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BEFORE THE ARIZONA CORPORATION COMMISSION

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Arizona Corporation Commission
DOCKETED

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IN THE MATTER OF THE REVIEW AND POSSIBLE REVISION OF ARIZONA UNIVERSAL SERVICE FUND RULES, ARTICLE 12 OF THE ARIZONA ADMINISTRATIVE CODE.

DOCKET NO. RT-00000H-97-0137

QWEST CORPORATION'S NOTICE OF FILING ITS SECOND SET OF COMMENTS ON THE POSSIBLE REVISION OF ARIZONA UNIVERSAL SERVICE FUND RULES

In response to Director Ernest G. Johnson's December 24, 2001 memorandum seeking comments on the reply comments filed by the other parties in response to Acting Director Steven Olea's September 20, 2001 memorandum, Qwest Corporation ("Qwest") hereby provides notice of filing its attached comments.

Respectfully submitted this 23rd day of January, 2002.

RESPECTFULLY SUBMITTED,

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QWEST CORPORATION'S SECOND SET OF COMMENTS ON THE COMMISSION'S QUESTIONS RELATED TO THE POSSIBLE REVISION OF THE ARIZONA UNIVERSAL SERVICE FUND RULES

Qwest Corporation's ("Qwest") November 2, 2001 comments primarily responded to the Arizona Corporation Commission Staff's ("Staff") questions on unserved and under-served areas. Qwest's comments were not meant to address all aspects of the Arizona Universal Service Fund ("AUSF") rules. Some of the participants raised surcharge assessment and methodology aspects of the AUSF rules in their responses to the questions posed by Staff. Qwest believes that these, too, are important aspects of the AUSF rules. Qwest looks forward to providing information to the Arizona Corporation Commission ("Commission") in future workshops on (i) the importance of a good fund design, (ii) the revenues the Commission should consider in the assessment, (iii) the AUSF reporting requirements, and (iv) the need to equally treat various classes of carriers serving high-cost customers. Further, Staff is currently looking into issues relating to access charges. Although Qwest believes that AUSF rules should be addressed separately, it understands that particular issues, such as access charges, are interrelated and must be considered as the docket moves forward.

Qwest has general comments in response to other participants. Qwest agrees with Residential Utility Consumer Office's ("RUCO") comment that taking positions on some of the issues raised in Staff's letter may be premature. As RUCO states, without more economic, demographic, fiscal, and cost/benefit information, the desirability and feasibility of various alternatives is difficult to determine. Qwest looks forward to the opportunity to further discuss information provided during the upcoming workshops.

As stated in Section 254(b) of the 1996 Telecommunications Act, one of the principles of universal service is to ensure everyone has access to basic local exchange telephone service at reasonable and affordable rates, regardless of location. Qwest is fully supportive of the goals of universal service and believes that the achievement of universal service can only be realized when the Commission creates a competitively and technologically neutral universal service fund.

Following are Qwest's comments on other participants' responses to each of the questions posed by Staff.

1. **Are there areas within the existing rules where revisions should be made? If yes, please provide specific language recommendations and explain the benefit of the recommended revision.**

Most commenters agreed that the rules should not require a carrier to make a rate case filing in order to receive AUSF funds. To make this revision, Qwest proposes that Arizona Administrative Code ("A.A.C.") R14-2-1203 be amended to read as follows:

> R14-2-1203. Request for AUSF Support.
> Eligibility for AUSF support is contingent upon a carrier being designated as an eligible telecommunications carrier ("ETC"). An ETC must make a need based application to the Commission requesting AUSF support and the ETC shall submit a revenue neutral filing offsetting implicit support with explicit support from the fund. Any need for support from the AUSF must be reduced by the amount of federal high cost support received by that carrier in Arizona. The ETC must be in compliance with all applicable rules set forth in R14-2-1101 through R14-2-1115. The Commission shall determine the appropriate cost of providing basic local exchange service and the carrier shall receive no more support than the difference of the cost and the affordability benchmark.

Additionally, many commenters agreed, either explicitly or implicitly, that the rules should be competitively and technologically neutral. AUSF support should not be limited solely to wireline providers. It should be portable.

As set forth earlier, Qwest believes that prior to further examining specific issues and suggestions related to the costs of support and calculation of AUSF support, the Commission may need to examine additional information for consideration in future proceedings.

2. **How might the AUSF rules be amended to ensure the availability of wireline telephone service in unserved areas (open territory)? Please provide specific recommendations on issues such as required population density before service to an area must be provided, the method for determining the serving carrier, the procedural process, etc.**

Qwest agrees with the commenters that propose competitive and technological neutrality as a means to achieving increased availability of basic service to unserved areas. Qwest stated in its November 2, 2001 comments that in Arizona no area is without a certificated carrier. When Qwest uses the term "unserved area" or "open territory," it means an area that is without an ETC.

Any rules adopted to promote the expansion of service must:

1) Encourage the construction of the most efficient technology: As recognized by Midvale in their comments, "As technology changes, equipment costs vary, making for a different business case in different areas...." RUCO correctly noted that the FCC does not restrict ETC status to merely wireline providers (page 3); and
2) Provide full, up-front recovery for construction charges, through a combination of the AUSF support and the end users.

The comments make clear that this is a complex issue and more input is required. Based upon the limited comments provided on this issue, Qwest believes that Verizon Wireless' suggestion has merit: that the Commission act on an area-by-area basis in response to petitions from individuals. A change made today in the rules to establish the framework for the process to examine the need for service will help serve as a guide, but Qwest does not believe that unserved area issues can be resolved without some Commission proceeding.

Table Top Telephone Company ("Table Top"), at page 2, recognized that "there are usually good reasons why telecommunications service is not available in this unserved territory." Qwest believes that the reason has to do with financial considerations undertaken by any entity: will a decision to expand service provide a carrier with a reasonable opportunity to make a profit? If not, there will be no carriers willing to serve.

Adoption of a bidding procedure as proposed by Qwest in its November 2, 2001 comments, with guaranteed, full up-front cost recovery, will serve as an initial framework to guide in achieving the goal of making basic local exchange telephone service available to all within the State of Arizona. To address the concerns voiced by AT&T, Qwest proposes that the bidding process would only be used in "open territory," those areas not currently served by an ETC.

3. How might the AUSF rules be amended to increase the availability or affordability of wireline telephone service in under-served areas? Under-served areas are defined as areas within a wireline carrier's service territory where construction or line extension charges apply.

As stated in its November 2, 2001 comments, Qwest recommends that prior to addressing concerns related to under-served areas, the Commission needs to clarify the definitions of unserved and under-served areas. Cox Communications had a similar comment. Qwest agrees with the other participants that suggest the rules should be technologically and competitively neutral.

Other participants also suggested that the AUSF be used to subsidize service to under-served areas. Qwest agrees that there are circumstances where the costs of new service in an ETC's service area may be prohibitive, from the end-user perspective. In limited cases, as set by some Commission-determined trigger, Qwest believes it would be appropriate to use AUSF one-time distributions to defray construction charges. Qwest does not agree with WorldCom that AUSF funds should be used solely to support the recurring costs of providing service. Due to prohibitively high construction charges some customers may face, the Commission may determine it is in the public interest to use support to assist in promoting the widespread availability of basic service.

WorldCom suggests that use of AUSF "to supplement" construction or line extension charges will overcompensate ILECs. Regardless of whether customer compensation comes from AUSF or line extension/construction charges, it is excluded from the carrier's rate base. Line extension charges are not revenue; they are treated as contributions in aid of construction and are excluded from the rate base for all traditionally regulated carriers, including ILECs. Thus, existing rates for such companies are lower than they would have been if the line extension costs had been included in the rate base. It is precisely because line extension charges to recover the construction cost are perceived as high by the outlying potential customers that there is an issue regarding the use of universal service to connect such customers to the network.

Table Top has proposed a rule regarding an AUSF program for under-served territories. Qwest recommends that prior to assessing this proposed rule, the Commission first develop economic, demographic, fiscal, and other cost/benefit information before developing specific criteria for calculating the amount of AUSF funds that should be provided in under-served areas. If a support mechanism is adopted to offset high construction charges, it will be critical to examine the opportunities for misuse or abuse of the support mechanism.

4. Under what circumstances, if any, could AUSF be made available to carriers that do not have Eligible Telecommunications Carrier status?

The almost universal response from the participants was that a carrier must have Eligible Telecommunications Carrier ("ETC") status prior to receiving AUSF funds. Receiving support from a customer-funded support system demands certain checks and balances. Along with receiving the benefits of receiving support, carriers must be held to certain standards, such as the obligation to serve all requesting customers throughout the service area in which a carrier is designated as an ETC. Regardless of (i) the carrier, (ii) the technology used to provide service, or (iii) the high cost area being served, these standards should not waver.

Qwest recognizes the distinction between a company's authority to decide as a business question the geographic area in which it is willing to hold itself out to serve, and the Commission's authority to designate a service area for an ETC under § 214(e)(2) of the 1996 Telecommunications Act. If a company, for business reasons, cannot accept the service area involved in its ETC designation, there is nothing in § 214(e)(2) to override that business decision; the impact is simply that the company would be ineligible for AUSF distributions that it otherwise could receive.

5. Should the definition of local exchange service, for AUSF purposes, be broadened to include other services? If yes, how might it be accomplished?

The majority of participants responded that the basic local exchange telephone services should not be expanded. Expanding the definition of core services to include advanced services would dramatically increase the size of the universal service program and, thus, increase the cost of telecommunications services for all. Moreover, it is not at all clear that this would be an efficient use of universal service funds. In many rural areas, there may be more economical means of providing advanced services and attempts to expand the definition of the supported services may very well impede the advancement of the competitive market.

6. Are there USF rules in other states that should be adopted in Arizona? If yes, please provide the specific language for each rule and explain the benefit that would be derived by adopting the rule in Arizona.

Although other participants did suggest that rules in other states might be appropriate in Arizona, no complete program adopted in another state should be adopted in Arizona. Arizona faces unique challenges regarding universal service, including both the limitations imposed by the state's Constitution and the large amount of unserved and under-served territory in the state. Some states have proposed rules with general principles that may be appropriate in Arizona, such as the rule proposed by Utah's Assistant Attorney General for the Division of Public Utilities that allows a customer to apply for a one-time distribution from the universal service fund. However, prior to the adoption of these rules, the Commission should compile economic, demographic, fiscal, and cost/benefit information concerning any revisions to the AUSF rules.

7. **How might construction or line extension tariffs be standardized between companies? Should there be an AUSF contribution in addition to the company contribution? Should there be a maximum amount a customer should be expected to pay to obtain service? Should this amount consider the median household income of the area being served? Assuming there is an AUSF contribution, what is a reasonable limit?**

If the Commission imposes the consideration of tariffs in under-served area support calculations, then it should standardize the construction and line extension tariffs so that each carrier contributes the same amount. If the tariffs are not standardized, certain carriers are required to bear more costs than other carriers and some customers may be required to bear more costs than other customers do. For instance, if two customers are located next door to each other but have different carriers, those customers could pay very different construction charges.

Prior to determining the maximum amount a customer should be required to pay or the "reasonable" AUSF contribution, the Commission should have more economic, fiscal, and demographic information regarding the particular area in question. The Commission can use this information to determine if it should use particular factors, such as median household income, whether an area includes primary residences or vacation homes, estimated construction costs, and whether the customer is in an unserved or under-served area, to establish the maximum amount a customer should pay.

8. **Are there changes in the Federal USF rules of which Staff should be aware? If yes, please identify them. How do these changes impact current AUSF rules? How might they impact recommended revisions to the existing rules?**

9. **Are there changes in other Federal rules that might impact current or future AUSF rules? If yes, please identify them and their potential impact.**

10. **For all other comments please provide a narrative fully explaining the issue being discussed, any recommendation and the benefit to be gained if the recommendation is adopted.**

Since the responses to these questions were similar, Qwest is responding to the participants' comments related to these questions as a whole.

We believe that unserved and under-served areas should be the focus of this proceeding and the recommended revisions to the universal service fund rules. Establishing a focus and scope to this proceeding will make the proposed changes more manageable. But we cannot ignore the access reform docket because the two dockets are inherently connected.

Access charge reform alone is insufficient to resolve all the issues. To remove implicit support inherent in access rates, below-cost local exchange rates should first be rate-rebalanced.

Although universal service funding is an issue to be considered, the concept of universal service is that everyone should have access to basic local exchange telephone service at affordable rates. Although universal service funds create support to offset the high cost of providing service in high cost areas, the fund is not intended to constrain all basic exchange rates. If rebalancing of local exchange rates to offset decreases in access charges results in higher rates for local exchange service rates that the Commission deems unaffordable, then

AUSF support may be contemplated to offset these higher rates.

Qwest does not believe that the access issues and the universal service fund must be reformed simultaneously, but the potential impacts of the access reform proceeding on the state universal service fund should not be ignored. Furthermore, any reform efforts must be competitively and technologically neutral.

Table Top argues that all AUSF support received related to rural service areas shall be applied to projects related to rural service areas, as opposed to urban service areas. Qwest notes that for any company except one that serves only rural areas, this requirement assumes the ability to trace the dollars received from the AUSF to specific expenditures for projects that would relate only to rural service areas. Funds received by a carrier from the AUSF would be classified as revenue for accounting purposes. Qwest submits that conventional accounting theory indicates that it is not possible to trace specific dollars of revenue to specific expenditures within an accounting unit, and so this requirement would have the practical effect of disqualifying any carrier that served urban as well as rural service areas from any AUSF funds. This would clearly be inequitable. Ensuring that rural service areas receive the benefit of AUSF disbursements could be satisfied by a sources and uses of funds analysis.

Qwest agrees with ALECA's statement at page 9 that the Commission should carefully examine each ETC request and find it in the public interest to designate another ETC. ETC status is an important responsibility – there are burdens with the benefits. Most importantly, the Commission should hold the same standards to all ETCs, whether that is an ILEC, a CLEC, or a wireless carrier.

Qwest also acknowledges ALECA's comment at page 9 that changes to federal funding may impact a carrier's need for AUSF funding. In A.A.C. R14-2-1202(A), the Commission has addressed the method by which support from federal sources affects the amount of AUSF support. This provision states "The amount of AUSF support to which a provider of basic local exchange telephone service is eligible for a given AUSF support area shall be based upon the difference between the benchmark rates for basic local exchange telephone service provided by the carrier and the appropriate cost to provide basic local exchange telephone service as determined by the Commission, net of any universal support from federal sources." A.A.C. R14-2-1202(A). The Commission has determined that this is the best mechanism to calculate AUSF support and Qwest believes this should not be changed.

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