcd at 8944-45 paras. 311-13.

<sup>325</sup> *See* John Staurulaukis, Inc. Comments at 9-10 (proposing a threshold requirement that a competitive carrier serve five or ten percent of the total lines within a study area); Telecom Consulting Associates Comments at 7-8 (proposing ten percent threshold); Townes Telecommunications Comments at 3 (proposing threshold of ten percent or more).

<sup>326</sup> *See* Rural Task Force Recommendation at 38 ("the competitive inroad of the [competitive eligible telecommunications carrier] usually begins with a slow ramp-up as customers are signed on for services"). We note that a total of six competitive carriers nationwide currently receive high-cost loop support for service to both rural carrier and non-rural carrier study areas. *See* Federal Universal Service Support Mechanisms Fund Size Projections and Contribution Base For the Second Quarter 2001, Appendix HC 1 (Universal Service Administrative Company, Feb. 6, 2001). There is no evidence in the record before us projecting specific levels of competitive entry in the future.

<sup>327</sup> *See* 47 C.F.R. § 54.307; *see also* Rural Task Force Comments at 7-8 (Rural Task Force plan guards against excessive fund growth as a result of increasing competition in part by recommending retention of the cap).

than it would based on its embedded costs.<sup>328</sup> The potential for excess support is increased because the rural growth factor includes annual rural line growth, so that its application to individual lines receiving frozen support would result in double counting of line growth.<sup>329</sup>

127. We are further concerned that the Rural Task Force's proposal would require us to implement complex and administratively burdensome regulations. For example, we would have to impose a new reporting requirement on rural carriers to implement the proposal that frozen per-line support be calculated based on cost and line count data for the 12 months prior to the quarter in which the competitive carrier initiates service.<sup>330</sup> Despite the fact that their support would be frozen, rural carriers would have to continue filing annual cost data, because the proposal that frozen support be subject to the cap would require comparison of a carrier's total frozen per-line support to its total capped support based on embedded costs.<sup>331</sup>

128. Furthermore, new administrative requirements and procedures would be necessary to implement the Rural Task Force's proposal to allow incumbent rural carriers to request increased support to recover the costs of catastrophic events affecting their ability to provide supported services.<sup>332</sup> To verify the need and eligibility for increased support under this proposal, and to address the concerns of the Joint Board and others that such support could be used as a substitute for insurance or other sources of funding,<sup>333</sup> we would have to impose additional reporting requirements on rural carriers, and/or adopt potentially cumbersome procedures for state certification.<sup>334</sup> Moreover, to avoid undermining the original purpose of fixing support, some procedure would be necessary to ensure that a carrier's need for increased per-line support is due to a catastrophic event rather than the loss of lines to a competitor. These examples illustrate the regulatory burdens and difficulties entailed in the Rural Task Force's recommended approach.

129. More importantly, freezing support in competitive study areas may have the unintended consequence of discouraging investment in rural infrastructure, contrary to the fundamental goals of the

---

<sup>328</sup> Under the Rural Task Force proposal, if the cap is triggered, an incumbent rural carrier would receive no more total frozen per-line support than it would have received under the cap, and its competitor's per-line support would be limited accordingly. *See* Rural Task Force Recommendation at 26; Rural Task Force Comments at 8.

<sup>329</sup> *See* Texas Commission Comments at 6. The Rural Task Force addresses this issue in its comments, but rather than refuting that such double counting would occur, it simply clarifies that the cap would constrain the overall growth of frozen per-line support. Rural Task Force Comments at 7-8.

<sup>330</sup> Currently, rural carriers are only required to file such data annually by July 31<sup>st</sup> for the prior calendar year, and may file quarterly updates on September 30<sup>th</sup>, December 30<sup>th</sup>, and March 30<sup>th</sup>. 47 C.F.R. §§ 36.611, 36.612.

<sup>331</sup> *See* Rural Task Force Recommendation at 26; *see also supra* para. 59.

<sup>332</sup> Under the Rural Task Force proposal, additional support would be available to recover the costs of hurricanes, floods, and other events that are declared to be natural disasters by Federal or state regulatory authorities, and that directly affect the provision of supported services within a study area. Rural Task Force Recommendation at 26. As a number of commenters point out, this provision would merely place rural carriers in the same position as they would be if their support were not frozen, for such costs are now recoverable from universal service support to the extent that they are not covered by insurance. *See* Innovative Telephone Comments at 20-21; NRTA, OPASTCO, & USTA Comments at 5; NTCA Comments at 14-15; Rural Task Force Comments at 9; Virgin Islands Commission Comments at 6.

<sup>333</sup> *See Recommended Decision* at para. 17; California Commission Comments at 14; CUSC Comments at 7; Florida Commission Comments at 6-7; Sprint Comments at 2-3.

<sup>334</sup> *See* Texas Commission Comments at 7 ("state regulators should participate in the decision on whether the carrier should receive additional funding as a result of catastrophic events").

Rural Task Force plan.<sup>335</sup> A number of commenters argue that carriers in competitive study areas will have reduced incentives to invest in infrastructure, because they will be unable to obtain additional support for such investments once their high-cost loop support is frozen.<sup>336</sup> One commenter states that fixing support could interfere with the normal, “cyclical” investment patterns of small rural carriers.<sup>337</sup> In addition, some commenters argue that the Rural Task Force’s proposal is over-inclusive and would distort incentives for competitive entry, because support would be frozen regardless of how many subscriber lines a competitive carrier serves within a study area, whether it captures or adds lines, or whether it serves only a limited geographic portion of the study area.<sup>338</sup> Furthermore, we are concerned that adoption of this proposal could hinder competitive entry in rural carrier study areas, again contrary to a fundamental goal of the Rural Task Force plan.<sup>339</sup> The Competitive Universal Service Coalition, although it does not oppose the proposal, raises concerns that it could increase the difficulty for new entrants by creating an additional incentive for incumbents to oppose designation of a new eligible telecommunications carrier.<sup>340</sup> Indeed, one carrier recently filed comments with the Commission opposing a petition for such status, in part, on the ground that the resulting freeze of support (assuming the Rural Task Force proposal were adopted) would “severely constrain” its ability to upgrade plant and provide quality service in the area.<sup>341</sup>

130. In sum, we conclude that, at this time, the costs of adopting the Rural Task Force’s proposal to freeze high-cost loop support in competitive study areas would significantly outweigh the potential benefits. Based on our examination of the present record, we believe that the proposed solutions to the problems identified above (*e.g.*, an expedited waiver process, a market-share threshold requirement, or freezing support only in geographic areas served by the competitive carrier) would compound the administrative complexity of the Rural Task Force’s recommended approach without resolving the problems. For example, a simple market-share threshold requirement would fail to target study areas where the harm sought to be avoided is most likely to occur, because it could not distinguish captured from new subscriber lines.<sup>342</sup> Similarly, freezing support only in limited portions of a study area would

---

<sup>335</sup> See *Recommended Decision* at para. 11 (Rural Task Force sought to provide rural carriers with “stability . . . for planning their investments over the next several years” and “increased incentives to invest in new infrastructure and technologies.”).

<sup>336</sup> See Evans Tel. Co., et al.. Comments at 7; Interstate Telecom Group Comments at 8; NTCA Comments at 11, 13-14; John Staurulaukis, Inc. Comments at 9-10; Telecom Consulting Associates Comments at 6-7; Townes Telecommunications Comments at 2-3; see also Alliance of Incumbent Rural Telephone Companies Reply Comments in CC Docket No. 00-256 at 9.

<sup>337</sup> Townes Telecommunications Comments at 2-3 (“Unlike larger carriers that are continuously upgrading their exchanges on a rotating basis, many smaller carriers do not have a continuous investment program. Rather, small carriers are more likely to have a ‘cyclical’ investment pattern and upgrade the major portion of their network on a periodic basis, such as once every fifteen (15) years.”).

<sup>338</sup> See Interstate Telecom Group Comments at 8-9; John Staurulaukis, Inc. Comments at 9-10; Telecom Consulting Associates Comments at 9; Townes Telecommunications Comments at 4; Western Alliance Comments at 9-10.

<sup>339</sup> See *Recommended Decision* at para. 11 (Rural Task Force Recommendation “seeks to encourage competitors to enter high-cost areas.”).

<sup>340</sup> See CUSC Comments App. A at 16-17 (“If the Commission adopts this recommendation, . . . it should also make perfectly clear that [the freezing of high-cost loop support] is not a basis for denying a competitive entrant’s petition for ETC designation.”); see 47 U.S.C. § 214(e)(2), (e)(5).

<sup>341</sup> Smith Bagley, Inc. Petitions for Agreement to Redefine the Service Areas of Navajo Communications Company, Citizens Communications Company of the White Mountains, and Century Tel of the Southwest, Inc. on Tribal Lands within the State of Arizona, CC Docket No. 96-45, Comments of Table Top Tel. Co., Inc., at 4-5 (filed Mar. 16, 2001).

<sup>342</sup> See Rural Task Force *White Paper 5* at 17 (“Dealing with ‘captured’ and ‘new’ lines may create administrative problems and the need to track customers from one [carrier] to another”).

complicate the administration of a frozen support provision without reducing the likelihood of such harm.<sup>343</sup> We conclude, therefore, that adoption of this proposal is not warranted.

131. We intend, however, to closely monitor the impact of competitive entry in rural carrier study areas to ensure that the fund remains specific, predictable, and sufficient consistent with section 254. We note that the quarterly reporting requirements we adopt below for rural incumbent carriers serving study areas in which a competitive eligible telecommunications carrier has been designated will enable us to closely monitor any excessive fund growth that may result from incumbent line loss to a competitive eligible telecommunications carrier.<sup>344</sup>

132. *Frequency of Reporting and Lag in Support.* As stated above, the Rural Task Force also raised concerns about frequency of reporting and the interval between the provision of service and receipt of support in competitive study areas.<sup>345</sup> With regard to frequency of reporting, the Rural Task Force observed that the number of lines served by carriers in competitive study areas “may change in a dynamic manner.”<sup>346</sup> Rural carriers and their competitors currently are required to file line count data annually, and may file quarterly updates on a voluntary basis.<sup>347</sup> Quarterly updates are required in non-rural carrier study areas.<sup>348</sup> Under the current rules, if an incumbent rural carrier does not update its line count data but its competitor does, the competitor’s more recent data may include lines captured from the incumbent since the incumbent’s last filing. Thus the incumbent may continue to receive support for the year based on an overstated number of lines.

133. To prevent an overpayment of support, and to address the Rural Task Force’s concerns, we will require the filing of line count data on a regular quarterly basis upon competitive entry in rural carrier study areas. By synchronizing such data, this requirement will ensure that only one carrier receives support for each line served.<sup>349</sup> In addition, it should allow closer monitoring of the impact of competitive entry, because it will reveal any loss or gain of subscriber lines by competing carriers on a quarter-to-quarter basis. We believe that this requirement will not significantly increase reporting burdens for the affected carriers because, although they will be required to report data more frequently, the data will be limited to changes in the number of lines that they served during a quarter. We emphasize that this requirement will not apply in rural carrier study areas in which an eligible telecommunications carrier has not been designated.<sup>350</sup>

134. We agree with the Rural Task Force’s general recommendation that the interval between

---

<sup>343</sup> If support were frozen in a limited portion of a study area and the incumbent carrier lost a significant number of lines there, per-line support levels would escalate even more quickly in the remainder of the study area, because embedded costs are calculated on a study-area basis. *See generally* 47 C.F.R. § Part 36.

<sup>344</sup> *See infra* paras. 132-133.

<sup>345</sup> Rural Task Force Recommendation at 38.

<sup>346</sup> *Id.*

<sup>347</sup> 47 C.F.R. §§ 36.612, 54.307.

<sup>348</sup> *Id.*

<sup>349</sup> *See Ninth Report and Order*, 14 FCC Rcd at 20480-81 para. 92 (mandating quarterly reporting for carriers serving non-rural study areas “[t]o ensure that [universal service support is] based on data from the same reporting periods, and to ensure equitable, non-discriminatory, and competitively neutral treatment of incumbent LECs and competitive eligible telecommunications carriers”).

<sup>350</sup> For purposes of this requirement, “competitive” will mean that a competitive eligible telecommunications carrier has initiated service within the study area and has reported line count data to the Administrator pursuant to section 54.307(c) of the Commission’s rules. 47 C.F.R. § 54.307(c).

the provision of service and receipt of universal service support should be as short as possible.<sup>351</sup> The Commission previously concluded that portability of support facilitates the entry of competition in areas served by rural carriers.<sup>352</sup> Because support represents an important source of funds for the operation of an exchange with high loop costs, the interval between the reporting of costs and receipt of support based on those costs may discourage competitive entry. Nevertheless, some interval is necessary for administrative reasons.<sup>353</sup> To ensure that the interval between the submission of data and receipt of support is as short as possible in rural carrier study areas, we clarify that competitive eligible telecommunications carriers may submit initial line count data and receive support on a regular quarterly basis under section 54.307(c) of the Commission's rules.<sup>354</sup>

135. The Rural Task Force also recommended that support in competitive study areas be distributed based on line count data for "the average of the quarter (*i.e.*, beginning of quarter plus end of quarter divided by two)."<sup>355</sup> This recommendation appears to hold promise as a means of promoting the distribution of support on an equitable, non-discriminatory, and competitively neutral basis. As proposed, however, the Rural Task Force's recommended approach would impose additional reporting requirements, as carriers currently are required to report only line count data as of the end of the relevant reporting period.<sup>356</sup> The present record lacks evidence on the administrative burden that such requirements would impose, if any, or on whether alternative measures might avoid the need for such requirements. Moreover, we believe that any such measure should be applicable to all carriers, including those serving non-rural study areas. Therefore, we intend to address the Rural Task Force's proposal at a later date.

## **D. Disaggregation and Targeting of Support**

### **1. Background**

136. Under the existing embedded cost mechanism, federal universal service high-cost support for rural carriers is averaged across all lines served by a carrier within its study area. Thus, support on a per-line basis is the same throughout a study area even though the costs of serving customers in that study area likely vary. As a result, support in low-cost areas of the study area may exceed the cost of serving those areas while support in high-cost areas may be insufficient to offset the higher cost of serving those areas. Recognizing that support is portable, the Rural Task Force contends that this may create uneconomic incentives for competitive entry.<sup>357</sup> The Rural Task Force stated in its recommendation that

---

<sup>351</sup> Rural Task Force Recommendation at 38.

<sup>352</sup> *First Report and Order*, 12 FCC Rcd at 8944.

<sup>353</sup> For example, lag between the reporting of data and the payment of support is necessary to allow projection of funding requirements and collection of contributions based on such data. *See Ninth Report and Order*, 14 FCC Rcd at 20485 para. 100. In addition, an interval between the initiation of service and receipt of support by a competitive carrier is necessary to synchronize the filing schedules of incumbents and competitors, thereby ensuring equal, non-discriminatory, and competitively neutral treatment of all carriers. 47 C.F.R. §§ 36.612, 54.307; *see Ninth Report and Order*, 14 FCC Rcd at 20478 para. 87, 20480-81 para. 92.

<sup>354</sup> 47 C.F.R. § 54.307; *see Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Twentieth Order on Reconsideration, 15 FCC Rcd 12070, 12078 para. 18 (2000); CUSC Comments App. A at 12 (requesting clarification that competitive carriers "have the option to make both their initial line count report and subsequent reports at least quarterly"). We will amend section 54.307(c) to remove reference to an annual July 31<sup>st</sup> deadline.

<sup>355</sup> Rural Task Force Recommendation at 38. Under the current rules, carriers report lines served as of the end of the relevant reporting period. *See* 47 C.F.R. §§ 36.612, 54.307.

<sup>356</sup> *See id.*

<sup>357</sup> Under the Commission's portability rules a competitive eligible telecommunications carrier receives the same per-line level of high-cost support for lines that it captures from an incumbent carrier, as well as for any new lines it serves in high-cost areas. *See* 47 C.F.R. § 54.307.

the current distribution method must be modified to be consistent with the Act and the principle of competitive neutrality.<sup>358</sup>

137. As part of its proposal to reform the federal universal service support mechanism for rural carriers, the Rural Task Force proposed that rural carriers be permitted to depart from study area averaging and instead disaggregate and target per-line high-cost universal service support, including high-cost loop support, LTS, and LSS, into geographic areas below the study area level.<sup>359</sup> By doing so, per-line support would not be the same throughout a study area but would vary to reflect the cost of providing service in a particular geographic area within the study area. The Rural Task Force concluded that the disaggregation and targeting of support is necessary to eliminate the economic distortions that may result from the delivery of support on a uniform per-line basis under the current mechanism thereby reducing the possibility for arbitrage of universal service support resulting in shortfalls or windfalls to either incumbent carriers or competitive eligible telecommunications carriers. At the same time, however, the Rural Task Force stated that rural carriers need flexibility in the manner in which support is disaggregated and targeted in light of the widely varying characteristics and operating environments of rural carriers. Recognizing that a disaggregation and targeting system must meet the unique regulatory and competitive environments in each state, the Rural Task Force recommended a disaggregation system consisting of three paths. Carriers would be required to elect one of these paths within 270 days of the effective date of the order implementing rural high-cost reform.<sup>360</sup>

138. Path One would allow a carrier to certify to the state commission, or other appropriate regulatory authority, that it does not want to disaggregate support. The carrier's election of this path would become effective upon filing of the certification and remain in place for at least four years unless (1) the state commission or other appropriate regulatory authority requires, on its own motion or upon petition by an interested party, the disaggregation of support, or grants eligible telecommunications carrier status below the study area level; (2) there is a change in state or federal laws or regulations; or (3) there is a change in ownership. If any of these events occur, the carrier would be permitted to target support under one of the other two paths.

139. Path Two would be available to carriers that want state commission review and approval of a disaggregation plan.<sup>361</sup> A carrier that chooses this path, which places no constraints on the disaggregation plan, would file a disaggregation plan with the state commission, or other appropriate regulatory authority. The Rural Task Force contemplates that the regulatory authority would hold workshops, hearings, or other appropriate administrative proceedings in which interested parties may participate, and that the regulatory authority would issue an order, which would set out the targeting method, a description of the zones, and a per-line support amount for each category of support in each zone. The Rural Task Force proposed that the disaggregation plan, once approved, would be effective until the regulatory authority approves a new plan, but would remain subject to change or challenge at any time.

140. Path Three would permit carriers to self-certify a method of disaggregation with the state commission or other appropriate regulatory authority. The Rural Task Force proposed that carriers certify that the disaggregation plan complies with certain requirements. First, carriers must certify that support would be disaggregated to the wire center level or into no more than two cost zones per wire center. A

---

<sup>358</sup> Rural Task Force Recommendation at 33.

<sup>359</sup> *Id.* at 33-36. See also *Disaggregation and Targeting of Universal Service Support: Rural Task Force White Paper 6* (Sept. 2000) (visited May 2, 2001) <<http://www.wutc.wa.gov/rtf>> at 4-6 (*White Paper 6*).

<sup>360</sup> Rural Task Force Recommendation at 34-36.

<sup>361</sup> *Id.* at 35.

different level of disaggregation would be permitted only if a state commission, previously determined that a different level of disaggregation is appropriate.<sup>362</sup> Second, if the appropriate regulatory authority has previously adopted a method of disaggregation, the carrier must certify that its plan uses the rationale previously adopted. Third, the carrier must certify that the plan uses a rationale for disaggregating support that is reasonably related to the cost of providing service for each cost zone within each disaggregated category of support (high-cost loop support, LSS and LTS). Fourth, if the plan uses a benchmark to determine support amounts, the benchmark must be generally consistent with how the total study area level of support is derived to compare the disaggregated costs for determining support for each cost zone. The certification filing must describe the rationale used, including the methods and data, and a discussion of how the plan complies with the self-certification guidelines.<sup>363</sup> If the plan uses a benchmark, the filing must explain what the benchmark is and how it was determined. The plan must show the per-line amount of support for each category of support in each zone.

141. The Rural Task Force proposed that a carrier's election of Path Three would become effective upon filing of the certification and remain in place for at least four years unless (1) the state commission or other appropriate regulatory authority requires, on its own motion or upon petition by an interested party, the disaggregation of support, or grants eligible telecommunications carrier status below the study area level; (2) there is a change in state or federal laws or regulations; or (3) there is a change in ownership.<sup>364</sup> At any time while in effect, the plan would be subject to complaint by interested parties before the appropriate regulatory authority on the grounds that the plan does not comply with the certification requirements proposed by the Rural Task Force. To the extent a plan is challenged, the Rural Task Force proposed that the relevant regulatory administrative procedures (including burden of proof allocation and availability of discovery) would apply to such complaints.

142. With regard to all three paths, the Rural Task Force also recommended that certain general requirements apply to each disaggregation plan.<sup>365</sup> First, the Rural Task Force recommended that relative per-line support relationships between disaggregation zones for each disaggregated category of support remain fixed over time (except as changes are allowed by the Path descriptions) and that such relationships be made publicly available. Second, the Rural Task Force recommended that, until a competitive eligible telecommunications carrier is certified in a study area, monthly payments to an incumbent carrier be made using current procedures based on total annual amounts for a study area divided by twelve. Third, when a competitive eligible telecommunications carrier is certified for a study area, per-line amounts to determine the competitive eligible telecommunications carrier's support should then be based on the incumbent carrier's then-current total support levels, lines, and disaggregated support relationships. Fourth, the Rural Task Force recommended that support per-line for each category of support for each disaggregation zone be determined such that the relative support relationships between zones would be maintained and that the product of all of the incumbent's lines for each cost zone multiplied by the per-line support for those zones would sum to the incumbent's total level of support. Fifth, the Rural Task Force recommended that per-line support amounts for each zone should be recalculated whenever the incumbent's total annual support amount changed using the changed support amounts and lines at that point in time. The Rural Task Force also recommended that the incumbent carrier's study area support available in total for a study area under the disaggregation method equal the total support available without disaggregation.

143. Finally, the Rural Task Force recognized that state commissions have the authority to

---

<sup>362</sup> *Id.* at 36.

<sup>363</sup> The Rural Task Force, however, does not propose that a carrier be required to file a complete cost study. *Id.*

<sup>364</sup> *Id.* at 35.

<sup>365</sup> *Id.* at 34.

determine whether more than one eligible telecommunications carrier should be designated in an area served by a rural carrier.<sup>366</sup> The Rural Task Force also recognized that, under section 214(e)(5) of the Act and the Commission's rules, carriers must seek approval from the Commission and the States, after taking into account recommendations of the Joint-Board, to change an eligible telecommunication carriers "service area" to a geographic area other than a rural carrier's study area.<sup>367</sup> The Rural Task Force recommended that the level of disaggregation of support be considered in determining whether to certify new eligible telecommunications carriers for a service area other than a rural carrier's entire study area.<sup>368</sup>

## 2. Discussion

144. We find that the Rural Task Force's disaggregation and targeting proposal achieves a reasonable balance between rural carriers' needs for flexibility and the Commission's goal of encouraging competitive entry. As discussed below, we agree with the Rural Task Force and the commenters that, as a general matter, support should be disaggregated and targeted below the study area level. At the same time, we agree with the Rural Task Force that, given the significant differences among rural carriers and the varying competitive environments among the states, there should be flexibility in the manner in which support is disaggregated and targeted for rural carriers. Accordingly, subject to certain modifications discussed below, we adopt generally the three paths for the disaggregation and targeting of high-cost universal service support proposed by the Rural Task Force. We also adopt the general requirements that the Rural Task Force proposed for all disaggregation plans.

145. We agree with the Rural Task Force and commenters that the provision of uniform support throughout the study area of a rural carrier may create uneconomic incentives for competitive entry and could result in support not being used for the purpose for which it was intended, in contravention of section 254(e).<sup>369</sup> Because support is averaged across all lines served by a carrier within its study area under the existing mechanism, the per-line support available throughout the study area is the same even though the costs throughout the study area may vary widely. As a result, artificial barriers to competitive entry in the highest-cost areas and artificial entry incentives in relatively low-cost portions of a rural carrier's study area are created. For example, support would be available to a competitor that serves only the low-cost urban lines, regardless of whether the support exceeds the cost of any of the lines. We conclude therefore that, as a general matter, support should be disaggregated and targeted below the study area level so that support will be distributed in a manner that ensures that the per-line level of support is more closely associated with the cost of providing service.<sup>370</sup>

146. While we recognize the benefits of disaggregating and targeting support, we also agree with the Rural Task Force's recommendation that there should be flexibility in the manner in which support is disaggregated and targeted for rural carriers. The Rural Task Force's multi-path system is premised on the proposition that, because of the diverse characteristics among rural carriers, there is not an adequate "one size fits all" approach that is workable for disaggregating support for rural carriers.<sup>371</sup>

---

<sup>366</sup> *Id.*

<sup>367</sup> *Id.* at 36.

<sup>368</sup> *Id.*

<sup>369</sup> *Id.* at 33-34, *White Paper* 6 at 4-5. See, e.g., CUSC Comments App. A at 5; Ad Hoc Telecommunications User Committee Comments at 23; SDITC Comments at 8-9. See also *Ninth Report and Order*, 14 FCC Rcd at 20471 para. 71.

<sup>370</sup> This conclusion is consistent with our determination in the *Ninth Report and Order* that support for non-rural carriers should be targeted to avoid the uneconomic incentives created by the delivery of federal support to non-rural carriers on a uniform per-line basis. *Ninth Report and Order*, 14 FCC Rcd at 20471 para. 71, 20472-73 para. 75.

<sup>371</sup> Rural Task Force Recommendation at 33-34, *White Paper* 6 at 6-11.

As discussed above, there are over 1300 study areas served by companies defined as rural carriers.<sup>372</sup> The population of rural carriers reflects diverse operating characteristics and operating environments. We find that providing rural carriers flexibility in the methods of disaggregation and targeting is a reasonable approach to address the significant diversity among such carriers. By providing carriers such flexibility, a carrier may better match the disaggregation and targeting methodology to its costs and geographic characteristics and the competitive and regulatory environment in the state in which it operates.

147. Similarly, we recognize that in some specific instances, as described below, the factors that militate in favor of disaggregation may not be present. We find that requiring the disaggregation and targeting of support in these instances would serve no rational economic purpose. We conclude that the multi-path system proposed by the Rural Task Force addresses the distinct needs of rural carriers and, therefore, we adopt the three paths recommended by the Rural Task Force for the disaggregation and targeting of support by rural carriers, subject to certain modifications discussed in greater detail below. We direct carriers to choose within 270 days of the effective date of the rules adopted in this Order one of these three paths.<sup>373</sup> Carriers failing to do so will not be permitted to disaggregate and target support unless ordered to do so by a state commission or other appropriate regulatory authority either on its own motion or in response to a request of an interested party.

148. First, we adopt with modifications Path One, which provides that a carrier may choose not to disaggregate. Path One is intended to address those instances where a carrier determines that, given the demographics, cost characteristics, and location of its service territory, and the lack of a realistic prospect of competition, disaggregation is not economically rational.<sup>374</sup> For example, a carrier may serve only a few lines or a very small study area with little geographic variability. We find that permitting such a carrier not to disaggregate support is appropriate.<sup>375</sup> We recognize commenters' concerns that a carrier may choose not to disaggregate and target support for anti-competitive reasons.<sup>376</sup> We find, however, that because a state nonetheless may require disaggregation, either on its own motion or that of an interested party, sufficient safeguards are in place to ensure that if disaggregation and targeting of support is warranted, the carrier will be required to do so. Indeed, if a state receives a request to require a carrier to disaggregate and target support under any of the paths adopted herein, we expect that it will be guided in making a determination on the request by our view that support should generally be disaggregated and targeted in a manner that the per-line level of support is more closely aligned with the cost of providing service.

149. We find, however, that it is necessary to modify Path One in order to minimize the risk of gaming and to ensure a competitive entrant certainty with regard to the level of available per-line support. As proposed by the Rural Task Force, a carrier would have the option to change to a different path if a competitor is granted eligible telecommunications carrier status below the study area level, a change in state or federal regulations occurs, or a change in ownership occurs. We are concerned that permitting a

---

<sup>372</sup> See *supra* at para. 13.

<sup>373</sup> In adopting this mechanism we recognize, as did the Rural Task Force, that in limited instances certain carriers may not be subject to the jurisdiction of a state, *e.g.*, tribally-owned carriers. In such limited circumstances, the Commission would be the appropriate regulatory authority for the administration of the disaggregation and targeting of support by such carriers.

<sup>374</sup> See Rural Task Force *White Paper* 6 at 10-11.

<sup>375</sup> See Texas Commission Comments at 7 (recognizing that it may be reasonable to allow some small rural carriers to not disaggregate and target support under Path One because of their size and cost characteristics.) The Texas Commission also encouraged the Commission to consider whether "larger rural carriers" should be permitted to elect Path One but did not offer additional support for its proposition. *Id.*

<sup>376</sup> See, *e.g.*, CUSC Comments App. A at 7-8.

carrier to disaggregate after election of Path One under these circumstances presents the opportunity for gamesmanship and undermines the certainty necessary to encourage a competitive eligible telecommunications carrier to enter a market.<sup>377</sup> Accordingly, we find that once an incumbent elects not to disaggregate under Path One, it shall remain in effect until a state commission or appropriate regulatory authority requires, on its own motion, or upon petition by an interested party, including the affected incumbent, a change to a different disaggregation and targeting methodology. We conclude that, by permitting a carrier to change from this path only upon the approval of a state commission or appropriate regulatory authority, a competitive eligible telecommunications carrier is provided sufficient certainty with regard to the level of available per-line support. Moreover, we believe that because a carrier's ability to change to a different disaggregation methodology after it elects Path One is constrained, a carrier is less likely to elect Path One for anti-competitive reasons.

150. Second, we adopt Path Two, which provides that a carrier may disaggregate based on a plan that has been approved by the appropriate regulatory authority. Because there are no constraints on disaggregation and targeting proposals under Path Two, a carrier could disaggregate and target support to multiple levels below a wire center, a disaggregation and targeting method can be tailored with precision, subject to state approval, to the cost and geographic characteristics of the carrier and the competitive and regulatory environment in which it operates.<sup>378</sup> Thus, this path provides the utmost flexibility in the development of a disaggregation plan, but at the same time provides for regulatory approval to ensure that the methodology implemented is competitively neutral.

151. Third, we adopt the Path Three self-certification process that permits carriers to choose (1) a disaggregation plan of up to two cost zones per wire center, or (2) a disaggregation plan that complies with a prior regulatory determination. We find that permitting carriers to self-certify its disaggregation and targeting plan to the state reduces the administrative burdens on carriers and states, and facilitates the rapid implementation of disaggregation and targeting plans. We believe that the certification requirements proposed by the Rural Task Force will ensure that the disaggregation plans are cost-based and consistent with the principles of competitive neutrality. For example, a carrier must provide the state and USAC with a description of the rationale used to disaggregate support, including the methods, and data, and a discussion of how the plan complies with the self-certification guidelines.<sup>379</sup> In addition, if the plan uses a benchmark, it must be generally consistent with how the total study area level of support for each category of costs (high-cost loop support, LSS, and LTS) is derived, to enable a competitor to compare the disaggregated costs used to determine support for each zone.<sup>380</sup> Moreover, the plan must show a per-line amount of support for each element in each disaggregation zone. We find that, given these requirements, the self-certification process strikes a reasonable balance between providing flexibility and ensuring that support is disaggregated in a competitively neutral manner.

152. We disagree with those commenters that assert that permitting carriers to self-certify to a disaggregation plan creates too great an opportunity for the incumbent carrier to manipulate the

---

<sup>377</sup> For example, a carrier could choose not to disaggregate then subsequently elect to do so under Path Two or Path Three when a competitor is granted eligible telecommunications carrier status below the carrier's study area level for the purpose of having lower per-line support levels established for the competitor's service area.

<sup>378</sup> Under this path, a carrier could choose among any of the various methods of disaggregation, such as use of a proxy model, long-run incremental cost studies, or the use of density factors to disaggregate support.

<sup>379</sup> A complete cost study is not required. *See* Rural Task Force Recommendation at 36.

<sup>380</sup> We recognize that carriers could choose a benchmark based on affordability or averaged rates. *See Wyoming Public Service Commission Petition for Waiver of Targeting Requirements Found in Section 54.309 and 54.311 of the Commission's Rules*, CC Docket No. 96-45, DA 01-612 (rel. Mar. 9, 2001). We require carriers to provide detailed information explaining what the benchmark is and how it was determined.

disaggregation and targeting of support in an anti-competitive manner.<sup>381</sup> We note that the states will play a significant role in the disaggregation and targeting of support. Under the plan we adopt here, a self-certified plan is subject to complaint by interested parties before the appropriate regulatory authority on the grounds that it does not comply with the self-certification requirements, which we believe ensure that the disaggregation plan will not be anti-competitive. Moreover, the state or appropriate regulatory authority may require on its own motion at any time the disaggregation of support in a different manner. We believe that state oversight in the administration of the disaggregation scheme will safeguard against the anti-competitive manipulation of the disaggregation and targeting of support.

153. To further ensure that Path Three is employed in a pro-competitive manner, however, we find that additional regulatory oversight of any proposed changes to the disaggregation plan is necessary. As proposed by the Rural Task Force, a carrier has the option to change to a different path and alter its existing disaggregation plan if a competitor is granted eligible telecommunications carrier status below the study area level, a change in state or federal regulations occurs, or a change in ownership occurs. As discussed above with regard to Path One, we are concerned that permitting a carrier this latitude may invite gaming by incumbent carriers and undermines the certainty necessary to encourage a competitive eligible telecommunications carrier to enter a market. Accordingly, we find that, once an incumbent elects a disaggregation plan under Path Three, the plan shall remain in effect until a state commission or appropriate regulatory authority requires, on its own motion, or upon petition by an interested party, including the affected incumbent, a change to a different disaggregation and targeting methodology. We conclude that by permitting a carrier to change from this path only upon the approval of a state commission or appropriate regulatory authority, a competitive eligible telecommunications carrier is provided greater certainty as to the level of available per-line support. Moreover, we believe that because a carrier's ability to move to a different path is constrained, a carrier is less likely to elect this path for anti-competitive reasons.

154. As discussed above with regard to Paths One and Three, by requiring a rural carrier to retain its disaggregation plan unless the state commission approves any changes to the plan, the disaggregation rules adopted in this Order will provide both rural carriers and competitive eligible telecommunications carriers greater certainty as to the level of available per-line support in the study area or disaggregation zone. We are concerned that permitting incumbent carriers to modify the disaggregation plans they have elected during the five year period may, in certain instances, undermine the universal service goals of specific and predictable support and allow carriers to engage in anti-competitive behavior. We are confident that state commissions, when considering modification requests, will safeguard against anti-competitive manipulation of the disaggregation and targeting of support that could occur with such requests.

155. We are also mindful that in a few limited instances, a competitive carrier may have, prior to the effective date of the disaggregation rules adopted in this Order, entered the service area of a rural incumbent local exchange carrier and been designated as an eligible telecommunications carrier for purposes of receiving high-cost support.<sup>382</sup> In such instances, we believe that permitting the incumbent carrier to self-certify to a disaggregation plan may result in the anti-competitive targeting of support. Accordingly, for those study areas in which a competitive carrier has been designated as an eligible telecommunications carrier prior to the effective date of these rules, an incumbent carrier may elect a disaggregation plan under Path Three only to the extent that it is self-certifying a disaggregation and targeting plan that has already been approved by the state. In all other instances in which a competitive eligible telecommunications carrier has been designated prior to the effective date of these rules, the incumbent carrier must seek prior state approval of its disaggregation and targeting plan under Path Two.

---

<sup>381</sup> See, e.g., CUSC Comments App. A at 7-8; Ad Hoc Telecommunications User Committee Comments at 25.

<sup>382</sup> See, e.g., Ad Hoc Telecommunications User Committee Comments at 24-25.

We believe this approach will prevent the anti-competitive targeting of support.

156. We disagree with commenters that argue that carriers self-certifying under Path Three should be permitted to disaggregate to three or more zones below the wire center level.<sup>383</sup> We believe that permitting carriers to disaggregate and target support to more than two zones below the wire center level without prior regulatory approval would provide too great an opportunity to disaggregate support in an anti-competitive manner. If allowed to disaggregate and target support to more than two zones, a carrier would have greater opportunity to target excessive support to areas in which competition is not likely to occur and inadequate support to areas likely to be served by competitors. For example, if permitted to disaggregate and target to three zones, a carrier could develop a zone that matches a wireless competitive eligible telecommunications carrier's footprint within a state and deliver little or no support to that zone.

157. By contrast, if a carrier is permitted to disaggregate and target to a maximum of two zones below the wire center level, there is greater incentive for the carrier to target support based only on the cost differentials between zones. For example, a rural carrier's wire center typically serves a small town and the surrounding agricultural areas. The cost of serving the town is significantly lower than the cost of serving the agricultural areas because of differences in population density and the distances of customers from the wire center. It is reasonable to expect that if two zones are developed, they would reflect the cost differences between serving the town and serving the agricultural areas respectively. If a carrier were to develop two zones in a manner that did not reflect these cost differences, the per-line support amount would not be related to the relative cost of serving the customer. This would result in the delivery of excessive support to one zone and thereby create an artificial incentive for a competitive carrier to enter in order to receive support in excess of its cost to serve the customer. Such a result is contrary to the incumbent carrier's interest. Given this outcome, we believe that less regulatory oversight is warranted as an initial matter with regard to developing two zones below the wire center level in contrast to three zones.

158. For this same reason, we reject the MAG proposal that carriers be permitted to disaggregate and target support up to three zones per wire center by filing these zones and the associated per-line support with the Commission, relevant state regulators and federal regulatory authorities, and USAC.<sup>384</sup> We note however, that, although carriers are precluded from self-certifying disaggregation plans for more than two zones below the wire center level, there are no such limitations on plans that may be approved by a state commission or other appropriate regulatory authority under Path Two. We disagree that Path Two does not represent a realistic option for disaggregating support to a level greater than two zones because the process would be a "lengthy and expensive one" and carriers would be faced with the process of having to repeat the process at any time due to fact that a plan approved under Path Two is "subject to change or challenge at any time."<sup>385</sup> While we acknowledge that a carrier may bear a heavier burden than under Path Three, we believe Path Two appropriately balances such burden with the greater need for scrutiny required of a plan that disaggregates support at a level greater than two zones below the wire center. Moreover, we note that Path Two, and the disaggregation and targeting scheme proposed by the Rural Task Force in general, as a consensus reflects the balancing of such concerns by rural carriers and competitive carries.

---

<sup>383</sup> See, e.g., SDITC Comments at 10; Texas Commission Comments at 7; M&B Reply Comments at 8.

<sup>384</sup> See *MAG NPRM*, 16 FCC Rcd at 464 para. 11, 495 App. A. Under the MAG proposal, support must be allocated in a manner reasonably related to the cost of providing service in each cost zone, and the plan must remain in effect for at least four years. See also Plains Rural Independent Companies Comments in CC Docket No. 00-256 at 14 (supporting the disaggregation of support to three zones); but see ASCENT Comments in CC Docket No. 00-256 at 6.

<sup>385</sup> See SDITC Comments at 9-10.

159. We agree with the Rural Task Force that certain general requirements should govern carriers' disaggregation plans and adopt those proposed by the Rural Task Force. We require that an incumbent carrier's study area support in total for a study area from the disaggregated method employed equal the total support available in the study area on a non-disaggregated basis. We also require that relative per-line support relationships between disaggregation zones for each disaggregated category of support remain fixed over time (except as changes are allowed by the Path descriptions described above) and that such relationships be made publicly available.<sup>386</sup> Once a competitive eligible telecommunications carrier is designated in a rural study area, per-line amounts to determine the competitive eligible telecommunications carrier's support should be based on the incumbent carrier's total support levels, lines, and disaggregated support relationships. We further require that the per-line support for each category of support in each disaggregation zone be determined such that the relative support relationships between zones will be maintained and that the product of all of the incumbent's lines for each cost zone multiplied by the per-line support for those zones when added together equal the sum of the incumbent's total level of support. Prior to the certification of a competitive eligible telecommunications carrier in a study area, monthly support payments to the incumbent carrier should be made based on the total annual amount of support for the study area divided by twelve. Finally, we require that per-line support amounts for each zone be recalculated whenever an incumbent's total annual support changes using the changed support amounts and lines at that point in time.

160. We find that these general requirements will ensure that the disaggregation and targeting of support is accomplished in a manner that is consistent with the universal service principles of specificity, predictability, and competitive neutrality.<sup>387</sup> By requiring that carriers make publicly available the per-line level of support for lines served in a particular zone and the basis for the disaggregation method, the distribution of disaggregated support will remain specific and predictable. Similarly, because support is portable among all eligible telecommunications carriers and disaggregated in a manner that ensures that support levels remain constant on a relative basis between zones regardless of the disaggregation and targeting path chosen, the distribution of support is competitively neutral. We expect the states will apply these general requirements to the approval and oversight of disaggregation and targeting plans implemented pursuant to this Order.<sup>388</sup>

161. We also recognize, as did the Rural Task Force and several commenters, that the integrity and flow of information to competitors is central to ensuring that support is distributed in a competitively neutral manner.<sup>389</sup> We find that in order to ensure portability and predictability in the delivery of support, rural incumbent local exchange carriers must submit to USAC maps in which the boundaries of the designated disaggregation zones of support are clearly specified, which USAC will make available for public inspection by competitors and other interested parties. We require that, when submitting information in support of self-certification, an incumbent carrier must provide USAC with publicly available information that allows competitors to verify and reproduce the algorithm used to determine zone support levels. As discussed above, the carrier also must demonstrate that the underlying rationale is

---

<sup>386</sup> For example, assume a study area with support disaggregated into two zones A and B each with 100 lines. Total support is \$3000 and support is disaggregated such that zone A receives \$10 per line and zone B receives \$20 per line. Thus, relative per line support is \$20/\$10 per line. Because per-line support relationships are to be fixed, zone B always receives twice as much support as zone A. If support were to decrease to \$2700 for the study area, zone A support would decrease to \$9 per line and zone B support would decrease to \$18 per line.

<sup>387</sup> See 47 U.S.C § 254(b)(5); *First Report and Order*, 12 FCC Rcd 8801-03 paras. 46-51.

<sup>388</sup> If a competitive eligible telecommunications carrier or other party believes that a state approved disaggregation plan is inconsistent with these general requirements, or the specific requirements enumerated under each of the various paths, it may file a petition for declaratory ruling, rulemaking, or other appropriate action with the Commission.

<sup>389</sup> See, e.g., CUSC Comments App. A at 10.

reasonably related to the cost of providing service for each cost zone within each disaggregated category. Similarly, we require carriers electing Path One to submit to USAC a copy of the certification to the state commission or appropriate regulatory authority certifying that it will not disaggregate and target support. Carriers selecting Path Two must submit a copy to USAC of the order approving the disaggregation plan submitted by the carrier to the state commission or appropriate regulatory authority and a copy of the disaggregation plan approved by the state commission or appropriate regulatory authority.

162. We decline to adopt WorldCom's proposal that we should not permit disaggregation of rural carrier universal service high-cost support until work on rural carrier specific inputs to the forward-looking model has been completed. According to WorldCom, the Commission recognized in the *First Report and Order* that "the only reasonable approach to disaggregation is to use a forward-looking cost model to allocate support among zones."<sup>390</sup> Contrary to WorldCom's contention, the Commission, while endorsing the use of a forward-looking mechanism to determine high-cost support for rural carriers in the future, simply recognized that once in place "such a mechanism could target support by calculating costs over a smaller geographic area than study areas currently used."<sup>391</sup> The Commission did not find that the use of a forward-looking mechanism is the only reasonable approach to disaggregation nor did the Commission address the issue of the appropriate methodology for the disaggregation of support during the period prior to the implementation of a forward-looking mechanism for rural carriers.<sup>392</sup>

163. We also reject the proposal to require disaggregation consistent with unbundled network element (UNE) zones in order not to discourage competition in some rural zones while artificially stimulating competition in others through universal service support windfalls.<sup>393</sup> As an initial matter, we note that a rural carrier is not required to provide UNEs until it has received a request to provide them and the state commission determines that the request is not unduly economically burdensome, is technologically feasible, and is consistent with section 254 of the Act.<sup>394</sup> Thus, as a general matter, rural carriers would not necessarily establish unbundled network element rates or zones. Moreover, as discussed above, the flexibility inherent in the Rural Task Force's proposal allows for the disaggregation and targeting of support to levels which may be more geographically deaveraged than a UNE zone level thus delivering a per-line level of support more closely associated with the cost of providing service.<sup>395</sup>

164. Finally, we note that the Rural Task Force recommended that the level of disaggregation of support be considered in determining whether to certify new eligible telecommunications carriers for a service area other than the entire study area of rural carrier study area. We believe that the level of disaggregation of support should be considered in determining whether to certify new eligible telecommunications carriers for a service area other than a rural carrier's entire study area to ensure that competitive neutrality is maintained between incumbent carriers and competitive eligible telecommunications carriers.

---

<sup>390</sup> WorldCom Comments Attachment at 9 (citing the *First Report and Order*, at para. (sic) 293).

<sup>391</sup> *First Report and Order*, 12 FCC Rcd at 8935-36 para 293.

<sup>392</sup> As WorldCom concedes, "[t]he Commission found in the [*First Report and Order*], that the ability to target support to smaller areas is one of the benefits of a forward-looking economic cost methodology." WorldCom Comments Attachment at 9 n.19.

<sup>393</sup> See California Commission Comments at 14.

<sup>394</sup> See 47 U.S.C. § 251(f).

<sup>395</sup> See 47 C.F.R. § 54.307(a)(2).

## E. Duration of the Rural Task Force Plan

### 1. Background

165. The Rural Task Force urged that its recommendation be implemented immediately and remain in place over a five-year period.<sup>396</sup> In support of this proposal, the Rural Task Force argued that “it is unrealistic to expect any universal service mechanism to provide a stable, predictable and workable funding source for a period longer than five years.”<sup>397</sup>

166. The Joint Board did not state a position on the overall duration of the Rural Task Force’s plan, but urged the Commission to refer to the Joint Board, no later than January 1, 2002, a proceeding to consider implementation of an appropriate high-cost mechanism for rural telephone companies after the expiration of the Rural Task Force’s plan.<sup>398</sup> According to the Joint Board, this proposed timing would permit the Joint Board and the Commission to consider the appropriate rural mechanism to succeed the Rural Task Force’s recommendation and devote sufficient time to the task prior to the termination of that plan. The Joint Board noted that the Commission and the Joint Board already are committed to reviewing the operation of the high-cost support mechanism for non-rural carriers on or before January 1, 2003.<sup>399</sup> The Joint Board also recommended eventual comprehensive review of the high-cost support mechanisms for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently and in a coordinated fashion. The Joint Board urged the Commission to use the transitional period during which a modified embedded cost mechanism is in place to develop a long-term universal service plan that better targets support to rural companies serving the highest cost areas and that recognizes the significant distinctions among rural carriers and between rural and non-rural carriers.

### 2. Discussion

167. We agree with the Rural Task Force that a modified version of the current high-cost loop support mechanism under Part 36 of the Commission’s rules should remain in place for no more than five years. Although the modifications we adopt are transitional in nature, we believe that providing rural telephone companies with a predictable level of universal service support during a five-year period will create a stable environment that will enable rural telephone companies to continue providing supported services at affordable rates to rural America. We therefore disagree with those commenters that claim the Rural Task Force’s proposals will not provide stability to rural carriers.<sup>400</sup> We find that the Rural Task Force’s proposed framework, with the modifications discussed herein, shall remain in place for five years. We would expect the Commission to consult with the Joint Board before allowing the plan to remain in effect longer than five years.

168. As we have stated, the duration of this interim plan is five years. In order to ensure that we have adequate time to consider, in consultation with the Joint Board, how these complex support issues should be addressed after five years, we intend to refer these issues to the Joint Board no later than January 1, 2002.<sup>401</sup> We agree with the Joint Board that this proposed timing will permit the Joint Board

---

<sup>396</sup> See Rural Task Force Recommendation at 15.

<sup>397</sup> *Id.*

<sup>398</sup> See *Joint Board Recommended Decision* at para. 21.

<sup>399</sup> See *id.* (citing *Federal-State Joint Board on Universal Service, Access Charge Reform*, CC Docket Nos. 96-45, 96-262, Seventh Report & Order and Thirteenth Order on Reconsideration in CC Docket No. 96-45, Fourth Report & Order in CC Docket No. 96-262, and Further Notice of Proposed Rulemaking, 14 FCC Rcd 8077, 8123 para. 94 (1999)).

<sup>400</sup> See, e.g., Texas Commission Comments at 3.

<sup>401</sup> See *Joint Board Recommended Decision* at para. 21.

and the Commission to consider the appropriate rural mechanism to succeed the plan we are adopting pursuant to the Rural Task Force's recommendation and to devote sufficient time to the task prior to the termination of that plan.

169. Consistent with the Joint Board's recommendations and in the context of the Joint Board's consideration of an appropriate high-cost mechanism for rural telephone companies, we anticipate conducting a comprehensive review of the high-cost support mechanisms for rural and non-rural carriers as a whole to ensure that both mechanisms function efficiently and in a coordinated fashion. We will use the transitional period during which a modified embedded cost mechanism is in place to develop a long-term universal service plan that better targets support to rural telephone companies serving the highest cost areas and recognizing the significant distinctions among rural carriers and between rural and non-rural carriers. In addition, we would include in that comprehensive review consideration of general issues related to excessive fund growth and competitive neutrality.

170. In developing a long-term universal service plan that better targets support to the highest cost rural areas, we intend to consider all options, including the use of forward-looking costs, to determine appropriate support levels for both rural and non-rural carriers. Although we find that distinct rural and non-rural mechanisms are appropriate at this time for the reasons discussed above, we are not convinced that this is a viable long-term solution. As we approach this task in the future, we will consider what plan best effectuates the mandates and goals of section 254 that supported services be provided at affordable and reasonably comparable rates to all Americans.

171. Although we recognize that the Act includes special provisions for markets served by rural telephone companies, we emphasize that these provisions do not require separate rural and non-rural universal service support mechanisms.<sup>402</sup> Several commenters argue that support should not be dependent upon the ownership characteristics of the carrier that happens to serve rural customers because section 254 requires comparable rates in rural *areas*.<sup>403</sup> The Maine and Vermont Commission emphasize that for every rural customer served by a rural telephone company, there are four rural customers served by a non-rural company.<sup>404</sup> These are important issues that we should consider further in the future.

172. We agree with the Rural Task Force that its empirical analysis showed that there are considerable differences between rural and non-rural carriers and significant variations among rural

---

<sup>402</sup> See *Tenth Report and Order*, 14 FCC Rcd at 20243 para. 200. See also Ad Hoc Telecommunications User Committee Comments at 13 ("The 1996 Act makes no distinction between rural and non-rural carriers when establishing the universal service guidelines. The 1996 Act requires no disparate treatment of rural and non-rural carriers when it directs the Commission to establish 'explicit and sufficient' support for universal service or when it specifies which carriers must contribute to the fund.") (citations omitted); Maine and Vermont Commissions Comments at 4 n.2 ("[T]he term [rural carrier] was not used in Section 254, and its use in the context of universal service actually obscures the objectives of Section 254, to make rates affordable and comparable for customers in all *rural areas*.").

<sup>403</sup> See, e.g., Ad Hoc Telecommunications User Committee Comments at 13 (urging the Commission "to recognize that rural, high cost areas are defined by their unique characteristics and not by the size of the companies that serve them, and to reject any universal service policies for rural and non-rural carriers alike, that do not reflect or incorporate this concept"); Maine and Vermont Commissions Comments at 4 n.2 (arguing that "any system based upon the classification of companies will necessarily be both under-inclusive and over-inclusive of the intended beneficiary class, namely rural high-cost customers"); see also Florida Commission Comments at 5 ("The amount of funding should not necessarily depend on the size of the serving carrier.")

<sup>404</sup> Maine and Vermont Commissions Comments at 4 n.1. Maine and Vermont Commissions urge the Commission to produce greater alignment between the rural and non-rural support mechanisms, focus support on rural carriers that have high overall costs, not merely high loop costs, and consider permitting non-rural companies to divide their study areas into rural and non-rural areas. *Id.* at 7.

carriers. At the same time, we observe that some of the data seem to show that some rural companies may be more similar to non-rural companies than to smaller rural companies.<sup>405</sup> We anticipate that our comprehensive review of the high-cost support mechanisms for rural and non-rural carriers as a whole will include an examination of our current classification of companies as rural or non-rural for purposes of receiving universal service support. In this regard, we believe that the information the Rural Task Force provided in *White Paper 2: The Rural Difference* will be valuable.

173. The Rural Task Force concluded that, in light of the differences between rural and non-rural carriers, a distinct rural mechanism is appropriate and recommended against use of the Commission's forward-looking high-cost mechanism for non-rural carriers to calculate support for rural carriers. Although we agree with the Rural Task Force that a distinct rural mechanism is appropriate at this time, we believe that there may be significant problems inherent in indefinitely maintaining separate mechanisms based on different economic principles.

174. The Commission previously determined that support based on forward-looking cost is sufficient for the provision of the supported services and sends the correct signals for entry, investment, and innovation.<sup>406</sup> Many commenters representing the interests of rural telephone companies argue that the Rural Task Force's analysis conclusively demonstrates that the forward-looking cost mechanism should not be used to determine rural company support and that only an embedded cost mechanism will provide sufficient support for rural carriers.<sup>407</sup> We disagree.<sup>408</sup> While the Rural Task Force demonstrated the inappropriateness of using input values designed for non-rural carriers to determine support for rural carriers, we do not find that its analysis justifies a reversal of the Commission's position with respect to the use of forward-looking cost as a general matter.<sup>409</sup>

---

<sup>405</sup> For example, the Rural Task Force reports that the average density is only 13 persons per square mile for areas served by rural carriers compared with 105 persons per square mile in areas served by non-rural carriers. At the same time, the average population density varies dramatically among rural carriers. Rural carriers in Alaska and Wyoming serve populations of 0.58 and 1.25 persons per square mile, respectively, while those in some states serve populations of over 100 persons per square mile. That is, some rural carriers serve areas with approximately the same density as the non-rural average. See Rural Task Force Recommendation at 11-12. Similarly, the Rural Task Force reports that average total plant investment per line ranges from \$3,000 for rural carriers with the largest study areas to over \$10,000 for rural carriers with the smallest study areas. The range of values for total plant investment per loop for rural carriers (\$1,400 to \$40,500) is far greater than the range for non-rural carriers (\$1,570 to \$4,350). That is, the largest rural carriers have an average total plant investment per line (\$3,000) that is lower than that of some non-rural carriers (\$4,350). See Rural Task Force Recommendation at 13.

<sup>406</sup> *First Report and Order*, 12 FCC Red at 8899 paras. 224-25. In rejecting arguments for basing support on a carrier's embedded cost, the Commission agreed with the Joint Board that "to the extent that it differs from forward-looking economic cost, embedded cost[s] provide the wrong signals to potential entrants and existing carriers. . . . [W]hen embedded costs are above forward-looking costs, support of embedded costs would direct carriers to make inefficient investments that may not be financially viable when there is competitive entry. . . . [I]f embedded cost is below forward-looking economic cost, support based on embedded costs, would erect an entry barrier to new competitors, because revenue per customer and support, together would be less than the forward-looking economic cost of providing supported services." *Id.* at 8901 para. 228.

<sup>407</sup> See, e.g., NRTA, OPASTCO, & USTA Reply Comments at 3; GVNW Consulting Reply Comments at 4.

<sup>408</sup> See *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d at 412; *Alenco Communications, Inc. v. FCC*, 201 F.3d at 619.

<sup>409</sup> The Rural Task Force proposed modifications to the current embedded cost system, rather than attempting to modify the Commission's forward-looking cost mechanism that currently is used to determine non-rural support. See Rural Task Force Recommendation at 17-19; *Recommended Decision* at para. 13. See also Ad Hoc Telecommunications User Committee Comments at 9-10 ("The RTF simply did not fulfill its mandate to evaluate whether or not the 'FLEC mechanism for rural carriers should have different platform design features or input values than the mechanism adopted for non-rural carriers.")(quoting Public Notice creating Rural Task Force); (continued....)

175. As some commenters point out, the Rural Task Force's analysis of the forward-looking mechanism was based on the results of running the existing high-cost universal service model for rural companies using non-rural inputs.<sup>410</sup> Because it found significant differences in comparing these results with actual company data, the Rural Task Force found that the model was not an appropriate tool for determining forward-looking costs of rural carriers. If inputs based on rural carrier data had been used, however, many of these differences could have been eliminated.<sup>411</sup> Other differences identified by the Rural Task Force with respect to individual companies are generally the discrepancies one would expect when inputs designed for non-rural companies are used for an analysis of rural costs.<sup>412</sup>

(Continued from previous page)

California Commission Comments at 3 ("The RTF, however, gives no consideration to modifying or improving the FCC's Synthesis Model for rural carrier purposes prior to concluding that universal service support should be based on embedded costs.").

<sup>410</sup> See Ad Hoc Telecommunications User Committee Comments at 9-10; WorldCom Comments at 2 ("Without exception, the issues the RTF discusses in its analysis of the Commission's synthesis model merely reflect input questions, not problems with the model structure itself.").

<sup>411</sup> For example, the Rural Task Force said "model lines differed significantly from actual lines served." Rural Task Force Recommendation at 17; see also GVNW Consulting Reply Comments at 4. This is not surprising because the Rural Task Force did not use current line count data as input values. Instead, the Rural Task Force used the line count data developed by AT&T's consultant for use in the industry-sponsored HAI model, which had been trued up to 1996 ARMIS line counts. Updating line counts on a regular basis is an important aspect of estimating costs in the non-rural mechanism. When the non-rural mechanism was adopted, the non-rural line counts were updated to reflect 1998 ARMIS line counts. See *Tenth Report and Order*, 14 FCC Rcd at 20186 para. 61. Line count input values for the non-rural mechanism were updated last year to reflect year-end 1999 line counts filed by the carriers pursuant to Part 36 of the Commission's rules. *Federal-State Joint Board on Universal Service*, CC Docket 96-45, Order, DA 00-2729 (rel. Dec. 8, 2000).

<sup>412</sup> For instance, the Rural Task Force said that model results for the type of plant varied from actual plant constructed. Rural Task Force Recommendation at 18; see also GVNW Consulting Reply Comments at 4. This is not surprising because the non-rural model currently uses nationwide plant mix values when developing the non-rural mechanism. Although the Commission sought comment on proposals to use company-specific or state-specific plant mix values, it found that there was no reasonable alternative to nationwide values at the time. See *Tenth Report and Order*, 14 FCC Rcd at 20257 para. 233. The Rural Task Force also said that the model underestimates wire center area. Rural Task Force Recommendation at 18; see also GVNW Consulting Reply Comments at 5. The wire center area reported by the model is the sum of the distribution areas. Model results report only the area within the wire center that is served. If, as it appears, the Rural Task Force's definition of area includes the entire area within a wire center, served and unserved, where the unserved can be lakes, mountains and deserts, then the Rural Task Force's area will always be greater than the model reported area. The Rural Task Force also said that the model underestimates switching investment. Rural Task Force Recommendation at 18; see also GVNW Consulting Reply Comments at 5. It is generally accepted that forward-looking switch costs are less than embedded switch costs. This conclusion is incorporated in the model switch estimation procedures through a negative trend coefficient. Thus, it can be claimed that the model underestimates switching investment by relying on the fact that embedded costs are greater than the forward-looking costs. Second, model switching investment is dependent on the number of lines connected to the switch. If the Rural Task Force had used current lines to estimate the model switch investment then that investment would have been higher. The Rural Task Force also said that the model results for general support investment varies widely from actual data. Rural Task Force Recommendation at 18; see also GVNW Consulting Reply Comments at 5. Model general support investment for rural companies was based on the average relationship between non-rural general support investment and forward looking network investment. Applying the average relationship to particular rural companies should generate results that have as many over-estimations as under-estimations. Thus, the results for rural companies simply and accurately reflect an input based on an average relationship. When rural carrier specific information becomes available this problem should be significantly mitigated. The Rural Task Force also said that the model underestimates network operations and corporate operations expenses. Rural Task Force Recommendation at 18; see also GVNW Consulting Reply Comments at 5. Model network operations and corporate operations expenses include only those related to universal service. Non-universal service expenses related to toll services, special access lines and mergers and acquisition have been removed from the total network and corporate operations (continued...)

176. In addition, the Rural Task Force acknowledged that the primary reason for the decrease in its estimated total support amounts for rural carriers is due to the statewide cost-averaging and nationwide benchmark employed in the non-rural mechanism to determine funding levels for non-rural carriers.<sup>413</sup> Indeed, the Rural Task Force's analysis in *White Paper 4* demonstrates how changing the area over which costs are averaged and changing the nationwide benchmark dramatically change support amounts.<sup>414</sup> That is, averaging and benchmarks have more impact on determining support levels than the cost estimates produced by the model. The Commission has long recognized that the mechanism used to determine forward-looking cost for rural carriers may differ from that used for non-rural carriers.<sup>415</sup> For instance, one could design a forward-looking mechanism for rural carriers that uses different benchmarks and averaging conventions.

177. We leave these issues for another day. Although we conclude that the Rural Task Force's analysis has not demonstrated that a forward-looking mechanism could never appropriately be used to estimate rural costs, we do not have sufficient information to do so at this time. Even those commenters who urge the Commission to move to forward-looking cost for rural carriers recognize that the Commission would need additional time to develop suitable rural input values.<sup>416</sup> Because the Commission has not developed rural inputs and it is not possible to determine forward-looking costs for rural carriers at this time, we find that rural carriers should continue to receive support based upon their embedded costs while the five-year plan adopted in this Order is in place.

## F. Identification of Service Locations

### 1. Background

178. All telecommunications carriers, including commercial mobile radio service (CMRS) carriers that provide supported services, regardless of the technology used, may be eligible to receive federal universal service support if they satisfy section 214(e)(1) of the Act.<sup>417</sup> Because such support is portable, a competitive eligible telecommunications carrier receives the same per-line high-cost support as an incumbent local exchange carrier for lines that it captures from the incumbent local exchange carrier, as well as for any "new" lines that the competitive eligible telecommunications carrier serves in the high-cost areas of the incumbent local exchange carrier.<sup>418</sup>

179. Consistent with its recommendation that high-cost support be disaggregated and targeted  
(Continued from previous page) \_\_\_\_\_  
expenses. Therefore, model expenses are and should be less than actual expenses. Comparing model expenses to actual expenses is inconsistent with the design and purpose of the universal service modeling process.

<sup>413</sup> See Rural Task Force Recommendation at 19.

<sup>414</sup> For example, if support were averaged at the study area level, rather than at the state level, the total amount of support to rural and non-rural carriers would double the amount available under the current embedded cost mechanism. *A Review of the FCC's Non-Rural Universal Service Fund Method and the Synthesis Model for Rural Telephone Companies: Rural Task Force White Paper 4* (Sept. 2000) (visited May 2, 2001) <<http://www.wutc.wa.gov/rtf>> at 18 (*White Paper 4*). If the benchmark were 115 percent of the nationwide average forward-looking cost instead of 135 percent, the total amount of support for rural and non-rural carriers would remain approximately the same as under the current mechanism. *White Paper 4* at 17.

<sup>415</sup> The Joint Board and the Commission "[did] not anticipate that all carriers will begin to receive universal service support in rural, insular, and high-cost areas based on forward-looking economic cost at the same time or even in an identical manner." *First Report and Order*, 12 FCC Rcd 8889 para. 203.

<sup>416</sup> See, e.g., WorldCom Comments at 3; Ad Hoc Telecommunications User Committee Reply Comments at 5-6.

<sup>417</sup> See 47 U.S.C. 254(e)(1); *First Report and Order*, 12 FCC Rcd at 8858 para. 145; *Seventh Report and Order and Thirteenth Order on Reconsideration*, 14 FCC Rcd at 8113 para. 72.

<sup>418</sup> See *Ninth Report and Order*, 14 FCC Rcd at 20480 para. 90.

below the study area level, the Rural Task Force recommended that a wireless mobile carrier providing service in an area served by a rural carrier use the customer's residential or business location as the basis for determining in which disaggregation zone a customer is located for purposes of targeting universal service support.<sup>419</sup> In making this recommendation, the Rural Task Force recognized that the use of any location address could allow arbitrage of the universal service support system. The Rural Task Force further recommended that the Commission establish a reasonable method for determining the customer location for mobile wireless customers. Finally, the Rural Task Force advocated that the Commission, or other appropriate regulatory authority, retain authority to prevent the misuse of mobile wireless customer locations and ensure that universal service support is being used in accordance with section 254(e).

## 2. Discussion

180. We adopt the Rural Task Force's recommendation that a wireless mobile carrier use a customer's location as the basis for determining in which disaggregation zone a customer is located for purposes of receiving high-cost universal service support for service provided to that customer. To that end, we find that a customer's billing address is a reasonable surrogate to identify a mobile wireless customer's location for the purpose of identifying a corresponding disaggregation zone and thus the appropriate per-line support level for service provided to the mobile wireless customer. We also clarify that this approach is applicable to competitive eligible telecommunications carriers providing mobile wireless service not only in a rural carrier's service area, but also in the service area of a non-rural carrier.

181. We recognize, as did the Rural Task Force and commenters, that, because mobile wireless carriers do not provide service at a fixed location, there is a question as to how to relate a mobile wireless carrier to a disaggregation zone for purposes of determining how much support a carrier is entitled to for serving that customer.<sup>420</sup> We find that a mobile wireless customer's billing address is a reasonable surrogate for the customer's location. Unlike wireline carriers or fixed wireless carriers,<sup>421</sup> who out of necessity must have a provisioning database to determine the point of service for their customers, mobile wireless carriers do not need such a database because a customer's point of use varies. Therefore, while some mobile wireless carriers may have databases that are similar to provisioning databases, most will have billing address databases. Thus, adoption of customer's billing address as a surrogate for service location eliminates the need for many mobile wireless carriers to create a new database for purposes of universal service funding. We note in this regard that in the *Local Competition and Broadband Reporting Report and Order*, we allow mobile wireless carriers who submit zip code data to use customer billing address as a surrogate for customer location because it is the most administratively easy solution to determining a customer's primary place of use.<sup>422</sup> Although we acknowledge that there may be several possible solutions to this problem,<sup>423</sup> we find that this approach is reasonable and the most administratively simple solution to this problem.<sup>424</sup>

---

<sup>419</sup> Rural Task Force Recommendation at 38.

<sup>420</sup> See *id.* at 38; *White Paper 5* at 21. See also CUSC Comments App. A at 15-16; John Staurulaukis, Inc. Comments at 16; Fred Williamson & Assoc. Comments at 9.

<sup>421</sup> Fixed wireless carriers, like wireline carriers, provision their services to a fixed point of use.

<sup>422</sup> *In the Matter of Local Competition and Broadband Reporting*, CC Docket No. 99-301, Report and Order, 15 FCC Rcd. 7717, 7785 (rel. Mar. 30, 2000).

<sup>423</sup> See John Staurulaukis, Inc. Comments at 16. Cf. Fred Williamson & Assoc. Comments at 9.

<sup>424</sup> See John Staurulaukis, Inc. Comments at 16 (“[u]se of the billing address is the most administratively tractable solution for the problem of defining a “fixed address” for service using a mobile station.”). Cf. CUSC Comments App. A at 15-16.

182. We, therefore, decline to use the residential or primary business location as a surrogate because, as noted above, not all mobile wireless carriers have databases capable of making such a determination. Further, we decline to use the system adopted by Congress in the Mobile Telecommunications Sourcing Act.<sup>425</sup> The Mobile Telecommunications Sourcing Act requires a designated database provider<sup>426</sup> or the states to develop an electronic database for determining the situs of customers' "place of primary use"<sup>427</sup> for purposes of state and local taxation.<sup>428</sup> Under this law, states or their designees will be required to establish an electronic database for making a determination on which municipality has taxing authority over the revenues generated by the customer.<sup>429</sup> In the event that such a database is not available, the carrier may take advantage of a safe harbor provision under which it certifies that it has "expended reasonable resources to implement and maintain an appropriately detailed electronic database of street address assignment to the taxing jurisdiction."<sup>430</sup> We note that the Mobile Telecommunications Sourcing Act's database provision does not require the states to establish such databases until some time after August 2001.<sup>431</sup> We therefore decline to impose such a requirement at this time. To do so would unnecessarily increase the administrative burden on mobile wireless carriers.

183. In reaching this determination, we acknowledge, as did the Rural Task Force, that the use of a customer's location address could allow arbitrage of the universal service support mechanism.<sup>432</sup> If a carrier were to engage in arbitrage, *e.g.*, misuse a customer's billing address by identifying a customer in a high-cost zone when service is primarily taken in a low cost zone for the purpose of receiving a higher level of per-line support, we will take appropriate enforcement action.<sup>433</sup> We will continue to monitor the reasonableness of using a customer's billing address as the surrogate for a mobile wireless customer's location in a disaggregation zone for universal service purposes. As more mobile wireless carriers are designated as eligible to receive support, we may revisit this approach in the future.

184. Finally, consistent with our decision here, we also conclude that a competitive eligible telecommunications carrier providing mobile wireless service should use a customer's billing address for purposes of determining the appropriate amount of support for providing service to a customer in the service area of a non-rural incumbent local exchange carrier. In the *Ninth Report and Order*, the Commission adopted a targeting methodology for the delivery of high-cost support for non-rural carriers in

---

<sup>425</sup> CUSC Comments App. A at 15-16. *See also* 4 U.S.C. §§ 116-124.

<sup>426</sup> Defined as "a corporation, association, or other entity representing all the political subdivisions of a State that is: (A) responsible for providing an electronic database as prescribed in section 119(a) if the State has not provided such electronic database; and (B) approved by municipal and county associations or leagues of the State whose responsibility it would otherwise be to provide such database prescribed by sections 116 through 126 of this Title." 4 U.S.C. § 124 (3)(A), (B).

<sup>427</sup> Defined as "the street address representative of where the customer's use of the mobile telecommunications service primarily occurs." 4 U.S.C. § 124 (8).

<sup>428</sup> 4 U.S.C. § 117.

<sup>429</sup> 4 U.S.C. § 119.

<sup>430</sup> 4 U.S.C. § 120.

<sup>431</sup> 47 U.S.C. §§ 116, 119 (this provision is "applicable only to customer bills issued after the first day of the first month beginning more than two years after July 28, 2000").

<sup>432</sup> *See* Rural Task Force Recommendation at 38-39.

<sup>433</sup> *See Seventh Report and Order*, 14 FCC Rcd at 8115-16 para. 78. States or other parties may petition the Commission, under section 208 of the Act, if they believe a carrier has misapplied its high-cost support, and may also fully avail themselves of the Commission's formal complaint procedures to bring any alleged misapplication of high-cost support before the Commission. *See also Ninth Report and Order*, 14 FCC Rcd at 20488 para. 110.

which support is targeted to high-cost wire centers.<sup>434</sup> The Personal Communications Industry Association (PCIA) requests that the Commission clarify how to determine which wire center should be used to determine the amount of support for any particular wireless customer.<sup>435</sup> PCIA contends that a customer's address is the most accurate surrogate for the incumbent's wire center and therefore support for mobile wireless customers should be based on the wire center associated with the customer's address.<sup>436</sup> We grant PCIA's request for clarification of the Commission's decision in the *Ninth Report and Order* to the extent it seeks clarification on the limited issue of assigning mobile wireless customers to the incumbent local exchange carrier's wire center.<sup>437</sup> We clarify that a mobile wireless customer's billing address is a reasonable surrogate for the customer's address for assigning the customer's location to a wire-center in a non-rural carrier's study area to target universal service support.<sup>438</sup>

## G. State Certification Under Section 254(e)

### 1. Background

185. Under section 254(e) of the Act, carriers must use universal service support "only for the provision, maintenance and upgrading of facilities and services for which the support is intended."<sup>439</sup> In the *Ninth Report and Order*, the Commission concluded that because the support provided to non-rural carriers is intended to enable the reasonable comparability of intrastate rates, and states have primary jurisdiction over intrastate rates, it is most appropriate for states to determine whether support is used consistent with section 254(e).<sup>440</sup> Accordingly, the Commission adopted, as a regulatory safeguard, rules requiring states seeking federal universal service high-cost support for non-rural carriers within their territory to file annually a certification with the Commission and USAC. The certification must state that all federal high-cost funds flowing to non-rural carriers in that state and/or competitive eligible telecommunications carriers seeking high-cost support in the service area of a non-rural carrier in that state, will be used in a manner consistent with section 254(e).<sup>441</sup> Absent such certification, a carrier

---

<sup>434</sup> See *id.* at 20470-73 paras. 70-76.

<sup>435</sup> See Petition for Reconsideration and/or Clarification of the Personal Communications Industry Association (PCIA Petition), CC Docket No. 96-45 at 4-5.

<sup>436</sup> We note that PCIA's petition, in requesting that support for mobile wireless carriers be based on "the wire center associated with the *customer's address*," does not provide additional guidance on the issue of what the customer's address is for mobile wireless carriers. PCIA Petition at 4 (emphasis added).

<sup>437</sup> We note that on reply PCIA states no party opposed its recommended approach. See Reply Comments of the Personal Communications Industry Association, CC Docket No. 96-45 at 2.

<sup>438</sup> PCIA states that a wireless carrier does not necessarily know the address of a prepaid customer, and therefore, it may not be possible to determine support for these customers based on address. See PCIA Petition at 4 n.6. In this Order we do not resolve the issue of how to assign prepaid mobile wireless customers when the carrier does not have customer billing address information. We will review this issue on a case-by-case basis.

<sup>439</sup> 47 U.S.C. § 254(e).

<sup>440</sup> *Ninth Report and Order*, 14 FCC Rcd at 20482 para. 95. The Commission noted that as long as the uses prescribed by the state are consistent with section 254(e), the states should have the flexibility to decide how carriers use the support provided by the federal mechanism. *Id.* at 20483 para. 96.

<sup>441</sup> *Id.* at 20483 para. 97. To ensure that carriers receiving *interstate* access universal service support will use that support in a manner consistent with section 254(e), the Commission adopted a certification scheme requiring carriers seeking such support to file a certification with the Commission stating that the carrier will use its support only for the provision, maintenance, and upgrading of facilities and service for which the support is intended. See *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers*, CC Docket Nos. 96-262 and 94-1, Sixth Report and Order, *Low-Volume Long-Distance Users*, CC Docket No. 99-249, Report and Order, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Eleventh Report and Order, 15 FCC Rcd 12962, 13062 (continued....)

cannot receive support.<sup>442</sup>

186. In its recommendation, the Rural Task Force recognized the need for accountability in the administration of the high-cost support mechanism for rural carriers.<sup>443</sup> The Rural Task Force found that existing procedures used by NECA, USAC, the Commission, and state commissions reasonably promote such accountability. The Rural Task Force recommended that the Commission delegate to the states responsibility for oversight of section 254(e) in a manner similar to that used for non-rural carriers.<sup>444</sup>

## 2. Discussion

187. We conclude that states should be required to file annual certifications with the Commission to ensure that carriers use universal service support “only for the provision, maintenance and upgrading of facilities and services for which the support is intended” consistent with section 254(e). We conclude that the mandate in section 254(e) applies to *all* carriers, rural and non-rural, that are designated as eligible to receive support under section 214(e) of the Act.<sup>445</sup> As we concluded with regard to non-rural carriers, the federal high-cost support that is provided to rural carriers is intended to enable the reasonable comparability of intrastate rates, and states have jurisdiction over intrastate rates. Given that states generally have primary authority over carriers’ intrastate activities, we believe that the state certification process provides the most reliable means of determining whether carriers are using support in a manner consistent with section 254(e). Accordingly, we will require states that wish to receive federal universal service high-cost support for rural carriers within their boundaries to file a certification with the Commission and USAC stating that all federal high-cost funds flowing to rural carriers in that state will be used in a manner consistent with section 254(e).<sup>446</sup> Absent such certification, carriers will not receive such support.

188. We recognize that some state commissions may have only limited regulatory oversight to ensure that federal support is reflected in intrastate rates. In the case of non-rural carriers, we concluded that states nonetheless may certify to the Commission that a non-rural carrier in the state had accounted to the state commission for its receipt of federal support, and that such support will be used “only for the provision, maintenance and upgrading of facilities and services for which the support is intended.”<sup>447</sup> We determined that, in states in which the state commission has limited jurisdiction over such carriers, the state need not initiate the certification process itself.<sup>448</sup> Instead, non-rural local exchange carriers, and competitive eligible telecommunications carriers serving lines in the service area of the non-rural local

(Continued from previous page) \_\_\_\_\_

para. 232 (*Interstate Access Support Order*), *pets. for review pending*, Texas Office of Public Util. Counsel et al. v. FCC, 5<sup>th</sup> Cir. No. 00-60434 (and consolidated cases) (2000). See 47 C.F.R. § 54.809.

<sup>442</sup> *Ninth Report and Order*, 14 FCC Rcd at 20484 para. 98. See 47 C.F.R. § 54.313(a).

<sup>443</sup> Rural Task Force Recommendation at 33.

<sup>444</sup> *Id.*

<sup>445</sup> See 47 U.S.C. § 254(e).

<sup>446</sup> As explained above, three federal universal service mechanisms provide high-cost support for rural carriers. These include high-cost loop support, LSS and LTS. See *supra* para. 13. High-cost loop support provides support for a portion of a carrier’s total cost allocated to the intrastate jurisdiction. Similarly, LSS is available to support the intrastate switching costs of carriers with 50,000 or fewer lines. By contrast, LTS supports interstate allocated loop costs of non-price cap carriers (typically small, rural carriers) that participate in the NECA common line pool. Because the Commission has primary jurisdiction over interstate rates, oversight of the use of LTS lies with the Commission. See *Interstate Access Support Order*, 15 FCC Rcd at 13062 para. 232. We anticipate addressing certification of LTS when we address interstate access reform in the MAG proceeding. See *infra* n.1.

<sup>447</sup> *Ninth Report and Order*, 14 FCC Rcd at 20483 para. 97.

<sup>448</sup> *Id.*

exchange carriers, may formulate plans to ensure compliance with section 254(e), and present those plans to the state, so that the state may make the appropriate certification to the Commission.<sup>449</sup> We conclude that this approach is equally appropriate here with regard to rural carriers and competitive eligible telecommunications carriers serving lines in the service area of a rural local exchange carrier. Absent the filing of such certification, carriers will not receive federal universal service support.

189. We also recognize that, in limited instances, certain carriers may not be subject to the jurisdiction of a state (*e.g.*, certain tribally-owned carriers). In such instances, there is no state regulatory authority to ensure compliance with section 254(e). We conclude that, in these limited instances, a carrier shall certify directly to the Commission that federal high-cost support will be used in a manner consistent with section 254(e). The certification must be filed in the form of a sworn affidavit executed by a corporate officer attesting to the use of the support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended pursuant to section 254(e) of the 1996 Act. A copy of this letter must also be submitted to USAC. Absent such a certification, carriers will not receive federal universal service support.

190. The certification requirement we adopt is applicable to all rural carriers and competitive eligible telecommunications carriers seeking high-cost support in the service area of a rural local exchange carrier. States, or carriers not subject to the jurisdiction of a state, shall file this certification annually. If filed by the state, the certification shall be applicable to all rural carriers and competitive eligible telecommunications carriers seeking high-cost support in the service area of a rural local exchange carrier that the state certifies as eligible to receive federal high-cost during that annual period.<sup>450</sup> The certification may be filed in the form of a letter from the appropriate state regulatory authority, or authorized corporate officer where the state lacks jurisdiction, and shall be filed with the Commission and USAC. A state may file a supplemental certification for carriers that were not eligible for support at the time the state filed its initial certification. In the event that a state determines that a carrier has not complied with section 254(e), the state shall have the authority to revoke certification. In addition, because states are responsible for filing section 254(e) certifications with the Commission, challenges to the propriety of the certifications, or revocation of the certifications, should be brought at the state level.

191. Under our existing rules, USAC submits to the Commission estimated universal service support requirements, including high-cost support, two months prior to the beginning of each quarter.<sup>451</sup> Thus, for the first quarter of 2002, USAC will submit estimated universal service support requirements on or before November 1, 2001. In order for USAC to submit an accurate estimate of the level of high-cost and local switching support, it will need to know which carriers have been certified pursuant to the section 254(e)-certification process. To allow USAC sufficient time to process section 254(e) certifications and estimate the level of high-cost support, we conclude that certifications should be filed one month before USAC's quarterly filing is due, that is on October 1. In the event that a certification is filed untimely, the carriers subject to that certification will not be eligible for support until the quarter for which USAC's subsequent filing is due. For example, if a state files a section 254(e) certification after October 1, 2001, but on or before January 1, 2002, the carrier would not be eligible for support until the second quarter of 2002.<sup>452</sup> In the event that a state revokes a certification, the state must notify USAC and the Commission within 30 days of the revocation.

---

<sup>449</sup> *Id.*

<sup>450</sup> The timing and effectiveness of these annual certifications are discussed *infra* in para. 191.

<sup>451</sup> 47 C.F.R. § 54.709(a)(3). The Commission uses those support requirements to establish a contribution factor for the upcoming quarter. *See* 47 C.F.R. § 54.709(a). USAC then uses the contribution factor to bill carriers and collect the appropriate amount of support to fund the universal service programs. *Id.*

<sup>452</sup> *See* Appendix A for the relevant rules.

192. In adopting this certification scheme, we recognize that rural carriers are receiving federal high-cost support under our existing rules and may be entitled to additional levels of federal high-cost support under our revisions to these rules, which will be effective July 1, 2001. We will not, however, require certifications for the last two quarters of 2001. Rather, we will require certifications to be submitted initially on October 1, 2001 for the first full year of implementation, January 1, 2002 – December 31, 2002. We acknowledge that, as a result, we will not have certifications for support distributed for the last two quarters of 2001. We believe that permitting the continued delivery of support during these two quarters without certification will ease the transition to the revised mechanism for states, carriers, and USAC, and ensure that the benefits accruing from its adoption are realized as quickly as possible. We note that we have the authority to take enforcement action against a carrier if we should determine that support is being used in a manner inconsistent with section 254(e).<sup>453</sup> We believe that this enforcement power will afford sufficient protection against abuse during this limited period of transition.

193. Finally, we reconsider, on our own motion, the existing rule requiring state certification of the use of universal service support by non-rural incumbent local exchange carriers and eligible telecommunications carriers serving lines in the service area of a non-rural incumbent local exchange carrier adopted in the *Ninth Report and Order*.<sup>454</sup> In its current form, the rule does not recognize that in limited instances, certain carriers may not be subject to the jurisdiction of a state. As a result, the rule does not provide a mechanism by which such a carrier's use of support can be certified as consistent with section 254(e). Consistent with our determination with regard to rural carriers and eligible telecommunications carriers serving lines in the service area of a rural incumbent local exchange carrier, we conclude that in these limited instances, a carrier shall certify directly to the Commission that federal high-cost support will be used in a manner consistent with section 254(e). The certification must be filed in the form of a sworn affidavit executed by a corporate officer attesting to the use of the support only for the provision, maintenance and upgrading of facilities and services for which the support is intended pursuant to section 254(e) of the Act. A copy of this letter must also be submitted to USAC. Absent such a certification, carriers will not receive support.<sup>455</sup>

## H. Advanced Services

### 1. Background

194. Section 254(c) of the Act defines universal service as an “evolving level of telecommunications services that the Commission shall establish periodically[.]”<sup>456</sup> In 1997, based on consideration of the definitional criteria set forth in section 254(c) and the Joint Board's recommendations, the Commission designated nine “core” services that are eligible for universal service support: single-party service; voice grade access to the public switched telephone network; Dual Tone Multifrequency signaling or its functional equivalent; access to emergency services; access to operator services; access to interexchange service; access to directory assistance; and toll limitation services for qualifying low-income

---

<sup>453</sup> See *Seventh Report and Order*, 14 FCC Rcd at 8115-16 para. 78. States or other parties may petition the Commission, under section 208 of the Act, if they believe a carrier has misapplied its high-cost support, and may also fully avail themselves of the Commission's formal complaint procedures to bring any alleged misapplication of federal high-cost support before the Commission. See also *Ninth Report and Order*, 14 FCC Rcd at 20488 para. 110.

<sup>454</sup> See *id.* at 20482-88 paras. 93-110. See also 47 C.F.R. § 54.313. This reconsideration on the Commission's own motion is appropriate given the pendency of petitions for reconsideration of the Commission's *Ninth Report and Order*. See *Central Florida Enterprises v. FCC*, 598 F.2d 37, 48 n.51 (D.C. Cir. 1978), *cert. dismissed*, 441 U.S. 957 (1979).

<sup>455</sup> See Appendix A for the relevant rule.

<sup>456</sup> 47 U.S.C. § 254(c)(1).

consumers.<sup>457</sup>

195. The 1996 Act addresses advanced telecommunications and information services in sections 254(b) and 706. Section 254(b) establishes the universal service principles that access to such services should be provided in all regions of the Nation, and should be reasonably comparable in rural, insular, and high-cost areas to the access in urban areas.<sup>458</sup> Section 706 directs the Commission and the states to utilize various regulatory methods to “encourage deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans[.]”<sup>459</sup>

196. The Rural Task Force recommended that the Joint Board review the definition of services that are supported by the federal universal service mechanisms.<sup>460</sup> It also recommended that the list of supported services “should evolve to include access to information services at a rate that is reasonably comparable to that provided in urban areas.”<sup>461</sup>

197. In addition, the Rural Task Force stated that its recommendation to continue distributing support to rural carriers based on their embedded costs “inherently provides incentives for the infrastructure investments necessary for providing access to advanced services.”<sup>462</sup> It recommended the adoption of a “no barriers to advanced services” policy for rural carriers, which it indicated would be comparable to that applied in connection with the forward-looking high-cost mechanism for non-rural

---

<sup>457</sup> *First Report and Order*, 12 FCC Rcd at 8807-25 paras. 56-87; see 47 U.S.C. § 254(c)(1).

<sup>458</sup> 47 U.S.C. §§ 254(b)(2), (3).

<sup>459</sup> Section 706(c) of the 1996 Act, reproduced in the notes under 47 U.S.C. § 157; see *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to all Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, CC Docket No. 98-146, Second Report, 15 FCC Rcd 20913 (2000) (*Second 706 Report*). Section 706 generally defines advanced telecommunications capability as “high-speed, switched, broadband telecommunications capability that enables users to originate and receive high-quality voice, data, graphics, and video telecommunications using any technology. In the *Second 706 Report*, the Commission defined as “advanced” for section 706 purposes services with a transmission speed of at least 200 kilobits per second (kbps) in two directions (provider-to-customer and customer-to-provider), and as “high-speed” services with a speed of at least 200 kbps in one direction. *Section 706 Report*, 15 FCC Rcd at 20921 para. 11.

<sup>460</sup> Rural Task Force Recommendation at 22. The Rural Task Force stated that “[t]he provision of access to advanced services . . . is separate and distinct from the actual provision of advanced services when and if they have been added to the supported services defined periodically by the FCC under Section 254(c).” *Id.* We note that, contrary to the Rural Task Force’s suggestion, inclusion of a service on the list of supported services under section 254(c) generally means that universal service mechanisms support *access* to the service, rather than “the actual provision” of the service.” *Id.*; see, e.g., *First Report and Order*, 12 FCC Rcd at 8817 para. 74 (“we support the telecommunications network components necessary for access . . . , but not the underlying services themselves”).

<sup>461</sup> Rural Task Force Recommendation at 23. In 1997, the Commission determined that dial-up Internet access should not be supported separately from voice grade access “because the record does not indicate that a substantial majority of residential customers currently subscribe to Internet access by using access links that provide higher quality than voice grade access.” *First Report and Order*, 12 FCC Rcd at 8823 para. 83. In 1999, the Commission’s Common Carrier Bureau sought comment on requests by the Rural Utilities Service (RUS) and three state commissions to redefine voice grade access by increasing the minimum frequency range from 300-3,000 Hertz (Hz) to approximately 200-3,500 Hz. RUS and these states expressed concerns that the current definition does not ensure that consumers in rural areas using 28.8 kbps modems for Internet access can achieve data transmission speeds reasonably comparable to those achieved by consumers in urban areas using the same modems. *Common Carrier Bureau Seeks Comment on Requests to Redefine “Voice Grade Access” for Purposes of Federal Universal Service Support*, CC Docket No. 96-45, Public Notice, DA 99-2985 (rel. Dec. 22, 1999).

<sup>462</sup> Rural Task Force Recommendation at 22.

carriers.<sup>463</sup> The Rural Task Force recommended that the “no barriers” policy incorporate the following general principles: (1) support should be provided for plant “that can, either as built or with the addition of plant elements, when available, provide access to advanced services[;]” (2) “carriers should be encouraged by regulatory measures to remove infrastructure barriers relating to access to advanced services[;]” and (3) “[t]he federal universal service support fund should be sized so that it presents no barriers to investment in plant needed to provide access to advanced services.”<sup>464</sup>

## 2. Discussion

198. The definition of universal service under section 254(c) of the Act is a matter currently pending before the Joint Board. The Commission asked the Joint Board to review the list of supported services and, if warranted, recommend modifications.<sup>465</sup> Among other things, the Commission asked the Joint Board to consider the record on requests to redefine voice grade access to ensure reasonable comparability of dial-up Internet access in urban and rural areas.<sup>466</sup> In accordance with section 254(c), the Commission will consider whether any modifications to the list of supported services are warranted after the Joint Board completes its review.<sup>467</sup>

199. We agree with the Rural Task Force that our universal service policies should not inadvertently create barriers to the provision of access to advanced services, and believe that our current universal service system does not create such barriers.<sup>468</sup> Initially, we emphasize that section 254(b) states that access to advanced services “should” be provided, and the Fifth Circuit has held that section 254(b) establishes “principles that the FCC should consider in developing its policies” rather than specific statutory commands.<sup>469</sup> As the Rural Task Force recognized, the Commission’s existing high-cost loop support mechanism for rural carriers “inherently provides incentives for the infrastructure investments necessary for providing access to advanced services.”<sup>470</sup>

200. Contrary to the arguments of some commenters, use of support to invest in infrastructure capable of providing access to advanced services does not violate section 254(e), which mandates that support be used “only for the provision, maintenance, and upgrading of facilities and services for which the support is intended.”<sup>471</sup> The public switched telephone network is not a single-use network. Modern network infrastructure can provide access not only to voice services, but also to data, graphics, video, and

---

<sup>463</sup> *Id.* The forward-looking high-cost support mechanism for non-rural carriers provides support for plant that does not impede the provision of access to advanced services. *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, *Forward-Looking Mechanism for High Cost Support for Non-Rural LECs*, CC Docket No. 97-160, Fifth Report and Order, 13 FCC Rcd 21323, 21351-52 paras. 68-70 (1998).

<sup>464</sup> Rural Task Force Recommendation at 22-23.

<sup>465</sup> *Referral Order*, 15 FCC Rcd 25257.

<sup>466</sup> *Id.* at 25256 para. 3; *see supra* n.461.

<sup>467</sup> *See* 47 U.S.C. § 254(c)(2) (“The Joint Board may, from time to time, recommend to the Commission modifications in the definition of the services that are supported by Federal universal service support mechanisms”); NYDPS Comments at 6; Sprint Comments at 3; Texas Commission Comments at 8.

<sup>468</sup> *See* Rural Task Force Recommendation at 22; *supra* n.463.

<sup>469</sup> *Texas Office of Public Utility Counsel v. FCC*, 183 F.3d at 421; 47 U.S.C. § 254(b); *cf.* Rural Task Force Recommendation at 22-23 (“The provision of access to advanced services is required under Section 254(b) . . . Sections 254(b)(2) and (3) require access to information services that is reasonably comparable to that provided in urban areas.”).

<sup>470</sup> Rural Task Force Recommendation at 22.

<sup>471</sup> 47 U.S.C. § 254(e); *see, e.g.*, NYDPS Comments at 5-7.

other services. High-cost loop support is available to rural carriers “to maintain existing facilities and make prudent facility upgrades[.]”<sup>472</sup> Thus, although the high-cost loop support mechanism does not support the provision of advanced services, our policies do not impede the deployment of modern plant capable of providing access to advanced services. Rural carriers may consider both their present and future needs in determining what plant to deploy, knowing that prudent investment will be eligible for support.<sup>473</sup> The measures that we adopt in this Order will increase incentives for carriers to modernize their plant by increasing the total amount of high-cost loop support available under the cap.

201. As we move forward in the future, we will consider ways to ensure that we do not create regulatory barriers to the deployment of advanced services. The principal thrust of the “no barriers” proposal appears to be that the Commission should require carriers to deploy plant capable of providing access to advanced services, and encourage them to replace plant that cannot provide such access.<sup>474</sup> Moreover, we believe any specific policies we adopt in this area should apply uniformly to all local exchange carriers, rather than as part of a transitional high-cost support mechanism for rural carriers.<sup>475</sup> Therefore, we believe that the “no barriers” policy as specifically proposed by the Rural Task Force should be considered further in connection with our comprehensive review of the high-cost loop support mechanisms for rural and non-rural carriers. In accordance with our mandate under section 706, we will continue to examine whether deployment of advanced telecommunications capability to all Americans is progressing in a reasonable and timely manner, and to consider means by which we can stimulate the further deployment of access to advanced services.<sup>476</sup>

## I. Interstate Access Universal Service Support for Rate-of-Return Carriers

### 1. Background

202. The Rural Task Force recommended a number of principles for the Commission to apply in addressing the issue of implicit support for high loop costs within the interstate access rates of rate-of-return carriers (typically rural carriers).<sup>477</sup> The Commission has taken various measures to reform the access rate structure of price cap carriers.<sup>478</sup> According to the Rural Task Force, rate disparity between

---

<sup>472</sup> *First Report and Order*, 12 FCC Rcd at 8939 para. 300.

<sup>473</sup> *Id.* Of course, carriers who make such investments using universal service support also must comply with the mandate that support be used “only for the provision, maintenance, and upgrading of facilities and services for which the support is intended.” 47 U.S.C. § 254(e).

<sup>474</sup> *See* Rural Task Force Recommendation at 22-23. *See also Second 706 Report*, 15 FCC Rcd at 21004 para. 247 (“Because the development of the advanced services market remains in a very early stage, . . . we believe that there is time for us to examine further the factors that affect infrastructure investment and develop policies that will ensure access to needed services, but that are not inappropriately linked to universal service mechanisms for voice telephony”). We note that the Rural Utilities Service makes funding for rural carriers contingent on their use of the funds to deploy plant capable of providing access to advanced services. *See* 7 C.F.R. §§ 1751.100-1751.106. No commenter addressed the Rural Utilities Service’s standards or whether they would comport with federal high-cost universal service mechanisms.

<sup>475</sup> *See* Maine and Vermont Commissions Comments at 4 (“According to the Rural Policy Research Institute, for every rural customer served by a ‘rural telephone company,’ there are four rural customers served by a non[-]rural company”).

<sup>476</sup> *See Second 706 Report*, 15 FCC Rcd at 21003-14 paras. 244-268.

<sup>477</sup> Rural Task Force Recommendation at 31-32. Although most rate-of-return carriers are rural carriers, whether a carrier is subject to price cap regulation does not turn on whether it meets the definition of rural telephone company. *See generally Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation*, CC Docket No. 98-77, Notice of Proposed Rulemaking, 13 FCC Rcd 14238 (1998); *see also supra* n.3.

<sup>478</sup> *See Interstate Access Support Order*, 15 FCC Rcd at 12962.

price cap and rate-of-return carriers results from both access rate structure differences and cost differences, and may create significant pressures on interexchange carriers to geographically deaverage toll rates, contrary to the requirements of section 254(g) of the Act.<sup>479</sup> To reform the access rate structure of rate-of-return carriers, the Rural Task Force recommended that the Commission determine the amount of implicit support within their access rates by calculating the difference between their current access rates and “the appropriate unit prices of interstate access[,]” and then replacing this amount with a new, uncapped support mechanism.<sup>480</sup> The purpose of the new interstate access support mechanism would be similar to that of the mechanism adopted in the *Interstate Access Support Order* for price cap carriers.<sup>481</sup>

203. The Rural Task Force did not recommend a specific method for determining the “appropriate unit prices of interstate access.” The Rural Task Force further recommended, among other things, that the new support mechanism be funded by collections from all providers of interstate telecommunications services, that support be subject to geographic deaveraging and targeted to high-cost areas, and that support be portable and available to all eligible telecommunications carriers on an equitable, non-discriminatory, and competitively neutral basis.

204. The Joint Board concurred with the Rural Task Force that the Commission should consider creating an explicit universal service support mechanism to replace support that may be implicit within the access rates of rate-of-return carriers, but acknowledged that access charge issues “are interstate in nature and, therefore, are properly before the Commission.”<sup>482</sup> The Joint Board stated, however, that the MAG plan now before the Commission “raises issues beyond interstate access reform, and proposes universal service policy and procedural changes, including rate comparability under section 254(b)(3) and the overall size of the universal service mechanisms.”<sup>483</sup> It therefore encouraged the Commission “to ensure the Joint Board remains actively involved in review of those aspects of the MAG plan that relate to universal service.”<sup>484</sup>

## 2. Discussion

205. We find the Rural Task Force’s recommended principles for access reform to be reasonable and generally consistent with prior Commission actions to reform the access rate structure of price cap carriers. More specifically, these principles are generally consistent with our prior actions to identify implicit support in interstate access charges and to replace such implicit support with explicit universal service support available to all eligible telecommunications carriers on an equitable, non-discriminatory, and competitively neutral basis.<sup>485</sup> As the Joint Board recognized, the Commission currently is considering access reform issues in a separate proceeding concerning the MAG plan.<sup>486</sup> We

<sup>479</sup> 47 U.S.C. § 254(g).

<sup>480</sup> Rural Task Force Recommendation at 31.

<sup>481</sup> See *Interstate Access Support Order*, 15 FCC Rcd at 13043-44 paras. 195-97.

<sup>482</sup> *Recommended Decision* at 10 para. 20.

<sup>483</sup> *Id.* As stated above, the MAG plan is an interstate access reform and universal service support proposal for rate-of-return carriers. See *supra* n.1.

<sup>484</sup> *Id.* The Joint Board further stated that “[a] significant number of Joint Board members urge that this involvement include a referral to the Joint Board of the universal service issues raised by the MAG plan.” *Id.*; see *id.* at Concurring Statement of Commissioner Laska Schoenfelder and Statement of Public Counsel Martha Hogery Concurring in Part and Dissenting in Part.

<sup>485</sup> See *supra* n.478.

<sup>486</sup> The MAG plan includes a proposal similar in some respects to the Rural Task Force recommendation to replace support that may be implicit within the access rate structure of rate-of-return carriers with a new, explicit support mechanism. See *MAG NPRM*, 16 FCC Rcd at 463 para. 8, 466 para. 18.

recognize the importance of completing access reform for rate-of-return carriers, and intend to act expeditiously to resolve issues raised in the MAG proceeding.<sup>487</sup> Our consideration of these issues in the MAG proceeding will be informed by the Rural Task Force's recommended principles, which we will incorporate into that docket, as well as by the comments filed in this proceeding and the MAG proceeding concerning those principles.<sup>488</sup> As we stated previously in the *MAG NPRM*, we intend to keep the Joint Board actively involved in review of those aspects of the MAG plan that relate to universal service.<sup>489</sup>

206. We reject AT&T's argument that "[t]he Commission must immediately address access reform for rural carriers as part of the [Rural Task Force] plan."<sup>490</sup> In contrast to the Rural Task Force's specific recommendations regarding reform of high-cost loop support under Part 36 of the Commission's rules, its recommendations regarding access reform consisted of general principles, which it recognized do not resolve fundamental questions that remain controversial.<sup>491</sup> We agree with NRTA, OPASTCO, USTA, and others that "[a]ccess charge reform issues would be more appropriately addressed in the MAG Plan proceeding[.]"<sup>492</sup> Likewise, we reject suggestions that we defer action on the Rural Task Force plan.<sup>493</sup> As discussed above, the Rural Task Force plan represents a consensus of competing views developed over the course of several years and endorsed by a Joint Board Recommended Decision. The MAG plan was first submitted to the Commission on October 20, 2000, and requires further consideration to resolve issues raised by commenters.<sup>494</sup> Accordingly, although we are considering the issues raised in both proceedings simultaneously, we conclude that the MAG plan's pendency before the Commission does not warrant delay in implementation of the Rural Task Force plan.<sup>495</sup>

---

<sup>487</sup> We recognize that the Fifth Circuit recently held that, pursuant to section 254(e) of the Act, the Commission cannot permit carriers to recover their universal service contributions through access charges imposed on interexchange carriers. We intend to address this matter expeditiously. *See Comsat Corp., et al. v. FCC*, No. 00-60044 (5<sup>th</sup> Cir. May 3, 2001); *see also* AT&T comments at 10-11.

<sup>488</sup> *See* Ad Hoc Telecommunications User Committee Comments at 26-27; Arizona LEC Assn. Comments at 3; AT&T Comments at 4-11; California Commission Comments at 3, 7; CUSC Comments at App. A 25-26; Evans Tel. Co., et.al. Comments at 8; General Communications, Inc. Comments at 2-3; John Staurulaukis, Inc. Comments at 17-18; Texas Commission Comments at 8; WorldCom Comments at 4.

<sup>489</sup> *See MAG NPRM*, 16 FCC Rcd at 466 para. 18 ("we intend to work closely with the Joint Board on those aspects of the MAG proposal related to interstate access universal service support"); *see also id.* at 462 para. 4.

<sup>490</sup> AT&T Comments at 8; *see* General Communications, Inc. Comments at 2-3; AT&T Reply Comments at 2-6; WorldCom Reply Comments at 13-14.

<sup>491</sup> Rural Task Force Recommendation at 31 ("there is no agreement on how much or how to determine the amount of implicit support"); *compare* AT&T Comments at 8-10 ("AT&T suggests that the Commission follow the CALLS model for rural carriers") *with* CUSC Comments at App. A 25-26 (Rural Task Force's recommended approach, "like the CALLS plan, makes the unfounded assumption that all residual access revenues not recovered through the rebalanced access charges constitute appropriate universal service subsidies.").

<sup>492</sup> NRTA, OPASTCO, & USTA Comments at 3; *see* NTCA Comments at 20.

<sup>493</sup> *See* NRTA, OPASTCO, & USTA Comments at 2-3; Fred Williamson & Assoc. Comments at 2; *see also* TDS Comments in CC Docket No. 00-256.

<sup>494</sup> *See, e.g.,* Alaska Commission Comments in CC Docket No. 00-256 at 2 ("Unlike the CALLS plan, the MAG's access charge reform proposals have not been tempered by industry consensus. Development of an industry consensus would likely result in changes that we believe are needed before the plan is approved."); WorldCom Comments at 2 ("the MAG plan's strengths are outweighed by obvious weaknesses. The Commission should not adopt the MAG plan in its current form").

<sup>495</sup> Wyoming Commission Comments at 1 (urging the Commission not to allow "any unresolved access reform issues to stand in the way of timely and necessary federal universal service reform."); *see* Alaska Commission Comments in CC Docket No. 00-256 at 2 ("we would not like to see approval of the RTF delayed while the considerable additional issues in the MAG Plan are debated.").

## V. FURTHER NOTICE OF PROPOSED RULEMAKING

### A. Background

207. As discussed in greater detail in the attached Order,<sup>496</sup> we decline at this time to adopt the Rural Task Force's proposal to freeze high-cost loop support on a per-line basis in rural carrier study areas where a competitive eligible telecommunications carrier initiates service. The purpose of the proposal was to prevent excessive growth in the universal service fund as a result of the entrance of competitive eligible telecommunications carriers in rural carrier study areas over the life of the five-year plan we adopt here. As discussed above in section IV.C.3, support provided to competitive eligible telecommunications carriers is not subject to the overall cap on the high-cost loop fund. During the five-year period, excessive growth in the fund is thus possible if incumbent carriers lose many lines to competitive eligible telecommunications carriers, or if competitive eligible telecommunications carriers add a significant number of lines. The first scenario raises particular fund growth concerns because as an incumbent "loses" lines to a competitive eligible telecommunications carrier, the incumbent must recover its fixed costs from fewer lines, thus increasing its per-line costs. With higher per-line costs, the incumbent would receive greater per-line support, which would also be available to the competitive eligible telecommunications carrier for each of the lines that it serves. Thus, a substantial loss of an incumbent's lines to a competitive eligible telecommunications carrier could result in excessive fund growth.

208. We base our decision not to adopt the Rural Task Force's proposal at this time on several concerns. First, the proposal may be of limited benefit in serving its intended purpose and may, in some instances, contribute to fund growth by freezing support at higher levels than would be warranted in the future. Second, the likelihood of a competitive eligible telecommunications carrier capturing a substantial percentage of lines from the incumbent during the five-year period is speculative. Third, the indexed cap on the high-cost loop fund will operate as a check on excessive fund growth to a certain extent. Fourth, we are concerned that the proposal may have the unintended consequence of discouraging efficient investment in rural infrastructure. Fifth, the proposal may hinder the competitive entry in rural study areas by creating an additional incentive for incumbents to oppose the designation of eligible telecommunications carriers in rural study areas. Finally, we are concerned that the proposal would require complex and administratively burdensome regulations to implement.

### B. Issues for Comment

209. Although we decline, at this time, to adopt the Rural Task Force's proposal to freeze per-line support in rural carrier study areas in which a competitive eligible telecommunications carrier is providing service, we recognize that excessive fund growth may occur during this five-year plan. We note that the indexed cap on high-cost loop support would not check this growth fully, because support received by competitive carriers currently is not included within the cap. To develop the record on this issue more fully, we invite interested parties to propose possible alternative measures that may be appropriate to address this issue. We also invite commenters to address the likelihood that such measures may be necessary to prevent excessive fund growth during the five-year period.

210. One possible approach suggested by commenters would be to freeze support only when a competitive carrier serves a specific percentage of the total lines within a study area.<sup>497</sup> Under this approach, the Commission would adopt a threshold percentage of lines lost for triggering the freeze. As discussed above, however, a simple threshold requirement would fail to target study areas where the excessive fund growth is most likely to occur, because it could not distinguish captured from new

---

<sup>496</sup> See *supra* discussion at section IV.B.3.

<sup>497</sup> See *supra* n.325.

subscriber lines.<sup>498</sup> With regard to any proposal to freeze support, commenters should address whether support should be frozen for the study area, the competitor's service area, or the incumbent's specific disaggregation zone. We also invite commenters to propose other alternatives. Commenters should address the administrative feasibility of any such proposals, and whether they are consistent with the principles of encouraging investment in rural infrastructure and promoting competitive entry.<sup>499</sup>

211. Although we are not convinced of the likelihood of excessive fund growth due to competitive entry in high-cost areas during the life of this five-year plan, we intend to resolve the issues raised in this Further Notice expeditiously after we have developed the record more fully. In the meantime, as discussed above, we intend to closely monitor the impact of competitive entry in rural carrier study areas to ensure that excessive fund growth does not occur, consistent with our obligation in section 254 to maintain a specific, predictable, and sufficient universal service fund.<sup>500</sup>

## VI. PROCEDURAL MATTERS

### A. Final Regulatory Flexibility Analysis

212. As required by the Regulatory Flexibility Act (RFA),<sup>501</sup> an Initial Regulatory Flexibility Analysis (IRFA) was incorporated in the *Further Notice*.<sup>502</sup> The Commission sought written public comment on the proposals in the *Further Notice*, including comment on the IRFA. This present Final Regulatory Flexibility Analysis (FRFA) conforms to the RFA.<sup>503</sup>

#### 1. Need for, and Objectives of, the Order

213. The 1996 Act requires the Commission to consult with the Joint Board in implementing section 254, which establishes a number of principles for the preservation and advancement of universal service in a competitive telecommunications environment.<sup>504</sup> The Commission initiated this proceeding to consider the Recommended Decision of the Joint Board regarding a rural universal service plan developed by the Rural Task Force. In this Order, consistent with the recommendation of the Joint Board, we adopt interim rules for determining high-cost universal service support for rural telephone companies based upon the modified embedded cost mechanism proposed by the Rural Task Force. These rules should benefit all rural carriers because they will result in predictable levels of support so that rural carriers can continue to provide affordable service in rural America, while ensuring that consumers in all regions of the Nation, including rural areas, have access to affordable and quality telecommunications services.

214. In this Order, we take the following actions in response to the Rural Task Force's recommended reforms to the rural high-cost loop support mechanism and the proposals made by the MAG relating to these rules. First, we adopt the Rural Task Force's recommendation to re-base the high-cost loop support fund for rural telephone companies and retain an indexed cap on the fund. Second, we

---

<sup>498</sup> See *supra* para. 130; Rural Task Force *White Paper 5* at 17 ("Dealing with 'captured' and 'new' lines may create administrative problems and the need to track customers from one [carrier] to another").

<sup>499</sup> See *supra* paras. 128-130.

<sup>500</sup> 47 U.S.C. § 254(b)(5); see *supra* at para. 130.

<sup>501</sup> See 5 U.S.C. § 603. The RFA, see 5 U.S.C. § 601 *et seq.*, has been amended by the Contract with America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) (CWAAA). Title II of the CWAAA is the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA).

<sup>502</sup> *Further Notice* at 3-9.

<sup>503</sup> See 5 U.S.C. § 604.

<sup>504</sup> 47 U.S.C. § 254.

adopt a rural growth factor that allows growth in the high-cost loop support fund based on the annual increases in the Gross Domestic Product-Chained Price Index (GDP-CPI) and growth in the total number of working loops of rural carriers. Third, we adopt a modified version of the Rural Task Force's proposal as it relates to corporate operations expense. We revise the corporate operations expense limitation calculation so that the dollar values in the formula are re-based and indexed by the GDP-CPI. We also raise the minimum cap for those carriers with 6,000 or fewer loops. In the revised corporate operations expense formula, we allow these carriers to receive support for corporate operations expenses of up to \$600,000 or amounts derived from the revised corporate operations expense formula, whichever is greater. Fourth, we adopt a modified version of the Rural Task Force's proposed safety net additive so that if certain criteria are met, a carrier may receive support for its incremental expense adjustment associated with new investment. Fifth, while we retain section 54.305 of the Commission's rules which provides that a carrier acquiring exchanges from an unaffiliated carrier shall receive the same per-line levels of high-cost support for which the acquired exchanges were eligible prior to their transfer, we also modify the rule to provide safety valve support for additional investment made in the acquired exchanges. Sixth, we adopt, with certain modifications, the three paths for the disaggregation and targeting of high-cost universal service support proposed by the Rural Task Force. We also adopt the general requirements that the Rural Task Force proposed for all disaggregation plans. Seventh, we adopt the Rural Task Force's proposed framework, with the above noted modifications, and it shall remain in place for five years. Finally, we conclude that states should file annual certifications with the Commission to ensure that rural carriers and competitive eligible telecommunications carriers providing service in the service area of a rural local exchange carrier use universal service support "only for the provision, maintenance and upgrading of facilities and services for which the support is intended" consistent with section 254(e) of the Act.

215. In this Order, the Commission also addresses certain issues raised in the MAG proceeding. Specifically, we find that the MAG proposal to remove the indexed cap entirely and to eliminate the limits on corporate operations expenses is unwarranted. We also decide against the MAG proposal to the extent that it recommends elimination of section 54.305 entirely. Finally, we disagree with the MAG proposal to allow rural carriers to disaggregate universal service support up to three zones per wire center. We find the Rural Task Force's recommended principles for access reform to be reasonable and generally consistent with prior Commission actions to reform the access rate structure of price cap carriers. These principles will aid our consideration of access charge reform issues in the pending MAG proceeding.

216. We find that the interim rules strike a fair and reasonable balance among the principles and goals enumerated in section 254 of the Communications Act of 1934, as amended by the Telecommunications Act of 1996. Specifically, as the Commission continues to develop a long-term coordinated universal service plan, this interim plan will provide predictable levels of support so that rural carriers can make prudent investments in rural America.

## **2. Summary of Significant Issues Raised by Public Comments In Response to the IRFA**

217. No comments were submitted in response to the IRFA, nor did commenters address the potential impact of these interim rules on small business. The Commission, however, did consider the burden that certain provisions contained in the Order may have on smaller carriers and sought to minimize that burden. For example, as the Commission states in this Order, to reduce the need for small carriers to seek a waiver under the corporate operations expense rules,<sup>505</sup> we raise the minimum cap on allowable corporate operations expenses supported by universal service to \$600,000 or amounts derived from the

---

<sup>505</sup> 47 C.F.R. § 36.621(a)(4).

revised corporate operations expense formulas, whichever is greater.<sup>506</sup> This eliminates the burden and expense associated with the waiver process for those carriers.

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

218. The RFA directs agencies to provide a description of, and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules adopted herein.<sup>507</sup> The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."<sup>508</sup> In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.<sup>509</sup> Under the Small Business Act, a "small business concern" is one that: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) meets any additional criteria established by the Small Business Administration (SBA).<sup>510</sup>

219. We have included small incumbent local exchange carriers in this RFA analysis. As noted above, a "small business" under the RFA is one that, *inter alia*, meets the pertinent small business size standard (*e.g.*, a telephone communications business having 1,500 or fewer employees), and "is not dominant in its field of operation."<sup>511</sup> The SBA's Office of Advocacy contends that, for RFA purposes, small incumbent local exchange carriers are not dominant in their field of operation because any such dominance is not "national" in scope.<sup>512</sup> We have therefore included small incumbent carriers in this RFA analysis, although we emphasize that this RFA action has no effect on the Commission's analyses and determinations in other, non-RFA contexts.

220. *Local Exchange Carriers.* Neither the Commission nor the SBA has developed a definition for small providers of local exchange services. The closest applicable definition under the SBA rules is for telephone communications companies other than radiotelephone (wireless) companies.<sup>513</sup> According to the most recent *Trends in Telephone Service* report, 1,335 incumbent carriers reported that

---

<sup>506</sup> See *supra* at para. 75.

<sup>507</sup> 5 U.S.C. § 603(b)(3).

<sup>508</sup> 5 U.S.C. § 601(6).

<sup>509</sup> 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 15 U.S.C. § 632). Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition in the Federal Register."

<sup>510</sup> 15 U.S.C. § 632.

<sup>511</sup> 5 U.S.C. § 601(3).

<sup>512</sup> See Letter from Jere W. Glover, Chief Counsel for Advocacy, SBA, to William E. Kennard, Chairman, FCC, dated May 27, 1999. The Small Business Act contains a definition of "small business concern," which the RFA incorporates into its own definition of "small business." See U.S.C. § 632(a) (Small Business Act); 5 U.S.C. § 601(3) (RFA). SBA regulations interpret "small business concern" to include the concept of dominance on a national basis. 13 C.F.R. § 121.102(b). Since 1996, out of an abundance of caution, the Commission has included small incumbent LECs in its regulatory flexibility analyses. See, *e.g.*, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket, 96-98, First Report and Order, 11 FCC Rcd 15499, 16144-45 (1996).

<sup>513</sup> 13 C.F.R. § 121.201, SIC Code 4813.

they were engaged in the provision of local exchange services.<sup>514</sup> We do not have data specifying the number of these carriers that are either dominant in their field of operations, are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of local exchange carriers that would qualify as small business concerns under the SBA's definition. Of the 1,335 incumbent carriers, 13 entities are price cap carriers that are not subject to these rules. Consequently, we estimate that fewer than 1,322 providers of local exchange service are small entities or small incumbent local exchange carriers that may be affected.

221. *Competitive Access Providers.* Neither the Commission nor the SBA has developed a definition of small entities specifically applicable to competitive access services providers (CAPs). The closest applicable definition under the SBA rules is for telephone communications companies other than radiotelephone (wireless) companies.<sup>515</sup> According to the most recent *Trends in Telephone Service* data, 349 CAPs/competitive local exchange carriers and 60 other local exchange carriers reported that they were engaged in the provision of competitive local exchange services.<sup>516</sup> We do not have data specifying the number of these carriers that are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of CAPs that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are less than 349 small entity CAPs and 60 other local exchange carriers that may be affected.

222. *Cellular Licensees.* Neither the Commission nor the SBA has developed a definition of small entities applicable to cellular licensees. Therefore, the applicable definition of small entity is the definition under the SBA rules applicable to radiotelephone (wireless) companies. This provides that a small entity is a radiotelephone company employing no more than 1,500 persons.<sup>517</sup> According to the Bureau of the Census, only twelve radiotelephone firms from a total of 1,178 such firms which operated during 1992 had 1,000 or more employees.<sup>518</sup> Therefore, even if all twelve of these firms were cellular telephone companies, nearly all cellular carriers were small businesses under the SBA's definition. In addition, we note that there are 1,758 cellular licenses; however, a cellular licensee may own several licenses. In addition, according to the most recent *Trends Report* data, 806 carriers reported that they were engaged in the provision of either cellular service or Personal Communications Service (PCS) services, which are placed together in the data.<sup>519</sup> We do not have data specifying the number of these carriers that are not independently owned and operated or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of cellular service carriers that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are fewer than 808 small cellular service carriers that may be affected.

223. *Broadband Personal Communications Service (PCS).* The broadband PCS spectrum is divided into six frequency blocks designated A through F, and the Commission has held auctions for each block. The Commission defined "small entity" for Blocks C and F as an entity that has average gross revenues of less than \$40 million in the three previous calendar years.<sup>520</sup> For Block F, an additional

---

<sup>514</sup> FCC, Common Carrier Bureau, Industry Analysis Division, *Trends in Telephone Service*, Table 16.3 (Dec. 2000) (*Trends Report*).

<sup>515</sup> 13 C.F.R. § 121.201, SIC code 4813.

<sup>516</sup> *Trends Report*, Table 16.3.

<sup>517</sup> 13 C.F.R. § 121.201, SIC code 4812.

<sup>518</sup> *1992 Census, Series UC92-S-1*, at Table 5, SIC code 4812.

<sup>519</sup> *Trends Report*, Table 16.3.

<sup>520</sup> See *Amendment of Parts 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, FCC 96-278, paras. 57-60 (rel. Jun. 24, 1996), 61 Fed. Reg. 33859 (Jul. 1, 1996); see also 47 C.F.R. § 24.720(b).

classification for "very small business" was added and is defined as an entity that, together with their affiliates, has average gross revenues of not more than \$15 million for the preceding three calendar years.<sup>521</sup> These regulations defining "small entity" in the context of broadband PCS auctions have been approved by the SBA.<sup>522</sup> No small businesses within the SBA-approved definition bid successfully for licenses in Blocks A and B. There were 90 winning bidders that qualified as small entities in the Block C auctions. A total of 93 small and very small business bidders won approximately 40 percent of the 1,479 licenses for Blocks D, E, and F.<sup>523</sup> Based on this information, we conclude that the number of small broadband PCS licensees will include the 90 winning C Block bidders and the 93 qualifying bidders in the D, E, and F blocks, for a total of 183 small entity PCS providers as defined by the SBA and the Commission's auction rules.

224. *Rural Radiotelephone Service.* The Commission has not adopted a definition of small entity specific to the Rural Radiotelephone Service.<sup>524</sup> A significant subset of the Rural Radiotelephone Service is the Basic Exchange Telephone Radio Systems (BETRS).<sup>525</sup> We will use the SBA's definition applicable to radiotelephone companies, *i.e.*, an entity employing no more than 1,500 persons.<sup>526</sup> There are approximately 1,000 licensees in the Rural Radiotelephone Service, and we estimate that almost all of them qualify as small entities under the SBA's definition.

225. *Specialized Mobile Radio (SMR).* The Commission awards bidding credits in auctions for geographic area 800 MHz and 900 MHz SMR licenses to firms that had revenues of no more than \$15 million in each of the three previous calendar years.<sup>527</sup> In the context of both the 800 MHz and 900 MHz SMR, a definition of "small entity" has been approved by the SBA.

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

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

228. *Fixed Microwave Services.* Microwave services include common carrier,<sup>528</sup> private-operational fixed,<sup>529</sup> and broadcast auxiliary radio services.<sup>530</sup> At present, there are approximately

---

<sup>521</sup> See *Amendment of Parts 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, FCC 96-278, para. 60 (1996), 61 Fed. Reg. 33859 (Jul. 1, 1996).

<sup>522</sup> See, *e.g.*, *Implementation of Section 309(j) of the Communications Act -- Competitive Bidding*, PP Docket No. 93-253, Fifth Report and Order, 9 FCC Rcd 5532, 5581-84 paras. 115-117 (1994).

<sup>523</sup> FCC News, *Broadband PCS, D, E and F Block Auction Closes*, No. 71744 (rel. Jan. 14, 1997).

<sup>524</sup> The service is defined in section 22.99 of the Commission's Rules. 47 C.F.R. § 22.99.

<sup>525</sup> BETRS is defined in sections 22.757 and 22.759 of the Commission's Rules. 47 C.F.R. §§ 22.757, 22.759.

<sup>526</sup> 13 C.F.R. § 121.201, SIC code 4812.

<sup>527</sup> 47 C.F.R. § 90.814(b)(1).

<sup>528</sup> 47 C.F.R. §§ 101, *et seq.* (formerly Part 21 of the Commission's Rules).

<sup>529</sup> Persons eligible under Parts 80 and 90 of the Commission's rules can use Private Operational-Fixed Microwave services. See 47 C.F.R. Parts 80, 90. Stations in this service are called operational-fixed to distinguish them from (continued....)

22,015 common carrier fixed licensees and 61,670 private operational-fixed licensees and broadcast auxiliary radio licensees in the microwave services. The Commission has not yet defined a small business with respect to microwave services. For purposes of this FRFA, we utilize the SBA's definition applicable to radiotelephone companies -- *i.e.*, an entity with no more than 1,500 persons.<sup>531</sup> We estimate, for this purpose, that all of the Fixed Microwave licensees (excluding broadcast auxiliary licensees) would qualify as small entities under the SBA definition for radiotelephone companies.

229. *39 GHz Licensees.* Neither the Commission nor the SBA has developed a definition of small entities applicable to 39 GHz licensees. Therefore, the applicable definition of small entity is the definition under the SBA rules applicable to radiotelephone (wireless) companies. This provides that a small entity is a radiotelephone company employing no more than 1,500 persons.<sup>532</sup> For purposes of the 39 GHz license auction, the Commission defined "small entity" as an entity that has average gross revenues of less than \$40 million in the three previous calendar years, and "very small entity" as an entity that has average gross revenues of not more than \$15 million for the preceding three calendar years. The Commission has granted licenses to 29 service providers in the 39 GHz service. We do not have data specifying the number of these carriers that are not independently owned and operated or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of 39 GHz licensees that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are no more than 29 39 GHz small business providers that may be affected.

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

230. In the Order, we adopt the Rural Task Force's proposal that rural carriers be given a choice of three different options for disaggregating and targeting per-line universal service high-cost support, including high-cost loop support, Long Term Support (LTS), and Local Switching Support (LSS). Rural carriers are required to choose one of the paths detailed below within 270 days of the effective date of the new rules through submission to the state commissions. Rural carriers not subject to the jurisdiction of the state are required to make such submissions to the Commission. Rural carriers that elect to disaggregate and target per-line support under either Path Two or Three are required to report loops at the cost-zone level, which is a modification of the current requirement that carriers report loops at the study-area level. This change will require only minor increases in a carrier's reporting burdens, and predominantly only in the first year that the carrier revises its method of reporting. Path 1 is available to rural carriers that do not want to target high-cost support. Path Two is available to rural carriers that want state commission review and approval of a disaggregation plan. Path Three is available to rural carriers interested in self-certifying a method for disaggregating universal service support into a maximum of two cost zones per wire center.<sup>533</sup> Only a disaggregation plan filed under Path Three requires additional

(Continued from previous page) \_\_\_\_\_  
common carrier and public fixed stations. Only the licensee may use the operational-fixed station, and only for communications related to the licensee's commercial, industrial, or safety operations.

<sup>530</sup> Auxiliary Microwave Service is governed by Part 74 of the Commission's rules. *See* 47 C.F.R. Part 74. Available to licensees of broadcast stations and to broadcast and cable network entities, broadcast auxiliary microwave stations are used for relaying broadcast television signals from the studio to the transmitter, or between two points such as a main studio and an auxiliary studio. The service also includes mobile TV pickups, which relay signals from a remote location back to the studio.

<sup>531</sup> 13 C.F.R. § 121.201, SIC code 4812.

<sup>532</sup> 13 C.F.R. § 121.201, SIC code 4812.

<sup>533</sup> Alternatively, the self-certified plan may comply with a prior regulatory determination that a different level of disaggregation is appropriate. Under the Rural Task Force's proposal, rural carriers also may disaggregate and target per-line support to cost zones within wire centers. In this Order, we deny the MAG's proposal to allow rural carriers to disaggregate support to up to three zones.

reporting requirements to the Commission. Under Path Three, a carrier must use a rationale that is reasonably related to the cost of providing service for each cost zone within each disaggregation category (high-cost loop support, LSS, and LTS). We estimate that the annual burden hours in the first year would be 60 hours. We estimate subsequent annual burden hours at 8 hours. We believe the burden associated with this reporting requirement is appropriately balanced with the benefits reporting rural carriers will receive.

231. The Commission also adopted the Rural Task Force's proposal to extend the section 254(e) certification process to rural carriers.<sup>534</sup> Under this process, state regulatory commissions provide the Commission with annual certifications indicating that the rural carriers in their states receiving federal universal service support will use the support "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended."<sup>535</sup> Carriers not subject to the jurisdiction of the state must submit a sworn affidavit to the Commission stating that they will use support "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended." This reporting requirement will provide states and carriers with access to federal universal service support in a way that ensures the integrity of the universal service fund. We estimate that the annual burden hours associated with the section 254(e) certification process would be 12 hours per carrier. This is a nominal burden on rural carriers and is balanced against the high degree of federal universal service benefits rural carriers would receive.

232. Finally, the Commission adopted a modification to an existing reporting requirement regarding working loops. Under the current rules, rural carriers are required to submit, on an annual basis, the number of working loops it has for each study area it serves.<sup>536</sup> In this Order, we modify this reporting requirement to require that once a competitor enters a rural carriers study area, working loops are required to be reported on a quarterly basis.<sup>537</sup> The Commission determined that this was necessary to prevent the overpayment of support to incumbent rural carriers, which occurs under the current rule because competitors have an incentive to update quarterly, while the incumbent has an incentive to only update annually.<sup>538</sup>

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

233. The RFA requires an agency to describe any significant alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance, rather than design, standards; and (4) an exemption from coverage of the rule, or any part thereof, for small entities.<sup>539</sup>

234. The Order adopted herein is the result of an analysis of a number of options for distributing federal universal service support to rural carriers. Throughout the Order, it is evident that the

---

<sup>534</sup> 47 U.S.C. § 254(e).

<sup>535</sup> *Id.* In jurisdictions where carriers are not subject to the jurisdiction of a state commission or other state regulatory authority, the carrier is required to self-certify that it will use the support "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended." 47 U.S.C. § 254(e).

<sup>536</sup> 47 C.F.R. §§ 36.612, 54.307.

<sup>537</sup> *See supra* paras. 133-134.

<sup>538</sup> *Id.*

<sup>539</sup> 5 U.S.C. § 603(c).

Commission took great strides in balancing the burdens associated with modification of the existing embedded cost mechanism and the benefits these modifications confer on rural carriers and competitive eligible telecommunications carriers. In this regard, it is important to note that we make these modifications with only minimal reporting requirements.

235. Among the significant alternatives, we considered whether modification of the corporate operations expense cap would minimize the burden and expense associated with seeking a waiver for smaller carriers. In this Order, we decide to raise the existing cap for carriers with 6,000 or fewer working loops so they can receive support for up to \$600,000 or amounts derived from the revised corporate operations expense formula adopted herein, whichever is greater.<sup>540</sup> We thus decrease the need of smaller carriers to request a waiver. In addition, we adopt a modified version of the safety net additive mechanism proposed by the Rural Task Force. We conclude that a modification to the safety net additive is warranted because as proposed, the mechanism potentially allowed for the recovery of more than 100 percent of incremental costs.<sup>541</sup> We also consider alternative measurements of “meaningful investment” for purposes of calculating safety valve support. We conclude that the alternatives considered would, in some instances, deny the recovery of such meaningful investments.

236. **Report to Congress:** The Commission will send a copy of the Order, including this FRFA, in a report to be sent to Congress pursuant to the Congressional Review Act.<sup>542</sup> In addition, the Commission will send a copy of the Order, including the FRFA, to the Chief Counsel for Advocacy of the SBA. A copy of the Order and FRFA (or summaries thereof) will also be published in the Federal Register.<sup>543</sup>

## **B. Paperwork Reduction Act**

237. As required by the Paperwork Reduction Act of 1995, the *Further Notice* invited the general public and the Office of Management and Budget (OMB) to comment on the proposed modifications contained in the Notice. In this Report and Order, we adopt with certain modifications the proposals contained in the *Further Notice*.

238. As described above, the rules we adopt in this Order reflect our efforts to balance the needs of rural carriers, while minimizing the burden on those entities that must comply with our reporting requirements. The information we request should not require significant additional resources as they are a modification of current reporting requirements. Additionally, by freezing the national average loop cost at \$240, we eliminate the need for non-rural carriers to file loop cost data on a quarterly basis, thus alleviating those carriers of an administrative burden.<sup>544</sup>

239. The action contained herein has been analyzed with respect to the Paperwork Reduction Act of 1995 and found to impose new or modified reporting and recordkeeping requirements or burdens on the public. Implementation of these new or modified reporting and recordkeeping requirements will be subject to approval by the Office of Management and Budget (OMB) as prescribed by the Act, and will go into effect upon announcement in the Federal Register of OMB approval.

---

<sup>540</sup> See *supra* para. 74.

<sup>541</sup> See *supra* paras. 79-80.

<sup>542</sup> See 5 U.S.C. § 801(a)(1)(A).

<sup>543</sup> See 5 U.S.C. § 604(b).

<sup>544</sup> See *supra* para. 59.

### C. Effective Date of Final Rules

240. We conclude that the amendments to our rules adopted herein shall be effective upon publication in the Federal Register. The final rules must take effect prior to 30 days after their publication in the Federal Register in order for NECA to be able to implement the necessary changes to the high-cost loop support mechanism by July 1, 2001. Accordingly, pursuant to the Administrative Procedure Act, we find good cause to depart from the general requirement that final rules take effect not less than 30 days after their publication in the Federal Register.

### D. Initial Regulatory Flexibility Analysis

241. As required by the Regulatory Flexibility Act (RFA),<sup>545</sup> the Commission has prepared this Initial Regulatory Flexibility Analysis (IRFA) of the possible significant economic impact on small entities by the policies and rules proposed in this *Further Notice of Proposed Rulemaking*.<sup>546</sup> Written public comments are requested on this IRFA. Comments must be identified as responses to the IRFA and must be filed by the deadlines for comments on the Notice provided below in section G. The Commission will send a copy of the Notice, including this IRFA, to the Chief Counsel for Advocacy of the SBA.<sup>547</sup> In addition, the Notice and IRFA (or summaries thereof) will be published in the Federal Register.<sup>548</sup>

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

242. In the Order accompanying this *Further Notice of Proposed Rulemaking*, we modify the rural high-cost mechanism. While we declined to adopt the Rural Task Force's proposal to freeze per-line support in rural carrier study areas in which a competitive eligible telecommunications carrier is providing service, we recognized that excessive fund growth may occur during the five-year duration of the interim plan. We noted that the indexed cap on high-cost loop support would not check this growth fully, because support received by competitive carriers is not included within the cap.<sup>549</sup> To develop the record on this issue more fully, we issue this *Further Notice of Proposed Rulemaking* and invite interested parties to propose possible alternative measures that may be appropriate to address this issue.<sup>550</sup> We also invite commenters to address the likelihood that such measures may be necessary to prevent excessive fund growth during the five-year period.

243. Although we are not convinced of the likelihood of excessive fund growth due to competitive entry in high-cost areas during the life of this five-year plan, we intend to resolve the issues raised in this *Further Notice of Proposed Rulemaking* expeditiously after we have developed the record more fully.

#### 2. Legal Basis

244. The legal basis as proposed for this *Further Notice of Proposed Rulemaking* is contained in sections 4(i), 4(j), 201-205, 254, and 403 of the Communications Act of 1934 (as amended by

---

<sup>545</sup> See 5 U.S.C. § 603. The RFA, *see* 5 U.S.C. § 601 *et. seq.*, has been amended by the Contract with America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) (CWAAA). Title II of the CWAAA is the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA).

<sup>546</sup> *See generally supra* paras. 207-211.

<sup>547</sup> *See* 5 U.S.C. § 603(a).

<sup>548</sup> *See id.*

<sup>549</sup> *See supra* para. 125.

<sup>550</sup> *See supra* paras. 207-211.

the Telecommunications Act of 1996), 47 U.S.C. §§ 4(i), 4(j), 201-205, 254, 403.

### 3. Description and Estimate of Small Entities to Which Rules Will Apply

245. The RFA directs agencies to provide a description of, and, where feasible, an estimate of the number of small entities that may be affected by the proposed rules adopted herein.<sup>551</sup> The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."<sup>552</sup> In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.<sup>553</sup> Under the Small Business Act, a "small business concern" is one that: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) meets any additional criteria established by the Small Business Administration (SBA).<sup>554</sup>

246. We have included small incumbent local exchange carriers in this RFA analysis. As noted above, a "small business" under the RFA is one that, *inter alia*, meets the pertinent small business size standard (*e.g.*, a telephone communications business having 1,500 or fewer employees), and "is not dominant in its field of operation."<sup>555</sup> The SBA's Office of Advocacy contends that, for RFA purposes, small incumbent local exchange carriers are not dominant in their field of operation because any such dominance is not "national" in scope.<sup>556</sup> We have therefore included small incumbent carriers in this RFA analysis, although we emphasize that this RFA action has no effect on the Commission's analyses and determinations in other, non-RFA contexts.

247. *Local Exchange Carriers.* Neither the Commission nor the SBA has developed a definition for small providers of local exchange services. The closest applicable definition under the SBA rules is for telephone communications companies other than radiotelephone (wireless) companies.<sup>557</sup> According to the most recent *Trends Report* data, 1,335 incumbent carriers reported that they were engaged in the provision of local exchange services.<sup>558</sup> We do not have data specifying the number of these carriers that are either dominant in their field of operations, are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of local exchange carriers that would qualify as small business concerns under the

---

<sup>551</sup> 5 U.S.C. § 603(b)(3).

<sup>552</sup> 5 U.S.C. § 601(6).

<sup>553</sup> 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in 15 U.S.C. § 632). Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such term which are appropriate to the activities of the agency and publishes such definition in the Federal Register."

<sup>554</sup> 15 U.S.C. § 632.

<sup>555</sup> 5 U.S.C. § 601(3).

<sup>556</sup> See Letter from Jere W. Glover, Chief Counsel for Advocacy, SBA, to William E. Kennard, Chairman, FCC, dated May 27, 1999. The Small Business Act contains a definition of "small business concern," which the RFA incorporates into its own definition of "small business." See U.S.C. § 632(a) (Small Business Act); 5 U.S.C. § 601(3) (RFA). SBA regulations interpret "small business concern" to include the concept of dominance on a national basis. 13 C.F.R. § 121.102(b). Since 1996, out of an abundance of caution, the Commission has included small incumbent LECs in its regulatory flexibility analyses. See, *e.g.*, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket, 96-98, First Report and Order, 11 FCC Rcd 15499, 16144-45 (1996).

<sup>557</sup> 13 C.F.R. § 121.201, SIC Code 4813.

<sup>558</sup> *Trends Report*, Table 16.3.

SBA's definition. Of the 1,335 incumbent carriers, 13 entities are price cap carriers that are not subject to these rules. Consequently, we estimate that fewer than 1,322 providers of local exchange service are small entities or small incumbent local exchange carriers that may be affected.

248. *Competitive Access Providers.* Neither the Commission nor the SBA has developed a definition of small entities specifically applicable to competitive access services providers (CAPs). The closest applicable definition under the SBA rules is for telephone communications companies other than radiotelephone (wireless) companies.<sup>559</sup> According to the most recent *Trends Report* data, 349 CAPs/competitive local exchange carriers and 60 other local exchange carriers reported that they were engaged in the provision of competitive local exchange services.<sup>560</sup> We do not have data specifying the number of these carriers that are not independently owned and operated, or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of CAPs that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are less than 349 small entity CAPs and 60 other local exchange carriers that may be affected.

249. *Cellular Licensees.* Neither the Commission nor the SBA has developed a definition of small entities applicable to cellular licensees. Therefore, the applicable definition of small entity is the definition under the SBA rules applicable to radiotelephone (wireless) companies. This provides that a small entity is a radiotelephone company employing no more than 1,500 persons.<sup>561</sup> According to the Bureau of the Census, only twelve radiotelephone firms from a total of 1,178 such firms which operated during 1992 had 1,000 or more employees.<sup>562</sup> Therefore, even if all twelve of these firms were cellular telephone companies, nearly all cellular carriers were small businesses under the SBA's definition. In addition, we note that there are 1,758 cellular licenses; however, a cellular licensee may own several licenses. In addition, according to the most recent *Telecommunications Industry Revenue* data, 806 carriers reported that they were engaged in the provision of either cellular service or Personal Communications Service (PCS) services, which are placed together in the data.<sup>563</sup> We do not have data specifying the number of these carriers that are not independently owned and operated or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of cellular service carriers that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are fewer than 808 small cellular service carriers that may be affected.

250. *Broadband Personal Communications Service (PCS).* The broadband PCS spectrum is divided into six frequency blocks designated A through F, and the Commission has held auctions for each block. The Commission defined "small entity" for Blocks C and F as an entity that has average gross revenues of less than \$40 million in the three previous calendar years.<sup>564</sup> For Block F, an additional classification for "very small business" was added and is defined as an entity that, together with their affiliates, has average gross revenues of not more than \$15 million for the preceding three calendar years.<sup>565</sup> These regulations defining "small entity" in the context of broadband PCS auctions have been

---

<sup>559</sup> 13 C.F.R. § 121.201, SIC code 4813.

<sup>560</sup> *Trends Report*, Table 16.3.

<sup>561</sup> 13 C.F.R. § 121.201, SIC code 4812.

<sup>562</sup> *1992 Census, Series UC92-S-1*, at Table 5, SIC code 4812.

<sup>563</sup> *Trends Report*, Table 16.3.

<sup>564</sup> *See Amendment of Parts 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, FCC 96-278, paras. 57-60 (rel. Jun. 24, 1996), 61 Fed. Reg. 33859 (Jul. 1, 1996); *see also* 47 C.F.R. § 24.720(b).

<sup>565</sup> *See Amendment of Parts 20 and 24 of the Commission's Rules -- Broadband PCS Competitive Bidding and the Commercial Mobile Radio Service Spectrum Cap*, WT Docket No. 96-59, Report and Order, FCC 96-278, para. 60 (1996), 61 Fed. Reg. 33859 (Jul. 1, 1996).

approved by the SBA.<sup>566</sup> No small businesses within the SBA-approved definition bid successfully for licenses in Blocks A and B. There were 90 winning bidders that qualified as small entities in the Block C auctions. A total of 93 small and very small business bidders won approximately 40 percent of the 1,479 licenses for Blocks D, E, and F.<sup>567</sup> Based on this information, we conclude that the number of small broadband PCS licensees will include the 90 winning C Block bidders and the 93 qualifying bidders in the D, E, and F blocks, for a total of 183 small entity PCS providers as defined by the SBA and the Commission's auction rules.

251. *Rural Radiotelephone Service.* The Commission has not adopted a definition of small entity specific to the Rural Radiotelephone Service.<sup>568</sup> A significant subset of the Rural Radiotelephone Service is the Basic Exchange Telephone Radio Systems (BETRS).<sup>569</sup> We will use the SBA's definition applicable to radiotelephone companies, *i.e.*, an entity employing no more than 1,500 persons.<sup>570</sup> There are approximately 1,000 licensees in the Rural Radiotelephone Service, and we estimate that almost all of them qualify as small entities under the SBA's definition.

252. *Specialized Mobile Radio (SMR).* The Commission awards bidding credits in auctions for geographic area 800 MHz and 900 MHz SMR licenses to firms that had revenues of no more than \$15 million in each of the three previous calendar years.<sup>571</sup> In the context of both the 800 MHz and 900 MHz SMR, a definition of "small entity" has been approved by the SBA.

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

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

255. *Fixed Microwave Services.* Microwave services include common carrier,<sup>572</sup> private-operational fixed,<sup>573</sup> and broadcast auxiliary radio services.<sup>574</sup> At present, there are approximately

---

<sup>566</sup> See, e.g., *Implementation of Section 309(j) of the Communications Act -- Competitive Bidding*, PP Docket No. 93-253, Fifth Report and Order, 9 FCC Rcd 5532, 5581-84 paras. 115-117 (1994).

<sup>567</sup> FCC News, *Broadband PCS, D, E and F Block Auction Closes*, No. 71744 (rel. Jan. 14, 1997).

<sup>568</sup> The service is defined in section 22.99 of the Commission's Rules. 47 C.F.R. § 22.99.

<sup>569</sup> BETRS is defined in sections 22.757 and 22.759 of the Commission's Rules. 47 C.F.R. §§ 22.757, 22.759.

<sup>570</sup> 13 C.F.R. § 121.201, SIC code 4812.

<sup>571</sup> 47 C.F.R. § 90.814(b)(1).

<sup>572</sup> 47 C.F.R. §§ 101, *et seq.* (formerly Part 21 of the Commission's Rules).

<sup>573</sup> Persons eligible under Parts 80 and 90 of the Commission's rules can use Private Operational-Fixed Microwave services. See 47 C.F.R. §§ 80 and 90. Stations in this service are called operational-fixed to distinguish them from common carrier and public fixed stations. Only the licensee may use the operational-fixed station, and only for communications related to the licensee's commercial, industrial, or safety operations.

<sup>574</sup> Auxiliary Microwave Service is governed by Part 74 of the Commission's rules. See 47 C.F.R. § 74. Available to licensees of broadcast stations and to broadcast and cable network entities, broadcast auxiliary microwave stations are used for relaying broadcast television signals from the studio to the transmitter, or between two points (continued....)

22,015 common carrier fixed licensees and 61,670 private operational-fixed licensees and broadcast auxiliary radio licensees in the microwave services. The Commission has not yet defined a small business with respect to microwave services. For purposes of this IRFA, we utilize the SBA's definition applicable to radiotelephone companies -- *i.e.*, an entity with no more than 1,500 persons.<sup>575</sup> We estimate, for this purpose, that all of the Fixed Microwave licensees (excluding broadcast auxiliary licensees) would qualify as small entities under the SBA definition for radiotelephone companies.

256. *39 GHz Licensees.* Neither the Commission nor the SBA has developed a definition of small entities applicable to 39 GHz licensees. Therefore, the applicable definition of small entity is the definition under the SBA rules applicable to radiotelephone (wireless) companies. This provides that a small entity is a radiotelephone company employing no more than 1,500 persons.<sup>576</sup> For purposes of the 39 GHz license auction, the Commission defined "small entity" as an entity that has average gross revenues of less than \$40 million in the three previous calendar years, and "very small entity" as an entity that has average gross revenues of not more than \$15 million for the preceding three calendar years.. The Commission has granted licenses to 29 service providers in the 39 GHz service. We do not have data specifying the number of these carriers that are not independently owned and operated or have more than 1,500 employees, and thus are unable at this time to estimate with greater precision the number of 39 GHz licensees that would qualify as small business concerns under the SBA's definition. Consequently, we estimate that there are no more than 29 39 GHz small business providers that may be affected.

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

257. In the Order accompanying this *Further Notice of Proposed Rulemaking*, the Commission revised the reporting frequency of line count data in study areas where competitive entry has occurred. Prior to the Order's adoption, rural carriers were required to submit line count data annually.<sup>577</sup> The Commission determined that the more frequent reporting requirement was necessary to ensure that only one carrier receives support for each line served and to monitor the concerns expressed by the Rural Task Force with regard to the potential impact of competitive entry in rural carrier study areas.<sup>578</sup> The line count data submitted by carriers on a quarterly basis under the Order should be sufficient for the Commission to implement any change it may adopt pursuant to this *Further Notice of Proposed Rulemaking*; however, the issues of frequency of reporting and timing of submission may need to be revisited for implementation purposes.

#### **5. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered**

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

(Continued from previous page) \_\_\_\_\_

such as a main studio and an auxiliary studio. The service also includes mobile TV pickups, which relay signals from a remote location back to the studio.

<sup>575</sup> 13 C.F.R. § 121.201, SIC code 4812.

<sup>576</sup> *Id.*

<sup>577</sup> *See supra* para. 133.

<sup>578</sup> *Id.*

standards; and (4) an exemption from coverage of the rule, or any part thereof, for small entities.<sup>579</sup>

259. Here, we have declined at this time to freeze per-line support in rural carriers' study areas in which a competitive eligible telecommunications carrier is providing service. Had we adopted the alternative of the freeze, we would, we believe, have also needed to adopt, *e.g.*, complex and administratively burdensome implementing regulations. By seeking additional comments on this issue, including comment from small entities regarding significant alternatives, we hope to identify alternatives that would include simpler reporting or other compliance requirements. Thus, the *Further Notice of Proposed Rulemaking* under consideration herein seeks to determine possible alternative measures that may be appropriate to address the issue of excessive fund growth that may result from competitive entry in rural study areas.<sup>580</sup> We invite comment on how any alternatives proposed would be likely to affect small businesses.

#### **6. Federal Rules that May Duplicate, Overlap, or Conflict with the Proposed Rules.**

260. None.

#### **E. Initial Paperwork Reduction Act of 1995 Analysis**

261. This *Further Notice of Proposed Rulemaking* contains either a proposed or modified information collection. As part of a continuing effort to reduce paperwork burdens, we invite the general public and the Office of Management and Budget (OMB) to take this opportunity to comment on the information collections contained in this Notice, as required by the Paperwork Reduction Act of 1995, Public Law 104-13. Public and agency comments are due at the same time as other comments on this Notice; OMB comments are due 60 days from the date of publication of this Notice in the Federal Register. Comments should address: (a) whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information shall have practical utility; (b) the accuracy of the Commission's burden estimates; (c) ways to enhance the quality, utility, and clarity of the information collected; and (d) ways to minimize the burden of the collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

#### **F. Ex Parte**

262. This is a non-restricted notice and comment rulemaking proceeding. *Ex parte* presentations are permitted, except during the Sunshine Agenda period, provided they are disclosed as provided in the Commission's rules.<sup>581</sup>

#### **G. Comment Filing Procedures**

263. Pursuant to sections 1.415 and 1.419 of the Commission's rules, 47 C.F.R. §§ 1.415, 1.419, interested parties may file comments 30 days or fewer from publication in the Federal Register, and reply comments 60 days or fewer from publication in the Federal Register. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies.<sup>582</sup>

---

<sup>579</sup> 5 U.S.C. § 603(c).

<sup>580</sup> *See supra* paras. 209-211.

<sup>581</sup> *See generally* 47 C.F.R. §§ 1.1202, 1.1203, 1.1206(a).

<sup>582</sup> *See* Electronic Filing of Documents in Rulemaking Proceedings, 63 Fed. Reg. 24,121 (1998).

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

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

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

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

## VII. ORDERING CLAUSES

268. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 1-4, 201-205, 214, 218-220, 254, 303(r), 403, 405, and 410 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151-154, 201-205, 214, 218-220, 254, 303(r), 403, 405, and 410, this Fourteenth Report and Order and Twenty-Second Order on Reconsideration in CC Docket No. 96-45, and Report and Order in CC Docket No. 00-256 IS ADOPTED.

269. IT IS FURTHER ORDERED that Part 36 of the Commission's rules, 47 C.F.R. Part 36, IS AMENDED as set forth in Appendix A hereto, effective immediately upon publication in the Federal Register.

270. IT IS FURTHER ORDERED that Part 54 of the Commission's rules, 47 C.F.R. Part 54, IS AMENDED as set forth in Appendix A hereto, effective immediately upon publication in the Federal Register.

271. IT IS FURTHER ORDERED that the Commission's Consumer Information Bureau, Reference Information Center, SHALL SEND a copy of this Order, including the Final Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

272. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 4(i), 4(j), 201-205, 254, and 403 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 154(i), 154(j), 201-205, 254, and 403, this Further Notice of Proposed Rulemaking in CC Docket No. 96-45 IS ADOPTED.

273. IT IS FURTHER ORDERED that the Commission's Consumer Information Bureau, Reference Information Center, SHALL SEND a copy of this Further Notice of Proposed Rulemaking in CC Docket No. 96-45, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

274. IT IS FURTHER ORDERED that the provisions in this Order SHALL BE EFFECTIVE immediately upon publication in the Federal Register. Pursuant to 5 U.S.C. § 553(d)(3), we find good cause exists to have the rules take effect immediately upon publication in the Federal Register. The final rules must take effect prior to 30 days after their publication in the Federal Register in order for NECA to be able to implement the necessary changes to the high-cost loop support mechanism by July 1, 2001. The collections of information contained within are contingent upon approval by the Office of Management and Budget.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas  
Secretary

**APPENDIX A – FINAL RULES**

Part 36 and Part 54 of Title 47 of the Code of Federal Regulations are amended as follows:

**PART 36 – JURISDICTIONAL SEPARATIONS PROCEDURES; STANDARD PROCEDURES FOR SEPARATING TELECOMMUNICATIONS PROPERTY COSTS, REVENUES, EXPENSES, TAXES AND RESERVES FOR TELECOMMUNICATIONS COMPANIES****Subpart F – Universal Service Fund**

1. Section 36.601 is amended as follows.

**§ 36.601 General**

(a)-(b) \* \* \* [unchanged]

(c) Until June 30, 2001, \* \* \*

2. Sections 36.602, 36.603, 36.604, and 36.605 are added to subpart F to read as follows:

**§ 36.602 Calculation of non-rural carrier portion of nationwide loop cost expense adjustment.**

Effective July 1, 2001, for purposes of determining non-rural carrier interim hold-harmless support, pursuant to § 54.311 of this chapter, the annual amount of the total nationwide loop cost expense adjustment calculated pursuant to this subpart F shall not exceed the amount of the total loop cost expense adjustment for the immediately preceding calendar year, increased by a rate equal to the rate of increase in the total number of working loops during the calendar year preceding the July 31st filing. The total loop cost expense adjustment shall consist of the loop cost expense adjustments, including amounts calculated pursuant to § 36.612(a) and § 36.631. The rate of increase in total working loops shall be based upon the difference between the number of total working loops on December 31 of the calendar year preceding the July 31st filing and the number of total working loops on December 31 of the second calendar year preceding that filing, both determined by the company's submissions pursuant to § 36.611. Non-rural incumbent local exchange carriers and eligible telecommunications carriers serving lines in the service area of non-rural incumbent local exchange carriers shall only receive support pursuant to this subpart F to the extent that they qualify pursuant to § 54.311 of this chapter for interim hold-harmless support. Support amounts calculated pursuant to this subpart F but not received due to the phase down of interim hold-harmless support or the receipt of forward-looking support pursuant to § 54.311 of this chapter shall not be redistributed to other carriers.

**§ 36.603 Calculation of rural incumbent local exchange carrier portion of nationwide loop cost expense adjustment.**

(a) Effective July 1, 2001, the rural incumbent local exchange carrier portion of the annual nationwide loop cost expense adjustment will be recomputed by the fund administrator as if the indexed cap calculated pursuant to § 36.601(c) and the corporate operations expense limitation calculated pursuant to § 36.621 had not been in effect for the calendar year 2000. For the period July 1, 2001, to December 31, 2001, the annualized amount of the rural incumbent local exchange carrier portion of the nationwide loop cost expense adjustment calculated pursuant to this subpart F shall not exceed the non-capped amount of the total rural incumbent local exchange carrier loop cost expense adjustment for the calendar year 2000, multiplied times one plus the Rural Growth Factor calculated pursuant to § 36.604. Beginning January 1,

2002, the annual amount of the rural incumbent local exchange carrier portion of the nationwide loop cost expense adjustment calculated pursuant to this subpart F shall not exceed the amount of the total rural incumbent local exchange carrier loop cost expense adjustment for the immediately preceding calendar year, multiplied times one plus the Rural Growth Factor calculated pursuant to § 36.604.

(b) The annual rural incumbent local exchange carrier portion of the nationwide loop cost expense adjustment shall be reduced to reflect the transfer of rural incumbent local exchange carrier access lines that are eligible for expense adjustments pursuant to § 36.631. The reduction shall equal the amount of the § 36.631 expense adjustment available to the transferred access lines at the time of the transfer and shall be effective in the next calendar quarter after the access lines are transferred.

(c) Safety net additive support calculated pursuant to § 36.605, and transferred high-cost support and safety valve support calculated pursuant to § 54.305 of this chapter shall not be included in the rural incumbent local exchange carrier portion of the annual nationwide loop cost expense adjustment.

#### **§ 36.604 Calculation of the rural growth factor.**

The Rural Growth Factor (RGF) is equal to the sum of the annual percentage change in the United States Department of Commerce's Gross Domestic Product – Chained Price Index (GPD-CPI) plus the percentage change in the total number of rural incumbent local exchange carrier working loops during the calendar year preceding the July 31<sup>st</sup> filing submitted pursuant to § 36.611. The percentage change in total rural incumbent local exchange carrier working loops shall be based upon the difference between the total number of rural incumbent local exchange carrier working loops on December 31 of the calendar year preceding the July 31<sup>st</sup> filing and the total number of rural incumbent local exchange carrier working loops on December 31 of the second calendar year preceding that filing, both determined by the company's submissions pursuant to § 36.611. Loops acquired by rural incumbent local exchange carriers shall not be included in the RGF calculation.

#### **§ 36.605 Calculation of safety net additive.**

(a) “*Safety net additive support.*” A rural incumbent local exchange carrier shall receive safety net additive support if it satisfies the conditions set forth in subsection (c). Safety net additive support is support available to rural telephone companies, as conditioned in subsection (c), in addition to support calculated pursuant to § 36.631 of this subpart. Safety net additive support shall not be available to rural telephone companies for exchange(s) that are subject to § 54.305 of this chapter.

(b) *Calculation of safety net additive support:* Safety net additive support is equal to the amount of capped support calculated pursuant to this subpart F in the qualifying year minus the amount of support in the year prior to qualifying for support subtracted from the difference between the uncapped expense adjustment for the study area in the qualifying year minus the uncapped expense adjustment in the year prior to qualifying for support as shown in the following equation: Safety net additive support = (Uncapped support in the qualifying year – Uncapped support in the base year) – (Capped support in the qualifying year – Amount of support received in the base year).

(c) *Operation of safety net additive support:*

(1) In any year in which the total carrier loop cost expense adjustment is limited by the provisions of § 36.603 a rural incumbent local exchange carrier shall receive safety net additive support as calculated in subsection (b), if in any study area, the rural incumbent local exchange carrier realizes growth in end of period Telecommunications Plant in Service (TPIS), as prescribed in § 32.2001, on a per loop basis, of at least 14 percent more than the study area's TPIS per loop investment at the end of the prior period.

(2) If subsection (c)(1) is met, the rural incumbent local exchange carrier must notify the

Administrator; failure to properly notify the Administrator of eligibility shall result in disqualification of that study area for safety net additive, requiring the rural incumbent local exchange carrier to again meet the eligibility requirements in subsection (c)(1) for that study area in a subsequent period.

- (3) Upon completion of verification by the Administrator that the study area meets the criterion stated above in paragraphs (a), (b), (c) of this section, the Administrator shall:
- (i) pay to any qualifying rural telephone company, safety net additive support for the qualifying study area in accordance with the calculation set forth in subsection (b); and
  - (ii) continue to pay safety net additive support for the succeeding four years. Support in the four succeeding years shall be the lesser of:
    - (A) the amount of support paid in the qualifying year; or
    - (B) the amount of support based on recalculation of support pursuant to paragraph (b) above.

3. Section 36.611 is amended by revising the first paragraph of introductory text to read as follows:

**§ 36.611 Submission of information to the National Exchange Carrier Association (NECA).**

In order to allow determination of the study areas and wire centers that are entitled to an expense adjustment pursuant to § 36.631, each incumbent local exchange carrier (LEC) must provide the National Exchange Carrier Association (NECA) (established pursuant to Part 69 of this Chapter) with the information listed below for each study area in which such incumbent LEC operates, with the exception of the information listed in subsection (h), which must be provided for each study area and, if applicable, for each wire center, as defined in Part 54 of this Chapter, and each disaggregation zone as established pursuant to § 54.315 of this chapter. This information is to be filed with NECA by July 31<sup>st</sup> of each year. The information provided pursuant to subsection (h) must be updated pursuant to § 36.612. Rural telephone companies that acquired exchanges subsequent to May 7, 1997, and incorporated those acquired exchanges into existing study areas shall separately provide the information required by paragraphs (a) through (h) of this section for both the acquired and existing exchanges.

4. Section 36.612 is amended by revising paragraph (a) to read as follows:

**§ 36.612 Updating information submitted to the National Exchange Carrier Association.**

(a) Any rural telephone company, as that term is defined in § 51.5 of this chapter, may update the information submitted to the National Exchange Carrier Association (NECA) on July 31<sup>st</sup> pursuant to § 36.611 (a) through (h) one or more times annually on a rolling year basis according to the schedule, except that rural telephone companies in service areas where an eligible telecommunications carrier has initiated service and has reported line count data pursuant to § 54.307(c) of this chapter must update the information submitted to NECA on July 31<sup>st</sup> pursuant to § 36.611(h) according to the schedule. Every non-rural telephone company must update the information submitted to NECA on July 31<sup>st</sup> pursuant to § 36.611 (h) according to the schedule.

5. Section 36.621 is amended by revising the last sentence of paragraph (a)(4) introductory text, paragraph (a)(4)(i), the first sentence of paragraph (a)(4)(ii), and paragraphs (a)(4)(ii)(A) through (C), and adding paragraph (a)(4)(ii)(D) to read as follows:

**§ 36.621 Study area total unseparated loop cost.**

(a) \* \* \*

(4) \* \* \* Total Corporate Operations Expense, for purposes of calculating universal service support payments beginning July 1, 2001, shall be limited to the lesser of:

(i) The actual average monthly per-loop Corporate Operations Expense; or

(ii) A monthly per-loop amount computed according to paragraphs (a)(4)(ii)(A), (a)(4)(ii)(B), (a)(4)(ii)(C), and (a)(4)(ii)(D) of this section. \* \* \*

(A) For study areas with 6,000 or fewer working loops the amount monthly per working loop shall be  $\$33.30853 - (.00246 \times \text{the number of working loops})$ , or,  $\$50,000 \div \text{the number of working loops}$ , whichever is greater;

(B) for study areas with more than 6,000 but fewer than 18,006 working loops, the monthly amount per working loop shall be  $\$3.83195 + (88,429.20 \div \text{the number of working loops})$ ; and

(C) for study areas with 18,006 or more working loops, the monthly amount per working loop shall be  $\$8.74472$ .

(D) Beginning January 1, 2002, the monthly per-loop amount computed according to paragraphs (a)(4)(ii)(A), (a)(4)(ii)(B), and (a)(4)(ii)(C) of this section shall be adjusted each year to reflect the annual percentage change in the United States Department of Commerce's Gross Domestic Product-Chained Price Index (GDP-CPI).

6. Section 36.622 is amended by adding a sentence at the end of paragraph (a) as follows:

**§ 36.622 National and study area average unseparated loop costs.**

(a) \* \* \* Effective July 1, 2001, the national average unseparated loop cost for purposes of calculating expense adjustments for rural incumbent local exchange carriers, as that term is defined in § 54.5 of this chapter, is frozen at \$240.00.

7. Section 54.5 is amended by adding the following definition:

**PART 54 -- UNIVERSAL SERVICE****Subpart A – General Information****§ 54.5 Terms and definitions.**

*Rural Incumbent Local Exchange Carrier.* "Rural incumbent local exchange carrier" is a carrier that meets the definitions of "rural telephone company" and "incumbent local exchange carrier," as those terms are defined in § 51.5 of this chapter.

8. Amend section 54.305 by adding '(a)' at the beginning of the first sentence of the current § 54.305 and by adding paragraphs (b), (c), (d), (e), and (f) to read as follows:

**Subpart D – Universal Service Support for High Cost Areas**

**§ 54.305 Sale or transfer of exchanges.**

(b) Transferred exchanges in study areas operated by rural telephone companies that are subject to the limitations on the transfer of high-cost universal service support in paragraph (a) of this section may be eligible for a safety valve loop cost expense adjustment based on the difference between a rural incumbent local exchange carrier's index year expense adjustment and subsequent year expense adjustments for the acquired exchanges. Safety valve loop cost expense adjustments shall only be available to rural incumbent local exchange carriers that, in the absence of restrictions on the transfer of high-cost support in § 54.305(a), would qualify for high-cost loop support for acquired exchanges under § 36.631 of this chapter.

(c) The index year expense adjustment for acquired exchange(s) shall be equal to the rural incumbent local exchange carrier's high-cost loop cost expense adjustment for acquired exchanges calculated at the end of the company's first year operating the acquired exchange(s). The index year expense adjustment for the acquired exchange(s) shall be established through cost data submitted in accordance with § 36.611 and § 36.612 and shall be calculated in accordance with § 36.631 of this chapter. For carriers establishing an index year for acquired exchanges pursuant to § 36.611, the index year for the acquired exchange(s) shall commence at the beginning of the next calendar year after the transfer of said exchanges. For carriers establishing an index year for acquired exchanges pursuant to § 36.612, the index year for the acquired exchange(s) shall commence at the beginning of the next calendar quarter after the transfer of said exchanges. The index year expense adjustment for rural telephone companies that have operated exchanges subject to this section for more than a full year on the effective date of this subsection shall be based on loop cost data submitted in accordance with § 36.612 for the year ending on the nearest calendar quarter following the effective date of this subsection. At the end of each subsequent year, a loop cost expense adjustment for the acquired exchanges will be calculated pursuant to § 36.631 and will be compared to the index year expense adjustment. A rural incumbent local exchange carrier's subsequent year expense adjustments shall end on the same calendar quarter as its index year expense adjustment. If acquired exchanges are incorporated into an existing rural incumbent local exchange carrier study area, the rural incumbent local exchange carrier shall exclude costs associated with the acquired exchanges from the costs associated with its pre-acquisition study area in its universal service data submissions filed in accordance with § 36.611 and § 36.612. Such excluded costs shall be used to calculate the rural incumbent local exchange carrier's safety valve loop cost expense adjustment.

(d) Up to fifty (50) percent of any positive difference between the subsequent year loop cost expense adjustment and the index year expense adjustment will be designated as the study area's safety valve loop cost expense adjustment and will be available in addition to the amounts available to the study area under § 54.305. In no event shall a study area's safety valve loop cost expense adjustment exceed the difference between the carrier's uncapped study area loop cost expense adjustment calculated pursuant to § 36.631 and transferred support amounts available to the acquired exchange(s) under paragraph (a) of this section. Safety valve support shall not transfer with acquired exchanges.

(e) The sum of the safety valve loop cost expense adjustment for all eligible study areas operated by rural telephone companies shall not exceed five (5) percent of the total rural incumbent local exchange carrier portion of the annual nationwide loop cost expense adjustment calculated pursuant to § 36.603. The five (5) percent cap on the safety valve mechanism shall be based on the lesser of the rural incumbent local exchange carrier portion of the annual nationwide loop cost expense adjustment calculated pursuant to § 36.603 or the sum of rural incumbent local exchange carrier expense adjustments calculated pursuant to § 36.631. The percentage multiplier used to derive study area safety valve loop cost expense adjustments for rural telephone companies shall be the lesser of fifty (50) percent or a percentage calculated to produce the maximum total safety valve loop cost expense adjustment for all eligible study areas pursuant to this paragraph. The safety valve loop cost expense adjustment of an individual rural incumbent local exchange carrier also may be further reduced as described in subsection (d).

(f) Once an acquisition is complete, the acquiring rural incumbent local exchange carrier shall provide written notice to the Administrator that it has acquired access lines that may be eligible for safety valve support. Rural telephone companies also shall provide written notice to the Administrator of when their index year has been established for purposes of calculating the safety valve loop cost expense adjustment.

9. Amend § 54.307 by revising paragraph (a)(1), by revising the second sentence in paragraph (b) and adding a sentence at the end of paragraph (b), and by revising the first sentence in paragraph (c) to read as follows:

**§ 54.307 Support to a competitive eligible telecommunications carrier.**

(a) \* \* \*

(1) A competitive eligible telecommunications carrier serving loops in the service area of a rural incumbent local exchange carrier, as that term is defined in § 54.5 of this chapter, shall receive support for each line it serves in a particular service area based on the support the incumbent LEC would receive for each such line, disaggregated by cost zone if disaggregation zones have been established within the service area pursuant to § 54.315 of this subpart. A competitive eligible telecommunications carrier serving loops in the service area of a non-rural incumbent local exchange carrier shall receive support for each line it serves in a particular wire center based on the support the incumbent LEC would receive for each such line.

(b) \* \* \* For a competitive eligible telecommunications carrier serving loops in the service area of a rural incumbent local exchange carrier, as that term is defined in § 54.5 of this chapter, the carrier must report the number of working loops it serves in the service area disaggregated by cost zone if disaggregation zones have been established within the service area pursuant to § 54.315 of this subpart. \* \* \* Competitive eligible telecommunications carriers providing mobile wireless service in an incumbent LEC's service area shall use the customer's billing address for purposes of identifying the service location of a mobile wireless customer in a service area.

(c) A competitive eligible telecommunications carrier must submit the data required pursuant to paragraph (b) of this section according to the schedule. \* \* \*

10. Section 54.313 is renamed "State certification of support for non-rural carriers" and amended by creating a new subsection (b), revising and re-designating subsection (c), and re-designating current subsection (c) as subsection (d):

**§ 54.313 State certification of support for non-rural carriers.**

(b) *Carriers Not Subject to State Jurisdiction.* A non-rural incumbent local exchange carrier not subject to the jurisdiction of a state or an eligible telecommunications carrier not subject to the jurisdiction of a state serving lines in the service area of a non-rural incumbent local exchange carrier that desires to receive support pursuant to §§ 54.309 and/or 54.311 of this subpart must file an annual certification with the Administrator and the Commission stating that all federal high-cost support provided to such carriers will be used only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Support provided pursuant to §§ 54.309 and/or 54.311 of this subpart shall only be provided to the extent that the carrier has filed the requisite certification pursuant to this section.

(c) *Certification Format.* A certification pursuant to this section may be filed in the form of a letter from the appropriate regulatory authority for the State, and must be filed with both the Office of the Secretary of the Commission clearly referencing CC Docket No. 96-45, and with the Administrator of the high-cost universal service support mechanism, on or before the deadlines set forth below in subsection (d). If provided by the appropriate regulatory authority for the state, the annual certification must identify which carriers in the State are eligible to receive federal support during the

applicable 12-month period, and must certify that those carriers will only use support for the provision, maintenance, and upgrading of facilities and services for which support is intended. A State may file a supplemental certification for carriers not subject to the State's annual certification. All certificates filed by a State pursuant to this section shall become part of the public record maintained by the Commission. Non-rural incumbent local exchange carriers not subject to the jurisdiction of a state or eligible telecommunications carrier not subject to the jurisdiction of a state serving lines in the service area of a non-rural incumbent local exchange carrier, shall file a sworn affidavit executed by a corporate officer attesting to the use of the support for the provision, maintenance, and upgrading of facilities and services for which support is intended. The affidavit must be filed with both the Office of the Secretary of the Commission clearly referencing CC Docket No. 96-45, and with the Administrator of the high-cost universal service support mechanism, on or before the deadlines set forth below in subsection (d). All affidavits filed pursuant to this section shall become part of the public record maintained by the Commission.

11. Section 54.314 is added to subpart D as follows:

**§ 54.314. State certification of support for rural carriers.**

- (a) *State Certification.* States that desire rural incumbent local exchange carriers and/or eligible telecommunications carriers serving lines in the service area of a rural incumbent local exchange carrier within their jurisdiction to receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this part and/or part 36, subpart F of this chapter must file an annual certification with the Administrator and the Commission stating that all federal high-cost support provided to such carriers within that State will be used only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Support provided pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter shall only be provided to the extent that the State has filed the requisite certification pursuant to this section.
- (b) *Carriers Not Subject to State Jurisdiction.* A rural incumbent local exchange carrier not subject to the jurisdiction of a state or an eligible telecommunications carrier not subject to the jurisdiction of a state serving lines in the service area of a rural incumbent local exchange carrier that desires to receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter shall file an annual certification with the Administrator and the Commission stating that all federal high-cost support provided to such carriers will be used only for the provision, maintenance, and upgrading of facilities and services for which the support is intended. Support provided pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter shall only be provided to the extent that the carrier has filed the requisite certification pursuant to this section.
- (c) *Certification Format.* A certification pursuant to this section may be filed in the form of a letter from the appropriate regulatory authority for the State, and shall be filed with both the Office of the Secretary of the Commission clearly referencing CC Docket No. 96-45, and with the Administrator of the high-cost universal service support mechanism, on or before the deadlines set forth below in subsection (d). If provided by the appropriate regulatory authority for the state, the annual certification must identify which carriers in the State are eligible to receive federal support during the applicable 12-month period, and must certify that those carriers will only use support for the provision, maintenance, and upgrading of facilities and services for which support is intended. A State may file a supplemental certification for carriers not subject to the State's annual certification. All certificates filed by a State pursuant to this section shall become part of the public record maintained by the Commission. Rural incumbent local exchange carriers not subject to the jurisdiction of a state or eligible telecommunications carriers not subject to the jurisdiction of a state serving lines in the service area of a rural incumbent local exchange carrier, shall file a sworn affidavit executed by a corporate officer attesting to the use of the support for the provision, maintenance, and upgrading of facilities and

services for which support is intended. The affidavit must be filed with both the Office of the Secretary of the Commission clearly referencing CC Docket No. 96-45, and with the Administrator of the high-cost universal service support mechanism, on or before the deadlines set forth below in subsection (d). All affidavits filed pursuant to this section shall become part of the public record maintained by the Commission.

- (d) *Filing Deadlines.* Upon the filing of the certification described in subsection (c), support shall be provided pursuant to the following schedule:
- (1) *Certifications filed on or before October 1.* Carriers for which certifications are filed on or before October 1 shall receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter, in the first, second, third, and fourth quarters of the succeeding year.
  - (2) *Certifications filed on or before January 1.* Carriers for which certifications are filed on or before January 1 shall receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter, in the second, third, and fourth quarters of that year. Such carriers shall not receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter in the first quarter of that year.
  - (3) *Certifications filed on or before April 1.* Carriers for which certifications are filed on or before April 1 shall receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter, in the third and fourth quarters of that year. Such carriers shall not receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter in the first and second quarters of that year.
  - (4) *Certifications filed on or before July 1.* Carriers for which certifications are filed on or before July 1 shall receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter, in the fourth quarter of that year. Such carriers shall not receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter in the first, second, or third quarters of that year.
  - (5) *Certifications filed after July 1.* Carriers for which certifications are filed after July 1 shall not receive support pursuant to §§ 54.301, 54.305, and/or 54.307 of this subpart and/or part 36, subpart F of this chapter, in that year.

12. Section 54.315 is added to subpart D as follows:

**§ 54.315 Disaggregation and targeting of support by rural incumbent local exchange carriers.**

(a) Within 270 days of the effective date of this rule, all rural incumbent local exchange carriers for which high-cost universal service support pursuant to §§ 54.301, 54.303, and/or 54.305 of this subpart and/or part 36, subpart F of this chapter is available must select a disaggregation path as described in subsections (b), (c), or (d) below. In study areas in which a competitive carrier has been designated as a competitive eligible telecommunications carrier prior to the effective date of this rule, the rural incumbent local exchange carrier may only disaggregate support pursuant to subsection (b), (c), or (d)(1)(iii). A rural incumbent local exchange carrier failing to select a disaggregation path as described in subsections (b), (c), or (d) within 270 days of the effective date of this rule will not be permitted to disaggregate and target federal high-cost support unless ordered to do so by the state commission as that term is defined in § 54.5 of this part.

(b) *Path 1: Carriers Not Disaggregating and Targeting High-Cost Support:*

- (1) A carrier may certify to the state commission that it will not disaggregate and target high-cost universal service support.
- (2) A carrier's election of this path becomes effective upon certification by the carrier to the state commission.
- (3) This path shall remain in place for such carrier for at least four years from the date of certification to the state commission except as provided in subsection (b)(4) below.
- (4) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by the rural incumbent local exchange carrier, the disaggregation and targeting of support under subsections (c) or (d).
- (5) A carrier not subject to the jurisdiction of a state, *e.g.*, certain tribally owned carriers, may select Path 1, but must certify to the Federal Communications Commission as described in paragraphs (b)(1) through (4) of this section.

*(c) Path 2: Carriers Seeking Prior Regulatory Approval for the Disaggregation and Targeting of Support.*

- (1) A carrier electing to disaggregate and target support under this subsection must file a disaggregation and targeting plan with the state commission.
- (2) Under this subsection a carrier may propose any method of disaggregation and targeting of support consistent with the general requirements detailed in subsection (e) of this provision.
- (3) A disaggregation and targeting plan under this subsection becomes effective upon approval by the state commission.
- (4) A carrier shall disaggregate and target support under this path for at least four years from the date of approval by the state commission except as provided in subsection (c)(5) below.
- (5) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by the rural incumbent local exchange carrier, the disaggregation and targeting of support in a different manner.
- (6) A carrier not subject to the jurisdiction of a state, *e.g.*, certain tribally owned carriers, may select Path 2, but must seek approval from the Federal Communications Commission as described in paragraphs (c)(1) through (5) of this section.

*(d) Path 3: Self-Certification of the Disaggregation and Targeting of Support.*

- (1) A carrier may file a disaggregation and targeting plan with the state commission along with a statement certifying each of the following:
  - (i) it has disaggregated support to the wire center level; or
  - (ii) it has disaggregated support into no more than two cost zones per wire center; or
  - (iii) that the carrier's disaggregation plan complies with a prior regulatory determination made by the state commission.
- (2) Any disaggregation plan submitted pursuant to this subsection must meet the following requirements:
  - (i) The plan must be supported by a description of the rationale used, including the methods and data relied upon to develop the disaggregation zones, and a discussion of how the plan complies with the requirements of this subsection (c)(2). Such filing must provide information sufficient for interested parties to make a meaningful analysis of how the carrier derived its disaggregation plan.
  - (ii) The plan must be reasonably related to the cost of providing service for each disaggregation zone within each disaggregated category of support.
  - (iii) The plan must clearly specify the per-line level of support for each category of high-cost universal service support provided pursuant to §§ 54.301, 54.303, and/or 54.305 of this subpart and/or part 36, subpart F of this chapter in each disaggregation zone.
  - (iv) If the plan uses a benchmark, the carrier must provide detailed information explaining what the benchmark is and how it was determined. The benchmark must be generally consistent with how

the total study area level of support for each category of costs is derived to enable a competitive eligible telecommunications carrier to compare the disaggregated costs used to determine support for each cost zone.

- (3) A carrier's election of this path becomes effective upon certification by the carrier to the state commission.
- (4) A carrier shall disaggregate and target support under this path for at least four years from the date of certification to the state commission except as provided in subsection (d)(5) below.
- (5) A state commission may require, on its own motion, upon petition by an interested party, or upon petition by the rural incumbent local exchange carrier, modification to the disaggregation and targeting of support selected under this path.
- (6) A carrier not subject to the jurisdiction of a state, *e.g.*, certain tribally owned carriers, may select Path 3, but must certify to the Federal Communications Commission as described in paragraphs (d)(1) through (5) of this section.

(e) *Additional Procedures Governing the Operation of Path 2 and Path 3:*

Disaggregation and targeting plan adopted under subsections (c) or (d) shall be subject to the following general requirements:

- (1) Support available to the rural incumbent local exchange carrier's study area under its disaggregation plan shall equal the total support available to the study area without disaggregation.
- (2) The ratio of per-line support between disaggregation zones for each disaggregated category of support shall remain fixed over time, except as changes are allowed pursuant to subsection (c) and (d) above.
- (3) The ratio of per-line support shall be publicly available.
- (4) Per-line support amounts for each disaggregation zone shall be recalculated whenever the rural incumbent local exchange carrier's total annual support amount changes using the changed support amount and lines at that point in time.
- (5) Per-line support for each category of support in each disaggregation zone shall be determined such that the ratio of support between disaggregation zones is maintained and that the product of all of the rural incumbent local exchange carrier's lines for each disaggregation zone multiplied by the per-line support for those zones when added together equals the sum of the rural incumbent local exchange carrier's total support.
- (6) Until a competitive eligible telecommunications carrier is certified in a study area, monthly payments to the rural incumbent local exchange carrier will be made based on total annual amounts for its study area divided by 12.
- (7) When a competitive eligible telecommunications carrier is certified in a study area, per-line amounts used to determine the competitive eligible telecommunications carrier's disaggregated support shall be based on the rural incumbent local exchange carrier's then-current total support levels, lines, and disaggregated support relationships.

(f) *Submission of Information to the Administrator:*

- (1) A rural incumbent local exchange carrier certifying under subsection (b) that it will not disaggregate and target high-cost universal service support shall submit to the Administrator a copy of the certification submitted to the state commission, or the Federal Communications Commission, when not subject to state jurisdiction.
- (2) A rural incumbent local exchange carrier electing to disaggregate and target support under subsection (c) shall submit to the Administrator a copy of the order approving the disaggregation and targeting plan submitted by the carrier to the state commission, or the Federal Communications Commission, when not subject to state jurisdiction, and a copy of the disaggregation and targeting plan approved by the state commission or the Federal Communications Commission.

- (3) A rural incumbent local exchange carrier electing to disaggregate and target support under subsection (d) shall submit to the Administrator a copy of the self-certification plan including the information submitted to the state commission pursuant to (d)(2)(i) and (d)(2)(iv) or the Federal Communications Commission.
- (4) A rural incumbent local exchange carrier electing to disaggregate and target support under subsection (c) or (d) must submit to the Administrator maps which precisely identify the boundaries of the designated disaggregation zones of support within the carrier's study area.

## APPENDIX B

## PARTIES FILING COMMENTS AND REPLY COMMENTS

Comments:

<u>Commenters</u>	<u>Abbreviation</u>
Ad Hoc Telecommunications User Committee	
Alaska Rural Coalition	
Alaska Telephone Association	Alaska Tel. Assn.
AT&T Corp.	AT&T
Arizona Local Exchange Carriers Association	Arizona LEC Assn.
CenturyTel, Inc.	CenturyTel
Competitive Universal Service Coalition	CUSC
Evans Telephone Co.	Evans Tel. Co., et al.
Humboldt Telephone Co.	
Kerman Telephone Co.	
Oregon-Idaho Utilities, Inc.	
Pine Tree Telephone & Telegraph Co.	
Pinnacles Telephone co.	
The Ponderosa Telephone Co.	
The Siskiyou Telephone Co.	
The Volcano Telephone Co.	
War Telephone Co.	
Florida Public Service Commission	Florida Commission
Fred Williamson & Associates, Inc.	Fred Williamson & Assoc.
General Communications, Inc.	
GVNW Consulting, Inc.	GVNW Consulting
Illinois Commerce Commission	Illinois Commission
Innovative Telephone	
Interstate Telcom Group	
John Staurulakis, Inc.	
Maine Public Utilities Commission and Vermont Public Service Board	Maine and Vermont Commissions
National Exchange Carrier Association, Inc.	NECA
National Rural Telecom Association, Organization for the Promotion and Advancement of Small Telecommunications Companies, and the United States Telecom Association	NRTA, OPASTCO, & USTA
National Telephone Cooperative Association	NTCA
New York State Dept. of Public Service	NYDPS
Public Service Commission of the U.S. Virgin Islands	Virgin Islands Commission
People of the State of California and California Public Utilities Commission (filing jointly)	California Commission
Public Utility Commission of Texas	Texas Commission
Rural Independent Competitive Alliance	
Rural Leadership Coalition	
Rural Task Force	
Rural Utilities Service	RUS
Sprint Corporation	Sprint

South Dakota Independent Telephone Coalition	
Telecom Consulting Associates	
Townes Telecommunications, Inc.	Townes Telecommunications
Universal Service Administrative Company	USAC
Verizon Telephone Companies	Verizon
Western Alliance	
Wisconsin Public Service Commission	Wisconsin Commission
Wyoming Public Service Commission	Wyoming Commission

**Reply Comments:**Commenter**Abbreviation**

Ad Hoc Telecommunications Users Committee	
Alaska Rural Coalition	
Alliance of Incumbent Rural Independent Telephone Companies	
AT&T Corp.	AT&T
CenturyTel, Inc.	CenturyTel
GVNW Consulting, Inc.	
Illinois Commerce Commission	Illinois Commission
Innovative Telephone	
Iowa Telecommunications, Inc.	Iowa Telecommunications
McLean & Brown	
National Exchange Carrier Association	NECA
National Rural Telecom Association, Organization for the Promotion and Advancement of Small Telecommunications Companies, and the United States Telecom Association	NRTA, OPASTCO, & USTA
New York State Department of Public Services	NYDPS
Roseville Telephone Company	Roseville Tel. Co.
Rural Task Force	
Southwestern Bell Telephone Company	SBC
Sprint Corporation	Sprint
Telecom Consulting Associates	

**APPENDIX C  
PARTIES FILING COMMENTS  
IN MAG PROCEEDING (CC DOCKET NO. 00-256)**

Comments:

<u>Commenter</u>	<u>Abbreviation</u>
Ad Hoc Telecommunications Users Committee	
Alabama Rural Local Exchange Carriers	Alabama Rural LECs
Alaska Rural Coalition	
Alaska Telephone Association	Alaska Tel. Assn.
Arizona Local Exchange Carriers Association	Arizona LEC Assn.
Association of Communications Enterprises	
AT&T Corp.	AT&T
BellSouth Corporation and BellSouth Telecommunications, Inc.	BellSouth
People of the State of California and California Public Utilities Commission (filing jointly)	California Commission
Competitive Universal Service Coalition	
Evans Telephone Co.	Evans Tel. Co., et. al
Humboldt Telephone Co.	
Kerman Telephone Co.	
Oregon-Idaho Utilities, Inc.	
Pine Tree Telephone & Telegraph Co.	
Pinnacles Telephone co.	
The Ponderosa Telephone Co.	
The Siskiyou Telephone Co.	
The Volcano Telephone Co.	
War Telephone Co.	
Florida Public Service Commission	Florida Commission
Fred Williamson & Associates, Inc.	Fred Williamson & Assoc.
General Communications, Inc.	
General Services Administration	GSA
Global Crossing North America, Inc.	Global Crossing
GVNW Consulting, Inc.	GVNW Consulting
Illinois Commerce Commission	Illinois Commission
Independent Telephone & Telecommunications Alliance	
ICORE, Inc.	
Innovative Telephone	
Interstate Telcom Group	
ITCs, Inc.	
John Staurulakis, Inc.	
Multi-Association Group	
Missouri Public Service Commission	Missouri Commission
New York State Dept. of Public Service	NYDPS
National Association of State Utility Consumer Advocates	NASUCA
Ohio Telecommunications Industry Association	
Plains Rural Independent Companies	

Public Service Commission of the State of Missouri	Missouri Commission
Public Service Commission of Wisconsin	Wisconsin Commission
Public Utility Commission of Texas	Texas Commission
Qwest Communications International Inc.	Qwest
Rate-of-Return Coalition	
Regulatory Commission of Alaska	Alaska Commission
Roseville Telephone Company	Roseville Tel. Co.
Rural Independent Competitive Alliance	
Small Company Members of the Telephone Association of New England	
Sprint Corporation	Sprint
Telecom Consulting Associates, Inc.	
TDS Telecommunications Corporation	TDS
Townes Telecommunications, Inc.	
Western Alliance	
WorldCom, Inc.	WorldCom

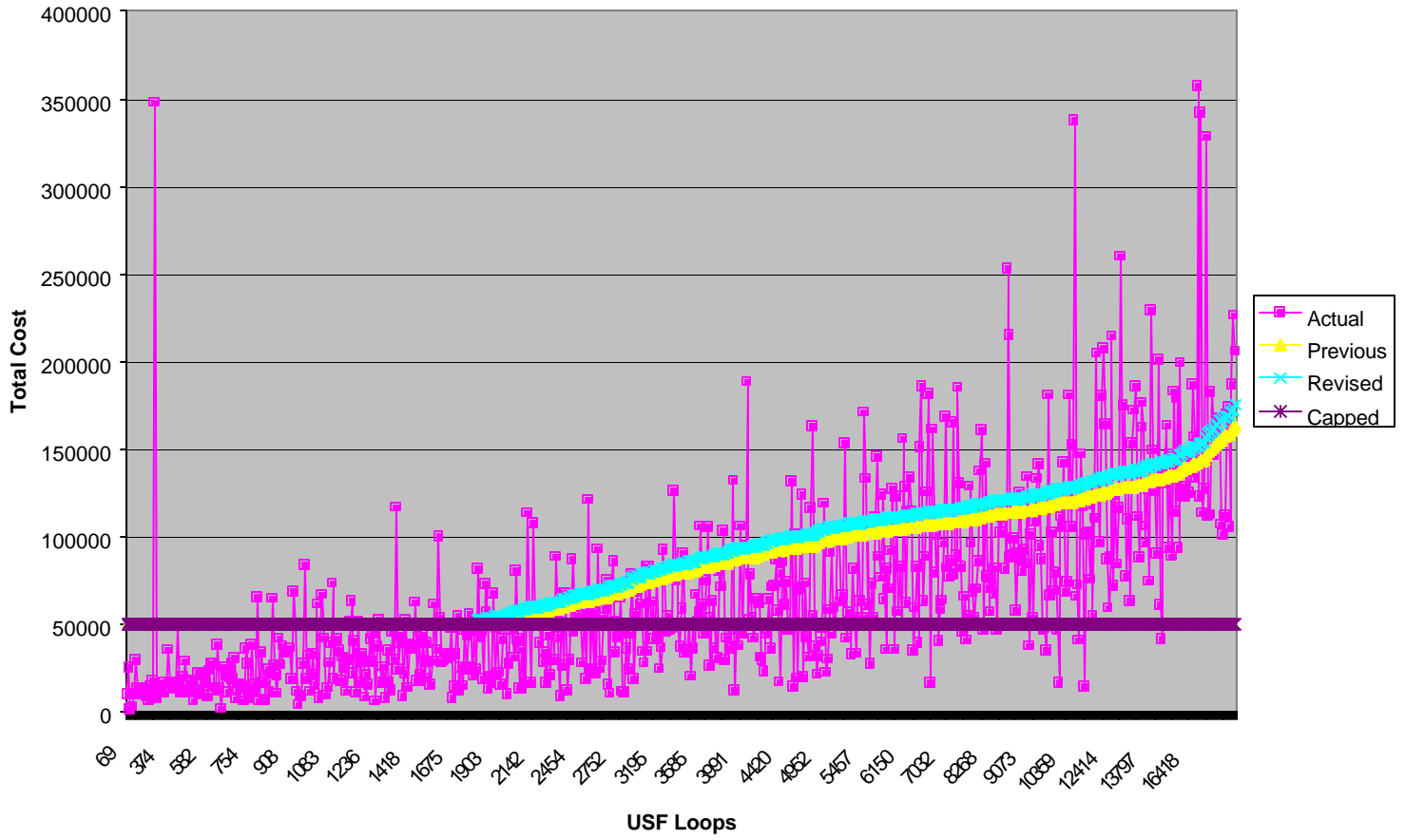
**Reply Comments:**CommenterAbbreviation

Ad Hoc Telecommunications Users Committee	
Alaska Rural Coalition	
Alliance of Incumbent Rural Independent Telephone Companies	
AT&T Corp.	AT&T
Dunkirk and Fredonia Telephone Company	Dunkirk and Fredonia Tel. Co.
Excel Communications, Inc.	Excel
General Service Administration	GSA
GVNW Consulting, Inc.	GVNW Consulting
Indiana Utility Regulatory Commission	Indiana Commission
Innovative Telephone	
Interstate Telcom Group	
Iowa Utilities Board	
John Staurulakis, Inc.	
Minnesota Independent Coalition	
Multi-Association Group	MAG
Plains Rural Independent Companies	
Puerto Rico Telephone Company, Inc.	Puerto Rico Tel. Co.
Rate-of-Return Coalition	
Regulatory Commission of Alaska	Alaska Commission
Ronan Telephone Company	Ronan Tel. Co.
Ronan Telephone Consumer Advisory Committee	
Roseville Telephone Company	Roseville Tel. Co.
Rural Independent Competitive Alliance	
State of Alaska	Alaska
State of Hawaii	Hawaii
Summit Telephone and Telegraph Company of Alaska, Inc.	Summit Tel. Co.
Telcom Consulting Associates, Inc.	
TDS Telecommunications Corporation	TDS
Verizon Telephone Companies	Verizon

Western Alliance  
WorldCom, Inc.  
Wyoming Public Service Commission

WorldCom  
Wyoming Commission

Appendix D - 1999 Corporate Operations Expense



**SEPARATE STATEMENT OF CHAIRMAN MICHAEL K. POWELL**

*Re: Fourteenth Report and Order and Twenty-Second Order on Reconsideration, Federal-State Joint Board on Universal Service and Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers (CC Dkt. Nos. 96-45, 00-256).*

I am pleased to support this Order because, today, the Commission finally takes action to fill in the third piece of the four-part universal service puzzle: high-cost loop support for rural carriers. The Commission filled in the first piece of this difficult puzzle in 1999 when it reformed high-cost loop support for non-rural carriers based on a forward-looking cost model. We moved the second piece of the puzzle into place in 2000 with the adoption of access reform and interstate access support for price cap carriers in the CALLS Order. Today's action on the third piece of the puzzle, rural high-cost loop support - and the pending proceeding on the puzzle's fourth piece, rural access reform - are two of the most important actions the Commission will take this year. Viewed as a whole, this comprehensive package of access and universal service reforms will ensure that consumers in all areas of the country, especially those living in high-cost rural areas, have access to telecommunications services at affordable rates.

A number of innovative rural carriers have begun to meet the challenge of ensuring that their customers benefit from the same twenty-first century telephone infrastructure that other Americans are starting to enjoy. Many others, however, have been less able to meet this challenge. In particular, in many cases, the costs of serving far-flung customers has outstripped rural carriers' financial resources. This has, in some cases, hindered these carriers from making much-needed improvements and upgrades to their networks to provide basic supported services.

With this Order, we adjust rural high-cost loop support to address a facet of this pressing problem. The increases to rural high-cost loop support will begin relatively modestly (roughly \$126 million total support for Year 1) and then ramp up to a total price tag over the five year term of the plan of over \$1 billion. Together with our other existing universal service programs, our total support for rural carriers during this five year period is projected to be well over \$9 billion - before we address rural access reform.

Although I vigorously support the Commission taking this important action, I acknowledge that there are limitations to this plan. As the Order emphasizes, this is an interim five-year plan, reflecting the fact that we have more work to do in this area. Specifically, I believe it is important that we develop a permanent support mechanism, based on forward-looking costs or another appropriate measure of costs, by which we can ensure that the rural high-cost loop fund grows no larger than is truly necessary to accomplish its purpose. As I have stated repeatedly, we must guard against allowing universal service programs to grow too large, lest we collect so much from carriers that they are hindered in their ability to compete and bring consumers new and better products and services.

If we could address this concern and adopt a permanent solution today, I would be the first to support it. But these issues are exceedingly complex and will take more time to develop. At the same time, further delay is not an option in my view. The Commission has taken simply too long to address rural carrier issues in its implementation of the Act's universal service requirements.

I would re-emphasize that this is only one piece of the puzzle for rural carriers. The Bureau intends to prepare a formal recommendation regarding rural access reform, including consideration of the "MAG proposal" within the next few months. It will be one of my top priorities to make significant progress on rural access reform as soon as logistically possible.

In closing, I would like to extend my deepest gratitude to my state colleagues and staff, as well as my fellow commissioners and staff, for their invaluable contributions to this reform effort. The Rural Task Force and the Joint Board on Universal Service are especially commended for their insight and vigor in developing this interim support mechanism.

**Separate Statement of Commissioner Susan Ness**

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

Today we complete another major chapter in our effort to preserve and advance universal service, one of the fundamental pillars of the Telecommunications Act of 1996. Section 254 of the Act requires us to ensure that all Americans have access to telecommunications services at affordable and reasonably comparable rates. Congress recognized that we need to pay special attention to the needs of (1) low-income consumers, (2) those living in rural, insular, and high-cost areas, and (3) schools, libraries, and rural health care providers.

We have made steady and significant progress in each of these areas. For low-income consumers, we augmented our Lifeline and Link-Up programs to increase the level of federal support and ensure that support is available to the urban and rural poor in every state. For schools, libraries, and rural health care providers, we have successfully implemented the bold vision in the 1996 Act to deliver the tools of the Information Age through discounts on telecommunications and information services.

And for consumers in high-cost areas, we have taken steps to establish universal service support mechanisms that are explicit and sustainable in a competitive market. We previously reformed the high-cost mechanisms for non-rural carriers, and they are making the transition to a support mechanism based on forward-looking costs. Today, we address high-cost reform for rural carriers by adopting a mechanism that works for rural America.

When the FCC undertook its review of the high-cost universal service mechanism following passage of the 1996 Act, we recognized the unique challenges facing rural carriers and did not adopt one-size-fits-all policies that might have impeded rather than supported the provision of affordable service by rural carriers. Instead, working with rural carriers and their associations, the Joint Board convened a Rural Task Force comprised of experts representing a wide range of companies, consumer advocates, and government officials to examine the cost structures and circumstances of rural carriers.

In October, after intensive research and deliberations, the Rural Task Force unanimously recommended a high-cost mechanism for rural carriers that takes into account not only the significant differences *between* rural and non-rural carriers, but also the vastly different cost structures *among* rural carriers. As is the case with any consensus proposal, the framework may not be exactly what any one entity would want. Nevertheless, the plan represents a solid compromise that balances competing interests. I support this order because it will provide the stability necessary for rural carriers to plan for the future and undertake critical investment to benefit rural consumers.

As we celebrate completion of this phase of high-cost reform, however, we note that much remains to be done.

First, we have not yet completed efforts to identify and make explicit the subsidies embedded in rural carriers' access charges. Reforming high-cost mechanisms without addressing access charges is like clapping with one hand. I urge the Commission to make access charge reform and resolution of the other issues raised by the Multi-Association Group a top priority. For many rural carriers, access charges comprise well over half of their revenue stream. It is not easy for rural carriers to plan for the future and invest in their communities when there is uncertainty about this portion of their revenue base.

Second, even as the Commission works to complete action to reform the federal universal service mechanisms, we must remember that keeping telephone service affordable and accessible is a shared federal and state responsibility. I commend the states that have implemented measures to address rate comparability within their borders and urge other states to undertake such initiatives. State commissions also have a critical role to play in ensuring that subsidies implicit in intrastate rates are made explicit.

Third, we must remain mindful that universal service is an evolving concept that merits our continuing attention. For low-income consumers, we must ensure that those for whom Lifeline and Link-Up are intended know about and have access to these programs. For schools and libraries, we must determine why some communities, including ones in rural and high-poverty areas, are not taking advantage of E-Rate discounts to hook up their classrooms and libraries to the Internet. We should also seek to build on our success with the E-Rate to find ways to leverage for the entire community – especially in remote areas -- the technological resources made available to schools and libraries.

For high-cost areas, our continuing challenge is to ensure that consumers have access to reasonably comparable services at reasonably comparable prices through a high-cost mechanism that is economically rational and competitively neutral. Today, we take an important step by adopting a framework for rural carriers. We must now focus our attention on further steps, including in the near future, a review of the services that are supported by universal service and an examination of ways to facilitate the deployment of advanced services to all Americans in a reasonable and timely manner. As we proceed on these and other measures, I urge the Commission to continue working together with our state colleagues – and with the Joint Board in particular -- to ensure that specific, predictable, and sufficient mechanisms remain in place.

As a final matter, I would like to acknowledge the many people who have demonstrated through hard work their commitment to preserving and advancing universal service for all Americans.

I commend the Rural Task Force for its unwavering efforts for rural consumers. I especially want to thank the chair of the Task Force, Bill Gillis, who worked tirelessly to fashion a consensus.

I would also like to thank the Joint Board and its staff for their dedication to ensuring that all Americans have access to affordable, quality telecommunications services. Together, we have worked hard to forge a federal-state partnership to promote the goals of universal service.

Finally, I would like to thank the Common Carrier Bureau, and in particular, the Accounting Policy Division. Bureau staff members have spent countless hours working through complex issues. They are indeed public servants of the highest caliber.