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

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

COMMENTS OF JOHN STAURULAKIS, INC.

John Staurulakis, Inc. ("JSI") hereby files these comments in response to the request by the Federal Communications Commission ("FCC" or "Commission") for comments on the Recommended Decision of the Federal-State Joint Board ("Joint Board") regarding a plan developed by the Rural Task Force ("RTF") for reforming the rural universal service support mechanism.[1]

JSI is a consulting firm specializing in regulatory and financial services to more than two hundred incumbent local exchange carriers ("ILECs") throughout the United States. Among its consulting services, JSI assists these ILECs in the preparation and submission of jurisdictional cost studies and Universal Service Fund ("USF") data to the National Exchange Carrier Association ("NECA"), and routinely prepares and files tariffs with the Commission on behalf of a number of these ILECs. JSI also provides consulting services for competitive local exchange carriers ("CLECs") that provide competitive local exchange services across the nation. Since the Commission seeks comments on the Petition that has the potential to alter the current federal universal service rules and potentially to alter interstate access rules, JSI is an interested party in this proceeding.

I. RTF HAS DEVELOPED A FOUNDATION FOR THE TRANSITION OF RURAL UNIVERSAL SERVICE

JSI has observed the activity of the RTF since its inception. Representatives of JSI have attended many of the RTF meetings and conference calls as observers. We acknowledge the leadership of former Commissioner Gillis in directing a diverse and occasionally disputatious group toward a unified consensus. JSI believes that the RTF has constructed a solid foundation on which the Commission should build to satisfy its statutory duties regarding universal service for rural telephone companies.

JSI believes that the foundation developed by the RTF is its evaluation and judgment that hypothetical cost proxy models are not sufficiently developed to accurately predict the need for universal service support, nor are such models able to ensure sufficiency of universal service support for rural telephone companies and their end-user customers. Based on JSI's experience in working with cost proxy models for clients, we concur with the RTF judgment and recommend that the Commission accept the recommendation that current hypothetical cost proxy models are not appropriate for rural carriers because the proxy model results do not result in reliable approximations for rural carriers' costs.[2]

Based on both the RTF Recommendation and the Joint-Board Recommended Decision, it is clear that the recommendations before the Commission are transitory.[3] Even before the Commission considers these recommendations, RTF members have stressed that their recommendations are useful for a transition period of only five years. Because of the transitory nature of the recommendations, JSI urges that the Commission carefully review whether some of the RTF proposals are unnecessary or administratively burdensome for the task of moving toward a "long term universal service plan."[4] JSI believes that, in some instances, the RTF recommendations resemble sandcastles built at low tide. The elaborate construction of these recommendations would seem disproportionate with the reality that all will be washed away after the designated transition period.

In light of this observation, JSI recommends that the Commission retain the foundation of the RTF recommendation - the continued use of actual embedded cost to determine the level of support. JSI also recommends that the Commission streamline other RTF recommendations that likely will lead to insufficient funding for rural universal service purposes or will not be competitively neutral.

Further, JSI suggests other technical adjustments to the RTF recommendations, including that disaggregation filing deadlines be extended to one year after the date of an order implementing disaggregation. Lastly, JSI recommends that the Commission adopt an embedded cost methodology to determine the level of any implicit universal service support extant in the interstate access system.

II. JSI DOUBTS WHETHER CERTAIN PORTIONS OF THE RTF PLAN MEET THE SUFFICIENCY REQUIREMENT OF THE ACT

Critical to the adoption of any federal universal service program is that it meets the statutory requirements imposed by Congress. Congress specifically requires that the Joint Board and the Commission shall base policies for the preservation and advancement of universal service on the principle that there should be specific, predictable, and sufficient Federal and State mechanisms to preserve and advance universal service.[5] JSI has concerns about whether certain RTF recommendations meet the sufficiency requirement of this congressional mandate. In addition to the statutory requirement that federal universal service be sufficient, the Commission has adopted principles for federal universal service that suggest that sufficient support for universal service is in the public interest and is sound public policy.[6] The RTF itself declares that it "attempts to provide" sufficient support but makes no guarantee or assurance that its attempt meets the sufficiency threshold established by Congress.[7]

In addressing the comments that suggest that the RTF Recommendation would provide insufficient support, the Joint Board cites that other parties predict that there will be too much support. The Joint Board received comments on the RTF recommendation prior to making its Recommended Decision that suggest that the RTF framework will lead to insufficient support levels for rural carriers. Notably absent in the Joint Board Recommended Decision is the determination that the RTF recommendations are sufficient for federal universal service purposes. The Joint Board merely concludes that it believes "that the nature of these comments is consistent with a recommendation that is a consensus proposal put forth by representatives of disparate interests."[8]

We certainly respect the disparate interests in the telecommunications industry and, in most cases, applaud the process of consensus to mitigate these interests. However, when statutory and public policy requirements dictate that support be sufficient, we believe that the process of compromise must include a determination that the compromise decision is sufficient. We fail to see any determination by the Joint Board that finds the RTF recommendations sufficient. We also see instances where the RTF Recommendation itself fails to address the sufficiency of universal service support. In some instances, it appears to JSI that the RTF split the proverbial baby when dealing with sufficiency - a statutory requirement - on one hand, and affordability of the federal high cost universal service program on the other hand.[9]

We believe there are four areas of the RTF Recommendation that need to be modified in order to ensure sufficient support for rural universal service purposes. We address these areas in greater detail and recommend streamlined alternatives that satisfy the Commission's duties and provide sufficient universal service support in the RTF's five-year planning horizon.

JSI observes that many RTF recommendations are aimed at establishing structural safeguards to prevent "waste, windfalls, and excessive expense for contributing carriers and their customers."[10] JSI submits that attempts to establish these structural safeguards are unnecessary because they duplicate a statutory requirement and existing Commission policies that provide a safeguard for public funds used for universal service. Section 254(e) requires that funds only be used for their federally designated purposes. The Commission has established its process whereby non-rural carriers receiving funds must demonstrate that these funds are used appropriately.[11] Since these safeguards are already in place for non-rural carriers, and are recommended for rural carriers by the RTF, it appears to JSI that many RTF recommendations are duplicative and unnecessary.[12]

A. The existing caps and proposed RTF modifications to caps and limitations on High Cost Loop ("HCL") support impede sufficient support and should be eliminated.

The RTF recommends that the existing caps on HCL support be revised because current funding limitations prevent sufficient support.[13] The RTF has computed the level of current insufficient support at $118.5 million. JSI agrees with the RTF that the existing caps and limitations on HCL support impede individual carriers in their deployment of additional and replacement infrastructure in rural areas. Because of these funding limitations, it is becoming increasingly difficult to improve, renew, and expand infrastructure necessary for providing existing universal service. However, JSI does not agree with the RTF that upgrading the cap will provide sufficient support. Evidence for JSI's position lies in the fact that any structural cap on the support funds will be a barrier to investment and will lead to insufficient support because individual rural carriers will be uncertain whether they will receive predictable and sufficient support for new investment within the five-year period.

The RTF attempts to resolve this dilemma with a litany of elaborate safeguards. First is the use of a rural growth factor ("RGF"). The RGF is the sum of the GDP-PI and the annualized growth rate in <u>national</u> access lines. The RGF is used to establish the HCL funding cap. It is also used to adjust the HCL per line frozen support in areas where there is competition among eligible telecommunications carriers ("ETCs"). JSI observes that there is no guarantee of sufficiency using a national growth rate in rural areas that can experience wide variances in individual growth rates. JSI also notes that the current HCL fund has an indexed cap that has resulted in an insufficient support level as shown by the RTF.[14]

JSI submits that the motivation for capping the HCL only for incumbent rural carriers is unclear and undocumented. The RTF fails to define its motivation to adjust the base of the HCL cap rather than remove the HCL cap altogether. Given the state certification safeguards proposed by the RTF, JSI recommends that the HCL cap for incumbent rural carriers be eliminated.

JSI observes that the proposed HCL cap is only for incumbent rural carriers. The HCL support received by CLECs in areas served by rural incumbent carriers is not capped. There is no public policy discussion in the RTF Recommendation why one class of ETC is treated differently from another. In light of these observations, JSI recommends that the Commission remove all HCL caps for all carriers. The removal of the HCL caps with the imposition of state certification requirements that funds are properly used is administratively efficient and ensures that federal universal service support is sufficient to meet public policy objectives.

B. The safety net does not ensure sufficiency, is duplicative and unnecessary.

After adopting an artificial HCL cap for ILECs, the RTF Recommendation adds byzantine safety-net regulations in an attempt to shore up its claim that HCL support is sufficient. JSI submits that the RTF Recommendation fails to demonstrate that the safety net is necessary or sufficient. First, the reason for a safety net is because the prior recommendation limits HCL support at an insufficient level. Without a cap on HCL for ILECs, there would be no need for a safety-net provision. JSI favors the elimination of the safety net in conjunction with the removal of all HCL funding caps. In the interest of a streamlined regulation for the five years of this program, JSI strongly recommends that the Commission remove HCL funding caps for incumbent carriers and allow state commissions to ensure that funding support is used for the purposes for which the support is intended.

JSI's examination of the RTF safety-net justification reveals several holes in reasoning. First, there is little or no defense of the 14 percent growth factor used as a safety-net qualifying threshold. The RTF states that the 14 percent was chosen because it is double the RGF in recent years. The RTF did not demonstrate that 14 percent provides sufficiency of support for incumbent carriers whose support is capped. JSI contends that the arbitrary nature of the 14 percent threshold is insufficient and provides no guarantee that the five-year RTF program will meet public policy objectives. For example, without a sound empirical foundation for the 14 percent, JSI is concerned with ILECs whose Total Plant in Service ("TPIS") grows at 1.5 times the RGF, or, in the extreme, where TPIS growth is 13 percent. Does such an ILEC have sufficient support under the RTF Recommendation? JSI submits that the RTF would not be able to determine whether support is sufficient for this carrier. The only mechanism established to determine sufficient support is under the Commission's state certification requirement in which the rural carrier submits its support need to the Universal Service Administrative Company and the state commission determines that the support is used for the purposes to which the support is intended. The second hole in reasoning observed by JSI is the use of 50 percent of the difference between the capped level and the uncapped level. As with the 14 percent figure, there is no determination by the RTF that this level of support is sufficient. Based on these observations, JSI repeats its recommendation that the Commission remove all HCL caps for ILECs and eliminate the proposed safety-net provisions.

C. The competitive freeze does not ensure sufficiency.

Both the RTF and Joint Board promote the principle that, once a competitive ETC ("CETC") is providing service and receiving support, HCL support for all ETCs in a study area should be frozen on a per-line basis.*15* Because there is no public policy discussion regarding the potential impact of freezing universal service support on a per-line basis on the arrival of a CETC, JSI recommends that the Commission closely examine this RTF recommendation. Specifically, JSI recommends that justification for frozen support be supplied, and thereafter, that the Commission consider using a percentage threshold to determine frozen support on a per-line basis. JSI does not believe that one line reported by a CETC necessarily requires that support be frozen. JSI recommends that the Commission examine whether a 5 percent or 10 percent threshold of access-line market share is better able to identify markets where there is emerging competition that would warrant a freeze of per-line support (assuming that this freeze is in the public interest and conforms to statutory requirements).

Absent a thorough examination of the public policy objective of freezing support, JSI believes that frozen support will not satisfy the sufficiency requirement of Congress. It may be that the frozen support addresses the issue of stranded costs for ILECs. However, since the RTF states explicitly that it was unable to reach a consensus on the issue of stranded cost,*16* JSI doubts that the frozen support concept advocated by the RTF can be justified solely on public policy issues surrounding stranded costs and investment. Without explicit justification of the frozen support provision, JSI questions whether frozen support, as proposed, will lead to sufficient support for universal service.*17* If frozen support is justified outside the ambit of stranded costs, JSI recommends that the Commission use a market-share percentage as the threshold for freezing support rather than the one-line proposal before the Commission.

In a technical matter related to frozen support, JSI notes that the proposed freeze may prevent certain carriers from receiving any federal support they would otherwise receive. JSI understands that if an average schedule carrier receives no federal support and has a CETC operating in its area, upon conversion to cost, according to Commission rules, this carrier would not be eligible to receive any federal support because the support level was frozen at $0.00 prior to conversion. JSI recommends that the Commission remove the freeze or, at minimum, provide for the normal conversion process of average schedule carriers that allows for a cost-based determination of universal service support prior to implementing a freeze.

D. The safety valve does not ensure sufficiency.

JSI supports the removal of the current merger and acquisition cap for rural ILECs. Many acquisitions by rural carriers are for exchanges of price-cap LECs. JSI supports NTCA's recent petition to the Commission to remove Section 54.305 for asset transfers from price cap to rural ILECs.*18* JSI believes it is in the public interest to replace this rule with a rule that "permits acquiring rural carriers to recalculate their per line support based on the average costs of all of their lines would permit rural carriers to complete upgrades and repairs necessary to provide high quality service to the acquired exchanges."*19*

The safety-valve principles promoted by the RTF are best embodied in the removal of the rule as it applies to rural ILECs.

III. JSI RECOMMENDS A MORE STREAMLINED INTERMEDIATE APPROACH TO UNIVERSAL SERVICE THAT UTILIZES EXISTING STATE CERTIFICATION FOR NON-RURAL CARRIERS.

The RTF recommendations for caps and safety nets, competitive freezes and safety valves are not in harmony with other aspects of the plan; for example, the disaggregation proposals that require state commission involvement or self-certification. To bring these principles into harmony, JSI recommends that the Commission streamline the RTF intermediate approach of universal service for rural carriers for the next five years. State commissions play a prominent role in the RTF's recommendation on disaggregation (discussed below) and JSI believes that the mechanisms already in place for state commissions to certify that federal universal service support is used in the manner in which it is intended will provide sufficient support as well as ensure that support will not be wasted or subject to abuse.

It is obvious that interstate service providers do not want universal service support to become too large. This is because these providers and their end-user customers are contributors to the federal universal service program. While seeking to minimize federal support to the extent possible, the size of the federal program still must be sufficient and predictable. JSI believes that reliance on the state commission certification process, for those LECs under state regulation for local service, and the Commission certification process for all other LECs will assure contributors that funds are used properly and for the intended use.

Because the RTF Recommendation is for only a five-year period, JSI believes that there is great benefit to removing the caps and limitations on current federal support programs and allowing the state commissions to certify that federal support is used properly. The benefit is that if, during the five-year period, the federal universal service program works as expected, there will be little need to establish a labyrinth of safety nets and safety valves for the future. The Commission can take one step closer to a more streamlined federal universal service program that addresses the statutory requirements and public policy objectives established for federal universal service while reducing the volume of regulations with which rural carriers must comply to receive support for high-cost areas.

There is no better time to allow state commissions to fulfil their duty according to current FCC regulations. The Commission can have the assurance that if state commissions do not fulfil their requirements, there is a time certain when the process stops. The five-year period will end and, as necessary, alternative mechanisms can be established. However, if the state commissions fulfil their duty in policing the use and designation of universal service funds and recipients, the Commission will be able to count on a collaborative effort with state commissions in future endeavors.

A state certification process also will ensure that CETCs are using funds for universal service purposes. Since CETCs receive funds based on the cost characteristics of the ILEC and not their own costs, there is considerable opportunity for overcompensating CLECs, who usually have larger economies of scope than the rural ILEC in a specific market[20] The state certification process will require CETCs to justify their support and demonstrate that it is being used in a specific geographic area and for universal service. Thus, while the caps and limitations recommended by the RTF are for ILECs, the streamlined process described above provides a check and balance for all ETCs. JSI recommends this approach to the Commission.

IV. JSI RECOMMENDS SEVERAL TECHNICAL CHANGES TO RTF RECOMMENDATIONS

A. JSI seeks clarification and recommends changes to the disaggregation timeline.

JSI seeks clarification on the mechanics of the RTF Recommendation that requires the disaggregation of support for all forms of current explicit universal service support: HCL, LTS, and LSS. JSI is unclear as to whether the RTF proposal of a per-line freeze for incumbent support applies only to the HCL fund. However, the disaggregated support proposal appears to include more than the HCL fund. This disparity needs clarification.

JSI further understands that the RTF proposal requires "support per line for each category of support" be determined and adjusted when total annual support amounts change[21] Within the RTF proposal, JSI fails to understand the need to have a different method or rationale for each of the three support mechanisms (a possible fourth mechanism is also recommended by the RTF, as the HCF III) within a single disaggregation plan. Thus, JSI seeks clarification and justification for the proposed process that may require extensive analysis and administrative effort to develop and maintain annual adjustments to disaggregated support zones.

The RTF recommends a 270-day timeframe for filing disaggregation plans with state commissions. JSI recommends that this nine-month timeframe be extended to one year from the publication of any rules requiring a disaggregated plan. While the extension of three months will not materially affect the objectives of the proposal, JSI believes that the extra three months will facilitate developing consensus among individual carriers that may wish to collaborate with other carriers in a particular state - thereby easing the state commission review process required when choosing certain path options.

B. Wireless CETCs should be required to use billing address to determine level of support.

The RTF recommended that the Commission examine how disaggregated support should be assigned to a wireless user. The problem with wireless service is that there is no specific location and, hence, it is arbitrary to determine a location for disaggregated support. While there are several likely solutions to this problem, JSI recommends that the billing address for the wireless account be used as the "fixed address" for which support is determined.

The public policy objective for this proposal is to ensure that federal support will be used properly by wireless CETCs. When these CETCs seek certification from state commissions for federal support, they will be able to use a definite location to determine the amount of disaggregated support they are eligible to receive[22] Use of the billing address is the most administratively tractable solution for the problem of defining a "fixed address" for service using a mobile station.

C. JSI recommends that the Commission provide specific guidelines to state commissions on determining whether federal universal service support is used for the purposes for which it is intended.

Within the RTF Recommendation, state commissions will play a role in determining whether federal funds are used for their intended purpose. JSI recommends that the Commission streamline several portions of the RTF Recommendation because it believes that these portions are either unnecessary or redundant. JSI recommends that the Commission use the existing price-cap carrier procedure that delegates oversight responsibility to state commissions. JSI recommends that the Commission consider developing guidelines to assist state commissions in determining whether or not federal funds are use in the manner intended. JSI suggests that the Commission may delegate the development of guidelines to the Joint Board on Universal Service. The purpose would be to develop a set of guidelines or best practices that could be used by state commissions in making their determinations.

V. JSI RECOMMENDS USING EMBEDDED COST METHODOLOGY TO DETERMINE ANY IMPLICIT SUPPORT IN CURRENT INTERSTATE ACCESS RATES

The RTF Recommendation provides general guidelines for the Commission to determine the existence and amount of universal service support implicit in current interstate access rates. JSI observes that these guidelines are very general and do not give the Commission a foundation upon which to judge the level of implicit support existing in current access rates. In prior orders, the Commission has moved Long Term Support to an explicit universal service program from the interstate access program[23] Moving LTS to the universal service program from the access rate structure eliminated a large portion of the implicit support then extant in interstate access rates. JSI believes that any remaining residual implicit support, after removal of LTS, is largely reflected in the use of an interstate subscriber plant factor ("SPF") of 25 percent instead of a subscriber line usage ("SLU")-determined rate based on interstate usage.

JSI recommends that the Commission continue to use its embedded cost methodology to determine the level of support implicit in current interstate access rates. Suggestions to use a hypothetical model or, simply, to choose arbitrarily a rate that "represents" the access cost for rural carriers and the level of implicit support for these carriers does not provide assurances that the actual costs of rural carriers to provide interstate access service is accurately represented. This would lead possibly to the scenario where interstate access service is supported within a universal service fund program. JSI does not believe that interstate long-distance service is a service qualifying as a universal service.[24]

We further believe that, to the extent possible, the access rate structure should mirror the manner in which costs are incurred. However, we do not suggest that interexchange carriers should be able to shed their shared-cost portion of the common line loop costs. It is undisputed that interexchange carriers use, as part of their retail service to end-user customers, the loop connection to the public switched network. JSI agrees that, to the extent possible, the IXCs' portion of this cost should be aligned to the manner in which these costs are incurred. This suggests that IXCs should pay for their share of non-traffic-sensitive costs on a non-traffic-sensitive basis. JSI recommends that the Commission reject any attempts of IXCs to shed these costs.

VI. JSI RECOMMENDATIONS

In summary, JSI recommends the following:

- Remove all caps and limitations on current HCL support.
- Do not implement RTF caps and limitations on federal support.
- Do not impose a competitive freeze on per-line support. In the alternative, and after justification of a freeze policy, use a market-share threshold of 5 percent or 10 percent of access lines before imposing a freeze.
- Instead of safety-net and safety-valve regulation, utilize the existing state certification process for rural carriers.
- Clarify the disaggregated support method and allow for one year to file disaggregation plans with the appropriate regulatory authority.
- Require that wireless CETCs use the billing address for an account as the "fixed location" for disaggregating support for end-user customers using mobile stations.
- Provide specific guidelines to state commissions so that they may use them in determining whether federal support is used in the manner intended.
- Use an embedded cost methodology to determine the level of implicit support in rural carrier interstate access rates.

VII. CONCLUSION

JSI recommends that the Commission adopt the foundation of the RTF proposal and streamline various aspects of the RTF Recommendation for the five-year interim period. JSI also recommends several changes and clarifications as outlined above. Lastly, JSI encourages the FCC to use an embedded cost methodology to determine the level of implicit support in current interstate access rates.

Respectfully submitted,

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Footnotes

1 In the Matter of *Federal-State Joint Board on Universal Service*, Further Notice of Proposed Rulemaking, FCC 01-8, rel. January 12, 2001.

2 The Joint Board has suggested that next year it will begin again to prepare a long-term program for universal service.

3 Joint Board Recommended Decision, FCC 00J-4, at paras 5 and 21. RTF Recommendation, page 4.

4 Joint Board Recommended Decision, at 21.

5 47 U.S.C. § 254(b)(5).

6 In the Matter of *Federal-State Joint Board on Universal Service*, 12 FCC Rcd 8776 (May 8, 1997).

7 RTF Recommendation, page 15.

8 Joint-Board Recommended Decision, ¶12.

9 It appears that the RTF principle of affordability, cited on page 16 of its recommendation, has been commingled with an unstated principle of minimizing the size of federal universal service funds. JSI believes that the RTF has sacrificed the guarantee of sufficiency in order to minimize the federal universal service program and to keep the program "affordable" for fund contributors rather than keep universal service affordable for universal service end-users.

10 RTF Recommendation, page 8.

11 47 CFR 54.313.

12 RTF Recommendation, page 4.

13 RTF Recommendation, page 24.

14 RTF documents at minimum a $118.5 million shortfall in sufficient support.

15 The RTF Recommendation is unclear as to whether or not its freeze applies to all federal rural universal service support programs (Local Switching Support ("LSS"), Long Term Support ("LTS") and HCL support) or whether its recommendation applies only to HCL support.

16 RTF Recommendation, page 39.

17 It may be that the RTF was overly concerned with the "affordability" of the federal universal service program when it made this recommendation. JSI believes that when a CETC receives universal service in a study area there is the likelihood for an increase in universal service support for this study area. The remedy chosen by the RTF was to limit or cap the incumbent's support while allowing the CETC to receive support not based on its costs of providing service.

18 Comments of the National Telephone Cooperative Association, CC Docket No. 96-45, FCC 00-428, January 17, 2001.

19 *Id*., page 2.

20 On page two of the Joint-Board Recommended Decision, the Joint-Board recognizes that rural LECs do not exhibit large economies of scale and scope. Alternatively, CETCs serving rural areas may exhibit large economies of scale and scope, especially if these CETCs currently serve upwards to 14 states. The cost characteristic of these two distinct types of ETCs leads to potential windfalls for CETCs.

21 RTF Recommendation, page 34.

22 Some wireless CETCs will object to the principle that they must seek state certification for federal universal service support. With the exception of Wyoming, the only state we know of that has a statutory prohibition for examining service using wireless spectrum, JSI believes that state certification for receiving ETC designation and state certification for certifying that funds are used properly go together.

23 LTS provides cost recovery to common line costs above a predetermined level. Since these costs are exclusive to common line cost recovery, the Commission determined that these costs fall under the ambit of "access to interexchange service," which is included in the Commission's definition of universal service.

24 Interstate long-distance service is different from "access to interexchange service." The latter is identified as a universal service supported by the federal universal service program. The former includes end office switching costs, transport costs as well as a shared-cost portion of the local loop.