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November 2, 2001

Arizona Corporation Commission
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Steven M. Olea, Assistant Director
Utilities Division
ARIZONA CORPORATION COMMISSION
1200 West Washington
Phoenix, Arizona 85007

Re: ***Review and Possible Revision of Arizona Universal Service Fund Rules, Article 12 of the Arizona Administrative Code (Docket No. RT-00000H-97-0137)***

Dear Steve:

In response to your memorandum dated September 20, 2001, regarding the above-referenced topic, attached are the responses of my client Western Wireless Corporation to the questions listed in Exhibit "A" to the memo. By copy of this letter to Sonn Ahlbrecht, I am requesting that I be placed on the formal service list in this docket.

Very truly yours,

SNELL & WILMER

Jeffrey W. Crockett

JWC:gdb
Enclosures
cc with enclosures:
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Gene Dejordy, General Counsel, Western Wireless Corporation
Suzie Rao, Regulatory Counsel, Western Wireless Corporation

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Comments of Western Wireless Corporation Regarding the Review and Possible Revision of Arizona Universal Service Fund Rules, Article 12 of the Arizona Administrative Code

Docket No. RT-00000-H-97-0137

Set forth below are the responses of Western Wireless Corporation ("Western Wireless" or the "Company") to the ten questions set forth in Exhibit "A" to the Memorandum of Steve Olea dated September 20, 2001, in Docket No. RT-00000H-97-0137.

Q-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.

A. Yes, the Arizona Universal Service Fund ("AUSF") rules should be amended and clarified in a number of sections throughout Article 12. While the Arizona Corporation Commission (the "Commission") has envisioned that competitive carriers (including wireless) are eligible to receive distribution from the AUSF, Western Wireless recommends that the rules be further refined.

Specifically, under R14-2-1202, "Calculation of Support," there is no mention of how AUSF support shall be calculated for competitive carriers. Support should be portable to all competitive carriers as envisioned in Section 254 of the Federal Telecommunications Act of 1996 (the "Federal Act"), and as specified in Federal Communications Commission ("FCC") implementing regulations. Any state universal service mechanism that does not provide for portability of support would run afoul of Section 253, which requires the implementation of competitively neutral universal service mechanisms. A state universal service support mechanism that makes only incumbent local exchange carriers ("ILECs") eligible for explicit support would effectively lower the price of ILEC-provisioned services by an amount equivalent to the amount of support provided to ILECs that is not available to their competitors.

As a result, non ILEC competitive eligible telecommunications carriers ("ETCs") such as Western Wireless would be left with two choices – either match the ILEC's price charged to the customer, even if it means serving the customer at a loss to the Company, or offer the service to the customer at a less competitive price based on the unsubsidized cost of providing such service. A mechanism that provides support to ILECs while denying funds to eligible prospective competitors would effectively foreclose a competitive carrier from the universal service market. The FCC specifically recognized that it is unreasonable to expect an unsupported carrier to enter a high-cost market and provide a service that its competitor already provides at a substantially supported price.

The proposed rules should be revised to make explicit that carriers eligible to receive AUSF include both ILEC ETCs and competitive ETCs. The changes recommended by Western Wireless will open the doors to competitive entry by carriers who can provide alternative choices, better services, and lower costs.

Western Wireless has produced a document entitled "Model Universal Service Rules," which it can share with the Commission and Staff upon request.

Q-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, procedural process, etc.

A. Any Commission policies of providing telephone service to unserved areas should include the policy of allowing competitive carriers who have been designated an ETC (such as wireless) to serve customers in these uncertificated or unserved areas. In many cases, wireless local loop is the least-cost and most efficient method of providing telephone service.

Q-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.

A. The Commission should address the policy of increasing phone service to under-served areas by factoring in the presence of wireless and other types of telecommunications service. The old monopoly regime, where the ILEC was the only telecommunications provider, no longer holds true in today's competitive marketplace. Today, wireless carriers that are ETCs can provision basic service to consumers in under-served areas. Many times, the wireless carrier can provide service more efficiently. Thus, by establishing a competitive universal service market, the commission will enable the forces of competition to squelch many of the unfriendly consumer practices by the ILECs, such as exorbitant construction or line extension charges.

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

A. Western Wireless believes that AUSF support should be made available only to carriers that have ETC status. This is not to state that the ETC eligibility criteria should be so onerous as to prevent competitive carriers from seeking and receiving ETC designation. For designation purposes, the Commission should follow the requirements set forth in the Federal Act under Section 214(e). Section 214(e) provides specific, exclusive requirements for ETC designation, namely that a carrier be a common carrier; provision a base set of supported services established by the FCC; advertise the availability of the services and charges; and provision the supported services throughout a designated service area. Additionally, in rural telephone company study areas, there must be a finding that an additional ETC designation is in the public interest. Once designated by a state commission, the ETC (competitive and ILEC alike) is eligible to receive state and federal universal service support.

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

A. No. Although Western Wireless supports the goal of connecting consumers to the Internet and facilitating the provisioning of high-speed data services, this goal should not be accomplished through additional funding of universal service support mechanisms.

The definition of basic local services should not be broadened to include other services such as advanced services. Western Wireless believes that the introduction of competition to the market for basic local telephone service is the most effective manner in which to expand the service offerings available at reasonable rates to customers in rural, high-cost areas. By way of example, it was the threatened entry of competitive local exchange carriers ("CLECs") that forced the incumbent providers to offer DSL services in urban areas. Wireless technology today can support high-speed data services. The entry of competitive basic local service carriers such as Western Wireless will incent competitors and incumbents to introduce new and innovative services such as advanced telecommunications services.

Q-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.

A. Yes. Many state funds adhere to the following three concepts: (1) competitively neutral fund; (2) explicit rather than implicit support; and (3) portability. For example, the Texas Public Utility Commission expressly adopted these principles when establishing the Texas Universal Service Fund. Specifically, the Texas Commission adopted a forward looking economic cost methodology for the purpose calculating monthly per-line costs of providing basic local telecommunications services and the resulting subsidy available to incumbents and competitors alike. At the federal level, the FCC has also adopted a forward-looking cost methodology for determining costs of service and available universal service support in non-rural telephone company study areas.

Regarding the processing of an applicant's ETC request, many states review applications administratively. Competitive ETCs that are not subject to the jurisdiction of the state should not be required to file for "certificates of public convenience and necessity" or submit tariffs. For example, commercial mobile radio service providers ("CMRS") are not subject to state rate and entry regulation as described in § 332(c)(3)(A) of the Federal Act. Any rules that the Commission adopts regarding ETC eligibility requirements should recognize the regulatory status of CMRS carriers. Western Wireless has been designated an ETC in 13 states and has never been required to file for certificates of pubic convenience and necessity.

Q-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, should there be a reasonable limit?

A. Each wire center is unique, with different funding needs, service issues, carrier issues, etc. In fact, it is probably impossible, in a generic proceeding, to accommodate all of the disparate issues that are unique to each area. That is why Western Wireless recommends that the Commission deal with each area in a separate proceeding. This will allow the Commission to analyze the area-specific issue most efficiently, with the participation of the interested parties and carriers.

The long-standing policy of universal service is to connect customers to the public switched network, therefore, a customer's income level or the median income level of the petitioning area should not be relevant in determining what the petitioning customer must be assessed in order to receive telecommunications service. In this debate, the Commission should focus on what the cost is of providing service to the consumer who happens to reside in an area that is either unserved or underserved. To the extent that there are customers with low-incomes in these areas, then federal and state mechanisms are already in place to subsidize telecommunications service to such consumers. For example, the Federal Lifeline and Link-Up America programs, as well as state assistance programs have been created for qualifying applicants.

Q-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?

A. Yes, there have been numerous changes/modifications in the federal universal service rules that impact state universal service rules. For example, in the recent Federal-State Joint Board on Universal Service, Fourteenth Report and Order, CC Docket No. 96-45, FCC 01-157 (released May 23, 2001) (Hereinafter *Universal Service Order*), requires state commissions to adopt procedures for the disaggregation of rural telephone company's federal universal service support. The *Universal Service Order* also requires state commissions to annually certify that federal high-cost universal service support provided to ETCs is being used consistent with § 254(e) of the Federal Act.

Western Wireless recommends that if the Commission intends to adopt an integrated, functional universal system, then it should also adopt the disaggregation procedures to the AUSF. Furthermore, in order to achieve full implementation of disaggregation reforms, the Commission should make clear in its amendments that the procedures being adopted provide for the disaggregation of the study area as a service area, as well as the disaggregation of universal service support. In other words, if support is going to be targeted more accurately to high-cost wire centers and, possibly zones within wire centers, then the service area of the telephone company – the study area – should disaggregated.

Once a rural LEC's study area is disaggregated, and universal service support is targeted by wire center, or further by zone, then ILECs will be providing service in a manner that more closely resembles their costs, and there will not be averaging across study areas. In conjunction with the disaggregation of support will come the disaggregation of the ILEC's study area. These changes will result in a more favorable environment for competition, and with competition comes benefits to consumers, such as lower pricing and improved and expanded services. Disaggregation will enable competition in high-cost areas where it is being repelled today. For example, under current law and rules, a competitive ETC must make the services available to every individual who resides within the study area of the rural telephone company, which includes all of the exchanges in the state that are served by the rural ILEC. With the disaggregation of the ILEC's study area, however, the competitive carrier will be able to propose a competitive service that more closely matches their own service coverage. In addition, since wireline and wireless service territories are geographically different, it would generally be impossible for either one to compete in the other's service area or service territory if the areas were to stretch across an entire state. Smaller, rather than larger, service area designations for ETCs promote competition and speed deregulation. In sum, disaggregation will encourage competition in rural study areas by eliminating the requirement that competitors enter into a rural ILECs' entire study area. Competition, in turn will provide consumers with better service, more choices of telecommunications service, lower prices, etc.

Q-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.

A. See the answer to question no. 8 above.

Q-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.

A. See "Competitive Universal Service White Paper" attached hereto.

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COMPETITIVE UNIVERSAL SERVICE COALITION

White Paper:
The Road To Competitive Universal Service Reform

July 2001

The Competitive Universal Service Coalition ("CUSC") members include mobile wireless carriers, wireline and wireless Competitive Local Exchange Carriers (CLECs), and industry trade associations. Specifically, CUSC's members are:

Association for Local Telecommunications Services
Competitive Telecommunications Association
Dobson Communications Corporation
Nucentrix Broadband Networks, Inc.
Personal Communications Industry Association
Smith Bagley, Inc.
U.S. Cellular Corporation
Verizon Wireless
VoiceStream Wireless Corporation
Western Wireless Corporation
Wireless Communications Association

White Paper: The Road To Competitive Universal Service Reform

Executive Summary

The Competitive Universal Service Coalition (CUSC) is a group of carriers and associations committed to pro-competitive reform of universal service programs to ensure that consumers in all regions of the country have access to affordable, quality telecommunications and information services.

The Federal Communications Commission (FCC) and some state commissions have made commendable progress toward crafting universal service programs that support the twin goals of universal service and competition. Consumers in some states are now beginning to realize the benefits of a competitive universal service system, but other consumers remain captive customers of the incumbent local exchange carriers (ILECs). Consequently, there is still much work to be done.

This paper discusses the consumer benefits of a competitive universal service system; describes the key regulatory obstacles to achieving full competition in rural areas; and addresses public policies that could solve these problems. Specifically, CUSC urges regulators and legislators to ensure that:

(1) competitive entrants can receive designation as eligible telecommunications carriers (ETCs) expeditiously through a non-discriminatory process, and

(2) all federal and state universal service support mechanisms are explicit and fully portable to competitive entrants.

CUSC is hopeful that by fostering dialogue on issues of critical importance, this paper will help pave the way toward a universal service system that is competitively and technologically neutral, economically efficient, and transparent. The result will be to transform the existing local telephone monopoly into a competitive universal service market that allows consumers in rural, high-cost parts of the country to realize the benefits of local competition for the first time.

CUSC's agenda for pro-competitive universal service reform includes the following action items:

- *Expedite ETC designation*
- *Reform federal universal service funding rules*
- *Reform state universal service funding systems*
- *Structure rural study areas in a manner that facilitates, rather than impedes, competition*

I. The Consumer Benefits of Competitive Universal Service

A. The Benefits of Competition in Rural Areas

Rural Consumers Need Telecommunications Competition. Consumers in rural America value and rely upon telecommunications services as much as, if not more than, urban consumers. And rural communities stand to benefit the most from the economic opportunities made possible by advanced telecommunications and Internet services. But rural consumers today are captive customers of a monopoly local telecommunications service provider; i.e., the ILEC. This market structure impedes the development of new services for telecommunications service consumers, such as advanced services.

Competition Benefits Consumers. Experience in other telecommunications market sectors and throughout the U.S. economy demonstrates that competition benefits consumers. As competition developed in the long-distance and other markets, consumers obtained access to new service options and competitive choices. The benefits resulting from competition are clear:

> **Texas Public Utility Commission:** "[T]he Commission is unwavering in its support of a simple proposition: Rural Texans are not second class citizens and should not be deprived of competitive alternatives or access to new technologies." *PUC Docket No. 22295, October, 2000*

- Introduction of new and innovative services;
- Access to a greater range of service choices, such as expanded calling areas;
- More rapid deployment of technological innovations, including next-generation technology;
- Incentives for the incumbent carrier to upgrade its facilities and improve its customer service;
- Lower rates.

Rural Consumers Are Entitled to The Benefits Of Local Telecommunications Competition. The Telecommunications Act of 1996 was intended to benefit "all Americans by opening all telecommunications markets to competition." Americans in rural areas are entitled to the benefits of competition no less than those in urban areas. In particular, competition for the local telecommunications services included in the definition of "universal service" will have positive effects similar to the effects of competition for other services. These benefits for rural consumers will include: more rapid deployment of advanced technology, a greater array of service offerings, more responsive providers, and more competitive rate levels.

> **Kansas Corporation Commission:** "The clear and unmistakable public policy imperative from both the federal and state legislatures is that competition is a goal, even in rural areas. Arguments have been made that competition is not in the public interest in any rural telephone company service area because it may jeopardize universal service. However, there has been no basis presented for reaching the broad conclusion that competition and universal service are never able to exist together in rural areas. The Commission does not accept the assertion that designating additional ETCs in rural areas will necessarily threaten universal service. The benefits of competition and customer choice are available to Kansans living in non-rural areas. General concerns and speculation are not sufficient justification for adopting a policy that would result in benefits and services that are available to other Kansans not also being available to rural telephone customers." *Order No. 10, May 19, 2000*

B. Case Studies: Competitive Wireless Local Loop in Rural North Dakota and Texas

Benefits of Competitive Entry In Regent, North Dakota. Western Wireless' entry into the rural community of Regent, North Dakota is one example of how rural consumers can benefit from competitive local telephone service. Western Wireless launched its wireless local loop offering, Wireless Residential Service ("WRS"), in Regent in January, 1999. With a population of approximately 200 residents spread out over a large geographical area and an estimated of more than $200.00 per month for local telephone service, Regent is the very definition of a rural, high-cost area.

Western Wireless' New WRS Offering. When Western Wireless entered the Regent market, consumers there had only one choice for local telephone service. At the time, the incumbent carrier offered a rate of approximately $16.00 per month, and a local calling area of Regent and only two other nearby towns. In contrast, Western Wireless offers WRS at a rate of $14.99 per month with a local calling area that includes not only Regent, but also twelve surrounding towns in North Dakota and three towns in South Dakota.

Expanded Local Calling Area. The expanded local calling area offered by Western Wireless has been a significant benefit to Regent's consumers. This allows the residents to place local calls to the only major business/residential community in the area, one of the surrounding towns which is approximately 50 miles from Regent, and a town not included in the incumbent's local calling plan. As of today, although it has not yet received ETC designation for the area, Western Wireless serves approximately 20 percent of households in Regent; a substantial proportion of these households continue to purchase service from the incumbent carrier, and have turned to Western Wireless for their unmet telecommunications needs.

Improvements to the Incumbent Carrier's Service. Western Wireless' entry also caused the incumbent local exchange carrier in Regent to make significant improvements to its retail service offerings. Since Western Wireless' entry into the market, the incumbent carrier has upgraded its facilities to offer new and innovative services, including high-speed Internet access. The incumbent also expanded its local calling area: for customers who also opt for its long distance service, the company now offers a rate of $13.95 per month for an expanded local calling area, plus savings on monthly Internet service.

Rural Texas: New Competitive Universal Service. To date, Texas consumers have benefited the most from a competitive universal service system. Why? Because Texas has taken significant steps towards establishing a competitive universal service system by adopting a non-discriminatory ETC designation process and an explicit, fully portable universal service fund. The result is the fulfillment of the promises of the Telecommunications Act of 1996, specifically that all consumers, including those in rural America, realize the benefits of a competitive local telecommunications market. The proof: in just three months since ETC designation and market entry approval by the state commission, Western Wireless has more than 1500 universal service customers, representing a greater than 10% market penetration.

Competition: A Win-Win Outcome. These case studies show how the entrance of one competitive carrier has benefited the residents of rural communities in North Dakota and Texas. Not only do competitive entrants offer innovative ways to communicate, they also create the incentive for incumbent service providers to lower their prices and broaden their services. The consumers suddenly have choice and innovation and lower prices. There is no evidence that competitive entry adversely affects the incumbent carrier. Instead, it leads to efficient pricing, improved customer service quality, and innovative service offerings for consumers that historically had no choices whatsoever. Indeed, America's rural markets have room for all types of carriers.

Minnesota Public Utilities Commission: "It is not self-evident that telephone companies serving rural areas cannot survive competition from wireless providers. For example, although competition could produce a disincentive to invest in infrastructure (for fear of being unable to recoup the investment), it could also spark investment in infrastructure (to provide superior service to beat the competition). Similarly, competition could perform its widely recognized function of motivating the incumbents to find and implement new operating efficiencies, lowering prices and offering better service in the process." *Minnesota Public Utilities Commission, Docket No. P-5695/M-98-1285, Oct. 27, 1999*

II. The Problem: A Subsidy Structure Skewed Toward Incumbent Wireline Carriers

Why Has There Been So Little Competition in Rural Areas to Date? Given the clear benefits of competitive entry described above, why do so few consumers in rural areas have access to competitive local service at this point? A significant part of the answer can be found in outdated regulatory structures that pose barriers to entry.

Competition Depends on Universal Service Reform. Without reform of universal service policy, new entrants cannot compete. Historically, local phone service was a monopoly, and local phone rates in rural areas were subsidized through regulatory mechanisms that were only available to the incumbent monopoly carriers. In enacting universal service provisions in the Telecommunications Act of 1996, Congress recognized that traditional regulatory mechanisms were incompatible with competition.

In particular, new entrants face two significant regulatory challenges when they seek to compete with incumbent local phone companies in rural areas.

1. ***Fair ETC Designation.*** First, in order to effectively compete with rural carriers, new entrants must obtain designation as eligible telecommunications carriers (ETCs) from state commissions, and, in some cases, from the FCC. This designation allows new entrants to receive universal service funding to serve these high cost areas. The FCC and some states have made progress in expediting this process, but in many other states the ETC application process poses a significant barrier to market entry. It is apparent that some states still need guidance in their development of expedient, fair procedures for designating ETCs.

> **Federal Communications Commission:** "No competitor would ever reasonably be expected to enter a high-cost market and compete against an incumbent carrier that is receiving support without first knowing whether it is also eligible to receive such support. We believe that it is unreasonable to expect an unsupported carrier to enter a high-cost market and provide a service that its competitor already provides at a substantially supported price. Moreover, a new entrant cannot reasonably be expected to be able to make the substantial financial investment required to provide the supported services in high-cost areas without some assurance that it will be eligible for federal universal service support. In fact, the carrier may be unable to secure financing or finalize business plans due to uncertainty surrounding its designation as an ETC." *Federal-State Joint Board on Universal Service, Declaratory Ruling, 15 FCC Rcd 15168, ¶ 13 (2000)*

2. ***Portable and Explicit Support.*** Second, competitive carriers must be able to receive the same universal service support as their incumbent rivals. Historically, federal and state access charges and other rate structures have included implicit, or hidden, universal service support funds. These

subsidy regimes were designed well before the Telecommunications Act of 1996 and the advent of a competitive communications marketplace. Under these regimes, incumbent carriers receive implicit subsidies that are not available to new entrants. As such, federal and state programs must be reformed to identify and eliminate this costly hidden support which distorts the competitive market. Implicit support should be replaced with explicit, portable universal service funding mechanisms that provide sufficient support, targeted to those areas that need it most, on an equal and competitively neutral basis to incumbents and new entrants alike.

The following example is telling:

Incumbent Carrier		Competitive Entrant	
$ 100	Cost of service	$ 100	Cost of service
$ 15	Rate paid by consumer	$ 15	Rate paid by consumer
$ 10	Explicit federal support	$ 10	Explicit federal support
– 0 –	Explicit state support	– 0 –	Explicit state support
$ 75	**Implicit subsidies from other sources**	**– 0 –**	**ILEC implicit subsidies not available to competitive entrant**
		$ 75	**Deficit makes it impossible to compete**

This example shows the difficulty a competitive entrant faces when competing against an ILEC, who has access to implicit hidden support, and trying to provide consumers with a choice for the local telecommunications needs.

Federal Communications Commission: "A new entrant faces a substantial barrier to entry if its main competitor is receiving substantial support from the state government that is not available to the new entrant. A mechanism that makes only ILECs eligible for explicit support would effectively lower the price of ILEC-provided service relative to competitor-provided service by an amount equivalent to the amount of the support provided to ILECs that was not available to their competitors. Thus, non-ILECs would be left with two choices — match the ILEC's price charged to the customer, even if it means serving the customer at a loss, or offer the service to the customer at a less attractive price based on the unsubsidized cost of providing such service. A mechanism that provides support to ILECs while denying funds to eligible prospective competitors thus may give customers a strong incentive to choose service from ILECs rather than competitors." *Western Wireless Corporation Petition for Preemption, 15 FCC Rcd 16227, ¶ 8 (2000)*

IV. CUSC's Agenda for Pro-Competitive Universal Service Reform

CUSC and Pro-Competitive Universal Service Reform. CUSC was formed to advocate for competitive universal service reform, which will serve the public interest by creating mechanisms that will lead to affordable, quality telecommunications and information services to all regions of the country. Resolving the inequities inherent in the present universal service system will make competitive entry easier and therefore more desirable. All consumers benefit when they have a real choice for local telecommunications service. This goal will be realized once a pro-competitive reform of the nation's universal service system is complete.

The FCC and state commissions have made some progress toward establishing a more pro-competitive universal service regime in the five years since enactment of the Telecommunications Act. (The progress to date is summarized in the attached Appendix to this White Paper.) However, substantial additional work remains.

Core Policy Principles for Reforming the Federal and State Universal Service Systems

CUSC urges both the FCC and state commissions to aggressively move forward to reform the universal service systems consistent with the Coalition's guiding principles:

1. Nondiscriminatory Designation of Eligible Telecommunications Carriers ("ETCs") – Competitive common carriers seeking designation as an ETC in order to receive federal universal service funding should not be subject to discriminatory and unlawful requirements. The criteria used to evaluate an application for ETC status must be consistent with Section 214(e) of the Telecommunications Act and applicable regulations. All common carriers must be subject to the same procedural requirements applicable to ETC applications, which should be processed in an expeditious, fair manner.
2. Competitive Neutrality – Any common carrier, regardless of technology, that offers the required universal services and complies with all applicable requirements should be designated as an ETC for purposes of federal and state universal service support.
3. Explicit Support – Universal service support should be available to ETCs through an explicit universal service fund and should not be hidden in the rate structures of the incumbent LECs and, therefore, unavailable to competitive ETCs.
4. Portability – Universal service should be portable among ETCs. Competitive ETCs should receive the same level of universal service support for serving a customer as the incumbent LEC would receive for serving the same customer.
5. Efficiency – Universal service support levels must be reasonably sufficient to ensure that customers in high-cost areas have access to affordable telecommunications services and carriers have incentives to provide service in high-cost areas, but should be as fiscally small as reasonably possible, by employing mechanisms such as fund caps.

In particular, CUSC challenges policymakers to take the following steps to remedy the regulatory barriers to competition in rural areas:

A. Expedite ETC Designation

The FCC should adopt rules, originally proposed in July 2000, that would expedite the process of designating ETCs. It is critical that the FCC take the lead to clearly establish that the ETC designation process should take no more than six months, from start to finish, no matter the technology involved or the deciding jurisdiction. State regulators must also set policies and rules that expedite rather than hinder the process of designating ETCs. States should refrain from implementing ETC designation rules that make it unnecessarily difficult for competitive carriers to provide universal service.

B. Reform Federal Universal Service Funding Rules

The Commission should complete its pending efforts to eliminate implicit support from rural ILECs' access charges, and to establish a pro-competitive, portable federal funding system for both rural and non-rural carriers.

C. Reform State Universal Service Funding Systems

State PUCs should also reduce the extent to which implicit support, which is not available to competitive entrants, is hidden in ILECs' historical rate structures. This implicit support includes: (1) intrastate ILEC access charges in excess of cost-based levels; and (2) geographic averaging of ILECs' rates, which effectively create artificial support for rural areas that are implicitly funded by consumers in lower cost, urban areas. Creating and maintaining state universal service systems based on explicit support will also be consistent with federal court precedent. Any and all state universal service support must be recovered and distributed through competitively neutral funds that are fully portable to competitive carriers that provide universal service. The fund amounts and procedures for qualification should be easy to understand and widely available to carriers and the public alike.

D. Structure Rural Study Areas In A Manner That Facilitates, Rather Than Impedes, Competition

The FCC and state commissions should reconsider their procedures for study area disaggregation. Quite simply, competitive entrants are not receiving competitively neutral treatment when ETC designation is declined because the competitive carrier cannot serve an entire study area, particularly when this is due to the carrier's licensing limitations. Study area disaggregation will also lead to more accurately targeted universal service support.

> **FCC Common Carrier Bureau:** "We reject the general argument that rural areas are not capable of sustaining competition for universal service support. We do not believe that it is self-evident that rural telephone companies cannot survive competition from wireless providers. Specifically, we find no merit to the contention that designation of an additional ETC in areas served by rural telephone companies will necessarily create incentives to reduce investment in infrastructure, raise rates, or reduce service quality to consumers in rural areas." *Western Wireless Corp. Petition for Designation as an Eligible Telecommunications Carrier In the State of Wyoming, 16 FCC Rcd 48, ¶ 22 (Com. Car. Bur. 2000)*

V. Conclusion

CUSC encourages policymakers to continue the process, set in motion by the Telecommunications Act of 1996, of implementing a competitive universal service system. Nonetheless, a number of policy issues continue to challenge legislators and regulators. As they continue to design and implement federal and state universal service systems, CUSC encourages policymakers to remove the remaining barriers to market entry by new competitors. When all carriers have a meaningful opportunity to compete on a level playing field, consumers in all areas of the nation – rural as well as urban – will benefit from a more plentiful array of basic and advanced telecommunications and information technologies and services. Thus, Congress' vision of a pro-competitive, de-regulatory national telecommunications policy will be fulfilled.

Appendix: Progress Toward Implementing Competitive Universal Service Systems

Since passage of the Telecommunications Act, both state and federal regulators have taken a number of actions to implement more pro-competitive universal service systems.

A. State PUC Decisions Regarding Designation of Competitive ETCs

Since 1996, the regulatory commissions in at least eighteen states and Puerto Rico have designated competitive carriers as ETCs. Competitive entrants are seeking ETC designation and, slowly but surely, most states are fulfilling their obligation to act upon the requests.

Competitive Carriers Designated As ETCs

State	Company	State	Company
Arkansas	Sprint PCS	New Mexico	Leaco
Arizona	Smith Bagley, Inc.	New York	Metropolitan Communications RCN Time Warner Communications
California	Cox Cable Sprint PCS Western Wireless	North Dakota	Western Wireless
Colorado	Northeast Colorado Western Wireless	Oklahoma	Western Wireless
Delaware	Verizon Wireless (granted by FCC)	Texas	Western Wireless
Iowa	Western Wireless	Utah	Western Wireless
Kansas	Sprint PCS Western Wireless	Washington	U.S. Cellular
Maryland	MCI	Wisconsin	CTC Telecom Wausau Cellular
Minnesota	Western Wireless	Wyoming	Western Wireless (granted by FCC)
Nebraska	Western Wireless		
Nevada	Western Wireless	Puerto Rico	Centennial Cellular

B. Key FCC Decisions Supporting the Goal of Nondiscriminatory Designation of Competitive ETCs

Since 1997, the FCC has issued a number of key decisions regarding the designation of competitive ETCs.

Universal Service First Report and Order (May 1997). The FCC, based on a Federal-State Joint Board recommendation, established the important principle of competitive neutrality. The FCC held that wireless carriers and other competitive entrants that meet the statutory criteria are eligible to be designated as ETCs in the identical manner as any other traditional wireline carrier. The FCC determined that all types of telecommunications carriers, no matter the technology, must be treated on an equitable, competitively neutral basis.

Universal Service Twelfth Report and Order (June 2000). Pursuant to Section 214(e)(6), the FCC itself has authority to grant ETC designation for carriers on tribal lands and other areas that are not subject to state commission jurisdiction. This important decision requires that the FCC analyze and rule on ETC designations submitted to the FCC pursuant to Section 214(e)(6) of the Communications Act within six months. Further, it set forth an expectation that state commissions should be able to act within the same time frame.

South Dakota Preemption Declaratory Ruling (August 2000). Prior to this FCC ruling, South Dakota had denied Western Wireless' ETC petition because the carrier, a new entrant, did not already provide service throughout an entire service area prior to receiving ETC designation. Upon examination, the FCC found that South Dakota's policy effectively precluded designation of new entrants as ETCs. As a result, the FCC issued a declaratory ruling holding that such a procedure was neither competitively neutral, consistent with Section 254 of the Act, nor necessary to preserve and advance universal service, and thus did not fall within the authority reserved to the states in Section 253(b). The FCC explained that this guidance would help state commissions to expeditiously designate competitive carriers as eligible for federal support under Section 214(e).

Wyoming and Delaware ETC Designation Orders (December 2000). The FCC Common Carrier Bureau's twin orders designating Western Wireless as an ETC in Wyoming and Verizon Wireless as an ETC in Delaware provide strong precedent on the procedural and substantive standards for designating ETCs. The FCC made it clear that a mobile wireless carrier could qualify as an ETC. With respect to the public interest standard that applies in rural areas of the country, the FCC found that designation of an additional ETC in an area historically served only by rural telephone companies serves the public interest, by promoting competition and fostering provision of new technologies to rural consumers.

C. Key FCC and Court Decisions Implementing Explicit, Portable, and Competitively Neutral Funding Systems

Since 1997, the FCC and the courts have issued a number of key decisions establishing a more competitively neutral universal service funding system and reaffirming that universal service and local competition are not mutually exclusive policy objectives.

Universal Service First Report and Order (May 1997). This initial comprehensive order established the important principle that competitive ETCs should receive identical per-line support to that received by incumbent local exchange carriers ("ILECs").

Universal Service Ninth Report and Order (November 1999). This order established a federal high-cost universal service funding plan for non-rural carriers (i.e., the Bell companies, other large incumbents, and competitors in their service areas). The FCC also eliminated a "quirk" in its rules that had previously delayed funding to competitive ETCs, while providing funds promptly to incumbents.

Alenco Communications v. FCC (5th Cir. 2000). The Fifth Circuit Court of Appeals affirmed the FCC's decision to make universal service support portable (i.e., the support moves with the customer rather than remaining with the incumbent LEC when the customer chooses to change LECs). The court found petitioners' contention that the portability of the support violated the statutory principle of sufficiency of universal service funding to be without merit. The court reasoned that the purpose of universal service is to benefit the customer, not the carrier; thus, "sufficient" funding of the customer's right to adequate telephone service can be achieved regardless of which carrier ultimately receives the payment. Significantly, the court also noted that "the FCC must see to it that both universal service and local competition are realized; one cannot be sacrificed in favor of the other."

Order Revising the Access Charge System ("CALLS Order") (May 2000). The FCC substantially reduced the implicit support that large ILECs recover through their access charges, and instead created an explicit fund to recover a smaller amount of portable universal service support. Specifically, the FCC eliminated from access charges $650 million that it determined constituted implicit support for universal service. In its place, the FCC established an explicit interstate access support mechanism that would be provided on a per-line basis, and would be portable on a competitively neutral basis to any ETC serving a supported customer, regardless of the technology used by that carrier. This explicit funding is targeted primarily to the highest-cost wire centers in each state.

Kansas Funding Preemption Order (August 2000). The FCC held that Kansas' original state universal service fund, which was designed to provide substantially greater funding to ILECs than to competitive ETCs, would have been preempted. Fortunately, preemption was not needed because, after the preemption petition was filed, the Kansas Corporation Commission adopted new regulations for determining and allocating universal service support that made all support fully portable among competing carriers in Kansas. In its decision, the FCC stated that any similar non-competitively neutral state programs would likely run afoul of Section 253 of the Act.

Comsat Corp. and AT&T Corp. v. FCC (5th Cir. 2001). The Fifth Circuit Court of Appeals held that permitting implicit universal service support, and rate mechanisms that effectively create such support, violate Congress' clear directive that universal service support must be explicit. Specifically, the court held that the FCC decision to permit ILECs to continue to recover universal service costs through access charges to interexchange carriers is an unlawful violation of Section 254(e). The Court expressly stated that the FCC cannot foster and maintain a universal service system based on any implicit support, whether on a permissive or mandatory basis.

Rural Task Force (RTF) Order (May 2001). The FCC adopted, with minor modifications, the universal service recommendations submitted by the Rural Task Force, which had included representatives of a broad cross-section of carriers, including rural telephone companies, competitive local exchange carriers, long distance carriers, wireless providers, consumer advocates, and state regulators. The FCC largely retained its existing universal service support mechanism for incumbent rural local telephone companies and competitors operating in their service areas, based on historic costs; allowed a one-time $118.5 million increase in the annual level of funding; and kept in place the inflation adjusted cap on the growth in funding. In so doing, the FCC adopted the RTF's compromise between the rural telephone companies' desire to allow unrestrained growth in funding levels, and that of net contributors to the fund who sought to retain the existing cap on funding growth. Finally, the FCC recognized the importance of completing the process of removing implicit support from incumbent rural local telephone companies' access charges. It pledged to address implicit subsidies in the upcoming Multi-Association Group (MAG) proceeding, in which it is considering a proposal to modify the access charge regime applicable to rural telephone companies.

U.S. Court of Appeals for the Fifth Circuit: "Petitioners' various challenges fail because they fundamentally misunderstand a primary purpose of the Communications Act — to herald and realize a new era of competition in the market for local telephone service while continuing to pursue the goal of universal service. They therefore confuse the requirement of sufficient support for universal service within a market in which telephone service providers compete for customers, which federal law mandates, with a guarantee of economic success for all providers, a guarantee that conflicts with competition."
Alenco Communications v. FCC, 201 F.3d 608 (5th Cir. 2000)