CORRECTED VERSION

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
	)	
	)	
Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge	)	CC Docket Nos. 96-262, 94-1, 91-213, 95-72

FOURTH ORDER ON RECONSIDERATION IN CC DOCKET NO. 96-45, REPORT AND ORDER IN CC DOCKET NOS. 96-45, 96-262, 94-1, 91-213, 95-72

Adopted: December 30, 1997 **Released:** December 30, 1997

By the Commission: Commissioners Ness and Powell issuing separate statements; Commissioner Furchtgott-Roth dissenting and issuing a statement.

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I. INTRODUCTION

1. In the Telecommunications Act of 1996,[1] Congress amended the Communications Act of 1934[2] by, among other things, adding a new section 254 to the Act. In section 254, Congress directed the Commission and states to take the steps necessary to establish support mechanisms to ensure the delivery of affordable telecommunications service to all Americans, including low-income consumers, eligible schools and libraries, and rural health care providers. Specifically, Congress directed the Commission and the states to devise methods to ensure that "[c]onsumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas . . . have access to telecommunications and information services . . . at rates that are reasonably comparable to rates charged for similar services in urban areas"[3] and to "establish competitively neutral rules . . . to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and non-profit elementary and secondary school classrooms, health care providers, and libraries."[4] On May 8, 1997, the Commission released the *Universal Service Report and Order*,[5] implementing section 254 of the Act and establishing a universal service support system that becomes effective on January 1, 1998 and that will be sustainable in an increasingly competitive marketplace.

2. In the *Order*, the Commission adopted rules that reflect virtually all of the recommendations of the Federal-State Joint Board on Universal Service[6] and meet the four critical goals set forth for the new universal service program: (1) that all of the universal service

[1] Pub. L. No. 104-104, 110 Stat. 56 (the 1996 Act).

[2] 47 U.S.C. §§ 151, *et seq*. (the Act). Hereinafter, all citations to the Act and to the 1996 Act will be to the relevant section of the United States Code unless otherwise noted.

[3] 47 U.S.C. § 254(b)(3).

[4] 47 U.S.C. § 254(h)(2)(A).

[5] Federal-State Joint Board on Universal Service, *Report and Order*, CC Docket No. 96-45, FCC 97-157, 12 FCC Rcd 8776 (rel. May 8, 1997) (*Order*). The Commission released an erratum correcting the *Order* on June 4, 1997.

[6] *See* Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Recommended Decision*, 12 FCC Rcd 87 (1996). Pursuant to section 254(a) of the Act, the Commission established a Federal-State Joint Board to make recommendations to the Commission regarding universal service. The Federal-State Joint Board is composed of eight members, three Federal Communications Commission Commissioners, four state Commissioners nominated by the National Association of Regulatory Utility Commissioners, and one state-appointed utility consumer advocate nominated by the National Association of State Utility Consumer Advocates. *See* In the Matter of Federal-State Joint Board on Universal Service, *Notice of Proposed Rulemaking and Order Establishing Joint Board*, CC Docket No. 96-45, FCC 96-93 (1996), at para. 132.

objectives established by the Act, including those for low-income individuals, for consumers in rural, insular, and high cost areas, and for schools, libraries, and rural health care providers, be implemented; (2) that rates for basic residential service be maintained at affordable levels; (3) that universal service funding mechanisms be explicit; and (4) that the benefits of competition be brought to as many consumers as possible. Recognizing that, as circumstances change, further Commission action may be needed to ensure that we create sustainable and harmonious federal and state methods of continuously fulfilling universal service goals, the Commission also committed itself to work in close partnership with the states to create complimentary federal and state universal service support mechanisms. These efforts are ongoing.

3. Through the *Order* and the accompanying orders reforming the Commission's access charge rules,[7] the Commission established the definition of services to be supported by federal universal service support mechanisms and the specific timetable for implementation. The Commission set in place rules that will identify and convert existing federal universal service support in the interstate high cost fund, the dial equipment minutes (DEM) weighting program, Long Term Support (LTS), Lifeline, Link Up, and interstate access charges to explicit competitively neutral federal universal service support mechanisms. The Commission also modified the funding methods for the existing federal universal service support mechanisms so that such support is not generated, as at present, entirely through charges imposed on long distance carriers. Instead, as the statute requires, equitable and non-discriminatory contributions will be required from all providers of interstate telecommunications service. The Commission took other steps to make federal universal service support mechanisms consistent with the development of local service competition, and established a program to provide schools and libraries with discounts on all commercially available telecommunications services, Internet access, and internal connections. The Commission also established mechanisms to provide support for telecommunications services for all public and not-for-profit health care providers located in rural areas.

4. The Commission also named the National Exchange Carrier Association (NECA) the temporary Administrator of the universal service support mechanisms on the condition that NECA agree to make changes to its governance that would render it more representative of non-incumbent local exchange carrier (LEC) interests.[8] As a condition of its appointment as

[7] Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing and End User Common Line Charges, CC Docket Nos. 96-262, 94-1, 91-213, and 95-72, *Notice of Proposed Rulemaking,Third Report and Other and Notice of Inquiry*, 62 Fed. Reg. 4,670 (rel. Dec. 24, 1996) (*Access Charge Reform NPRM*); *First Report and Order*, FCC 97-158 (rel. May 16, 1997) (*Access Charge Reform Order*). *See also* Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, *Fourth Report and Order*, FCC 97-159 (rel. May 21, 1997).

[8] *Order*, 12 FCC Rcd at 9216-17.

temporary Administrator, the Commission subsequently directed NECA to establish the Universal Service Administrative Company (USAC), an independently functioning subsidiary corporation that will perform the billing, collection, and disbursement functions for all of the universal service support mechanisms.[9] The Commission further directed NECA to create the Schools and Libraries Corporation and Rural Health Care Corporation to perform all functions associated with administering the schools and libraries and rural health care programs, respectively, except those directly related to billing and collecting universal service contributions and disbursing support.[10]

5. On July 10, 1997, the Commission released a reconsideration order on its own motion in this proceeding.[11] Among other things, the *July 10 Order* (1) clarified certain issues relating to contracts for services to schools and libraries; (2) modified the formula for recovery of corporate operations expense from high cost loop support mechanisms; and (3) clarified issues concerning coordination between the Commission staff and the state staff of the Joint Board in CC Docket No. 96-45 in implementing the new monitoring program.

6. Sixty-one parties have filed petitions for reconsideration and/or clarification of the *Order* and the *July 10 Order*.[12] In this Fourth Order on Reconsideration, we address issues raised by petitioners that either must or should be addressed before the new universal service program begins. We will address the remaining issues in one or more subsequent reconsideration orders in this docket.

7. In this order, we clarify or make further findings regarding: (1) the rules governing the eligibility of carriers and other providers of supported services; (2) methods for determining levels of universal service support for carriers in rural, insular and high cost areas; (3) support for low-income consumers; (4) the rules governing the receipt of universal service support under the schools and libraries and rural health care programs; (5) the determinations of who must contribute to the new universal service support mechanisms; and (6) administration of the support mechanisms.

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[9] *See* Changes to the Board of Directors of the National Exchange Carrier Association, Inc. and Federal-State Board on Universal Service, CC Docket Nos. 97-21 and 96-45, FCC 97-253, *Report and Order and Second Order on Reconsideration* (rel. July 18, 1997) (*NECA Report and Order*).

[10] *NECA Report and Order* at para. 30.

[11] *See* Federal-State Joint Board on Universal Service, *Order on Reconsideration*, CC Docket No. 96-45, FCC 97-246 (rel. July 10, 1994) (*July 10 Order*).

[12] A complete list of all petitioners and other parties filing comments or reply comments appears in Appendix B hereto.

II. DEFINITION OF UNIVERSAL SERVICE: SERVICES THAT ARE ELIGIBLE FOR SUPPORT

A. Local Calling Provided by Satellite Companies

1. Background

8. In the *Order*, the Commission defined the "core" or "designated" services that will be supported by universal service support mechanisms as: single-party service; voice grade access to the public switched network; Dual Tone Multifrequency signaling or its functional equivalent; access to emergency services; access to operator services; access to interexchange service; access to directory assistance; and toll limitation for qualifying low-income consumers.[13] In its discussion of the services to be supported by the universal service support mechanisms in the *Order*, the Commission concluded that some amount of local calling must be included within the supported services.[14] The Commission reasoned that in order for consumers in rural, insular, and high cost areas to realize the full benefits of affordable voice grade access, universal service should support usage of, and not merely access to, the local network.[15]

2. Pleadings

9. AMSC, which uses a satellite system to provide voice and data communications services, asks the Commission to clarify that calls to and from "fixed-site" subscribers that originate and terminate within the subscriber's local area constitute local calling.[16] AMSC explains that its satellite communications system provides voice and data communications services to people who live in rural and remote areas of the United States that are unserved by terrestrial technologies.[17] AMSC further explains that, along with mobile service, it provides

[13] *Order*, 12 FCC Rcd at 8809-10.

[14] *Order*, 12 FCC Rcd at 8812-14.

[15] The Commission did not quantify in the *Order* the amount of local usage that must be provided without additional charge by carriers receiving universal service support for serving rural, insular, and high cost areas, nor did the Commission generally define "local usage." Rather, the Commission determined that it would seek comment in a further notice of proposed rulemaking on a forward-looking cost methodology concerning the amount of local usage that must be provided by eligible telecommunications carriers. *See Order*, 12 FCC Rcd at 8813. The Commission adopted and released that further notice of proposed rulemaking on July 18, 1997. *See* Federal-State Joint Board on Universal Service, Forward-Looking Mechanism for High Cost Support for Non-Rural LECs, CC Docket Nos. 96-45 and 97-160, *Further Notice of Proposed Rulemaking*, FCC 97-256 (rel. Jul. 18, 1997) (*July 18 Further Notice*).

[16] AMSC petition at 5.

[17] AMSC petition at 2.

"fixed-site" telephone service by installing a transceiver (with a standard interface and handset) at the customer's location. Outbound calls from the customer are routed through the satellite to AMSC's earth station and into the public switched telephone network (PSTN). Similarly, inbound calls to the customer are routed through AMSC's earth station to the satellite and terminate at the customer's location.[18] AMSC asserts that such calls constitute local calls and therefore should qualify as local calling. AMSC argues that a determination that calls completed via satellite do not constitute local calling "would not only be counter to the interests of rural consumers, it also would penalize AMSC for its system design, thereby conflicting with the Commission's explicit goal of technological and competitive neutrality."[19] No party commented on AMSC's petition.

3. Discussion

10. We grant AMSC's request and conclude that calls to and from a satellite company's fixed-site subscribers, for which such subscribers pay a non-distance and non-usage sensitive rate, constitute local calling for purposes of determining whether a carrier is eligible for federal universal service support. We find that, consistent with the principles of competitive and technological neutrality established in the *Order*,[20] non-landline telecommunications providers should be eligible to receive universal service support even though their local calls are completed via satellite. We conclude that any call for which a satellite company's subscribers are not charged on a distance- or usage-sensitive basis constitutes a local call. Our discussion of local calling with respect to satellite companies is not intended to prejudge any other issue pertaining to the definition of local calling with respect to the amount of local calling to be supported by universal service support mechanisms that we may adopt in our forthcoming Order. In that Order, we intend to define the amount of local calling that must be provided by eligible telecommunications carriers.[21]

B. Provision of E911 by MSS Providers

1. Background

11. In the *Wireless E911 Decision*, released on July 26, 1996, the Commission exempted Mobile Satellite Service (MSS) from the rules requiring wireless carriers to implement

[18] AMSC petition at 2-3.

[19] AMSC petition at 5.

[20] *See Order*, 12 FCC Rcd at 8801-03.

[21] *See July 18 Further Notice* at paras. 177-181.

911[22] and Enhanced 911 (E911)[23] services.[24] The Commission expressed its expectation in the *Wireless E911 Decision* that MSS providers eventually would be required to provide access to emergency services, but did not adopt a schedule for implementing such a requirement.[25]

12. In the *Order*, the Commission concluded that access to emergency services, including access to 911 and E911 services, should be included in the services designated for universal service support.[26] The Commission found that E911 service is "widely recognized as essential to . . . public safety"[27] and is consistent with the public interest, convenience, and necessity.[28] The Commission concluded that all eligible telecommunications carriers in localities that have implemented E911 service[29] should be required either to provide access to E911 service or demonstrate "that exceptional circumstances" prevent them from offering access to E911 service at this time.[30] The Commission concluded that a carrier that is otherwise eligible to receive universal service support, but is currently incapable of providing access to E911 within a

[22] 911 service is an emergency reporting system whereby a caller can dial 911 and be routed to a common answering location that will assess the nature of the emergency and dispatch the proper response teams.

[23] E911 service includes the ability to provide Automatic Numbering Information, which permits the Public Safety Answering Point to have call back capability if the call is disconnected, and Automatic Location Information, which permits emergency service providers to identify the geographic location of the calling party.

[24] Revision of the Commission's Rules to Ensure Compatibility with Enhanced 911 Emergency Calling Systems, CC Docket No. 94-102, *Report and Order and Further Notice of Proposed Rulemaking*, 11 FCC Rcd 18676 (1996) at para 83.

[25] *Wireless E911 Decision* at para 83.

[26] *Order*, 12 FCC Rcd at 8815-17.

[27] *See* 47 U.S.C. § 254(c)(1)(A).

[28] *See* 47 U.S.C. § 254(c)(1)(D).

[29] As discussed in the *Wireless E911 Decision*, a wireless carrier's obligation to provide E911 services applies only if: (1) a locality has implemented E911 service, i.e., if a public safety answering point (PSAP) capable of receiving and utilizing the data elements associated with the E911 services has requested that the carrier provide E911 service; and (2) if a mechanism for the recovery of costs relating to the provision of such services is in place.

[30] *Order*, 12 FCC Rcd at 8827. The Commission further stated that "[a] carrier can show that exceptional circumstances exist if individualized hardship or inequity warrants a grant of additional time to comply with the general requirement that eligible carriers must provide . . . access to E911 when the locality has implemented E911 service and that a grant of additional time to comply with these requirements would better serve the public interest than strict adherence to the general requirement that an eligible telecommunications carrier must be able to provide these services to receive universal service support." *See Order*, 12 FCC Rcd at 8827-28.

locality that has implemented E911 service may petition its state commission for permission to receive universal service support for the designated period during which it is completing the network upgrades necessary for it to offer access to E911 service.[31] The Commission concluded that the period during which a carrier may receive support while completing the essential upgrades should extend only as long as the relevant state commission finds that "exceptional circumstances" exist and should not extend beyond the time that the state commission deems necessary to complete the network upgrades.[32]

2. Pleadings

13. AMSC asks the Commission to clarify that MSS providers are included among the wireless carriers that may petition their state commission for permission to receive universal service support for the designated period during which they are completing the network upgrades necessary to offer access to E911.[33] AMSC further states that, "[i]n its 1996 E911 decision, the Commission fully exempted MSS providers from the E911 requirements for the indefinite future. [citation omitted]. In addition, this exemption should be automatic for MSS providers, since the Commission has already determined that for MSS providers the burden of offering E911 is 'exceptional.'"[34] No party commented on AMSC's petition.

3. Discussion

14. In response to AMSC's petition, we clarify that MSS providers, like other wireless providers in localities that have implemented E911 service, may petition their state commission for permission to receive universal service support for the designated period during which they are completing the network upgrades required to offer access to E911. We deny AMSC's petition, however, to the extent that it requests that MSS providers in localities that have implemented E911 service be relieved of the obligation to demonstrate that "exceptional circumstances" prevent them from offering access to E911 service. We decline to exempt MSS providers "automatically" from the requirement to offer access to E911 service in order to be eligible for federal universal service support. We find that this determination is consistent with the *Wireless E911 Decision*, which held that MSS providers are not presently required to provide

[31] The carrier generally must provide the other core services in order to receive universal service support. Carriers that are currently unable to provide single-party service and toll limitation, however, may petition the state commission for permission to receive universal service support for the period during which they are completing the network upgrades necessary to offer these services. *See Order*, 12 FCC Rcd at 8827.

[32] *Order*, 12 FCC Rcd at 8828.

[33] AMSC petition at 6-7.

[34] AMSC petition at 6-7.

access to E911 service. To receive federal universal service support, however, MSS providers must satisfy the eligibility requirements we previously established. We rely on state commissions to ensure that providers that are not currently able to provide access to E911 service are making the network upgrades necessary to provide access to E911 service as quickly as possible.

C. Voice Grade Access to the Public Switched Network

1. Background

15. In the *Order*, the Commission included voice grade access to the PSTN within the "core" services that will be supported by the high cost program of the federal universal service support mechanisms.[35] Consistent with the Joint Board's recommendation, the Commission concluded that voice grade access should occur in the frequency range between approximately 500 Hertz and 4,000 Hertz.[36]

2. Discussion

16. We reconsider, on our own motion, the Commission's specification of a bandwidth[37] for voice grade access to the PSTN and conclude that bandwidth for voice grade access should be, at a minimum, 300 Hertz to 3,000 Hertz.[38] In the *Order*, the Commission determined that voice grade access bandwidth be approximately 500 Hertz to 4,000 Hertz. We reconsider that determination based on our recognition that the 500 Hertz to 4,000 Hertz bandwidth established in the *Order* would require eligible carriers to comply with a voice grade access standard that is more exacting than current industry standards, a result that we did not intend. We note that AT&T operating principles recommend that voice grade access bandwidth be 200 Hertz to 3,500 Hertz,[39] while Bellcore recommends a range of 200 Hertz to 3,200 or 3,400 Hertz.[40] American National Standards Institute (ANSI) defines voice grade access

[35] *Order*, 12 FCC Rcd at 8810-11.

[36] *Order*, 12 FCC Rcd at 8811-12. *See also* 47 C.F.R. § 54.101(a)(1).

[37] Bandwidth, as a measure of channel capacity for analog signals, is the range of frequencies that the channel can carry with attenuation less than some specified amount.

[38] We may revisit this definition as voice grade standards evolve.

[39] *See* AT&T, Engineering and Operations in the Bell System 194-195 (Second Edition).

[40] *See* Bellcore, Principles of Bellcore's Telecommunications Transmission Engineering 666, 680-681 (Third Edition).

bandwidth as 300 Hertz to 3,000 Hertz.[41] We did not intend to impose a more onerous definition of voice grade access than those generally established under existing industry standards, and conclude that our decision here will ensure that consumers receive voice grade access at levels that are consistent with Commission rules and that are not incompatible with current industry guidelines. We do not adopt the broader voice grade access bandwidth specified in the AT&T and Bellcore operating principles. To the extent that the bandwidth recommended in the AT&T and Bellcore operating principles exceeds the bandwidth established in the ANSI definition of voice grade access, we are concerned that a substantial number of otherwise eligible carriers may be unable to qualify for universal service support if we were to require all carriers to meet this standard as a condition of eligibility. Moreover, networks utilizing loading coils may experience difficulty operating properly at bandwidths exceeding 3,400 Hertz. Carriers that meet current AT&T and Bellcore guidelines, however, will be able to satisfy our definition of voice grade access.

III. CARRIERS ELIGIBLE FOR UNIVERSAL SERVICE SUPPORT

A. Designation of Eligible Carriers

1. Background

17. Section 254(e) provides that, after the effective date of the Commission's regulations implementing section 254, "only an eligible telecommunications carrier designated under section 214(e) shall be eligible to receive specific Federal universal service support."[42] Section 214(e)(1) sets forth the obligations of an eligible telecommunications carrier.[43] Section 214(e)(2) states that "[a] State commission shall upon its own motion or upon request designate a common carrier that meets the requirements of paragraph (1) as an eligible telecommunications carrier for a service area designated by the State commission."[44]

18. In the *Order*, the Commission noted that some carriers are not subject to the jurisdiction of a state commission.[45] The Commission concluded, however, that nothing in section 214(e)(1) requires that a carrier be subject to the jurisdiction of a state commission in

[41] American National Standards Institute, *Interface between Carriers and Customer Installations - Analog Voicegrade Switched Access Lines with Distinctive Alerting Features* 4 (1995).

[42] 47 U.S.C. § 254(e).

[43] 47 U.S.C. § 214(e)(1).

[44] 47 U.S.C. § 214(e)(2).

[45] *Order*, 12 FCC Rcd at 8859.

order to be designated an eligible telecommunications carrier.[46] Thus, the Commission stated, "tribal telephone companies, CMRS providers, and other carriers not subject to the full panoply of state regulation may still be designated as eligible telecommunications carriers."[47]

2. Pleadings

19. In their petitions, Sandwich Isles and GVNW request that, for carriers not subject to the jurisdiction of a state commission, the Commission should allow the agency with regulatory authority over the geographical area being served to make the eligible telecommunications carrier designation.[48] As it explains in its petition, Sandwich Isles is a telephone company that received a license from the State of Hawaii's Department of Hawaiian Home Lands (DHHL) in 1995 to construct a telecommunications network on Hawaiian Home Lands throughout the state of Hawaii.[49] Sandwich Isles maintains that the government agency that has regulatory authority over either the area being served or the telephone company serving that area should be permitted to make the eligibility designation in order to ensure that the designation will be made by an agency that has knowledge regarding the area to be served and the consumers that reside there.[50] Sandwich Isles further argues that, where a carrier is not subject to the jurisdiction of a state commission, the Act does not require the state commission to make the eligibility designation.[51] No party commented on these petitions.

3. Discussion

20. We read Sandwich Isles' petition to contend that the DHHL, rather than the Hawaii Public Utilities Commission (PUC), should have authority to designate eligible telecommunications carriers on the Hawaiian Home Lands.[52] Section 153(41) defines "[s]tate

[46] *Order*, 12 FCC Rcd at 8859.

[47] *Order*, 12 FCC Rcd at 8859.

[48] GVNW petition at 22; Sandwich Isles petition at 9-11.

[49] DHHL, according to Sandwich Isles' petition, is a state agency created by federal statute that has exclusive statutory control of, and responsibility for, the management of the Hawaiian Home Lands in Hawaii. Organized under the Hawaiian Homes Commission, DHHL was created to provide land (i.e., the Hawaiian Home Lands) to native Hawaiians. Sandwich Isles explains that, "In recognition of the special relationship that exists between the United States and the native Hawaiian people, Congress has extended to native Hawaiians the same rights and privileges accorded to . . . American Indians . . . under the Native American Programs Act of 1974." Sandwich Isles petition at 1-2, n.1.

[50] Sandwich Isles petition at 10.

[51] Sandwich Isles petition at 11.

[52] We note that Sandwich Isles' petition regarding its eligibility to receive universal service support for serving

commission" as "the commission, board, or official (by whatever name designated) which under the laws of any State has regulatory jurisdiction with respect to intrastate operations of carriers."[53] Based on the record before us, it is unclear whether the DHHL meets the Act's definition of "state commission." Based on further information provided by the parties, it now appears that the issue here is not whether there is a state commission with jurisdiction to designate eligible carriers, but which of the state agencies should be considered to be the "state commission" for purposes of designating Sandwich Isles.[54] Before undertaking to develop the record further and to interpret the term "state commission," we encourage Sandwich Isles and the relevant state agencies to resolve this dispute. If they are unable to do so, we encourage Sandwich Isles and the relevant state agencies to bring that fact to our attention so that we may complete action on the pending petitions.[55]

B. Eligibility Designation Date

1. Background

21. Section 254(e) of the Act provides that, after the effective date of the Commission's regulations implementing section 254, "only an eligible telecommunications

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unserved rural areas in Hawaii will be addressed in a separate proceeding. *See* Sandwich Isles' Petition for Waiver of Section 36.611 of the Commission's Rules and Request for Clarification, AAD 97-82, (July 8, 1997).

[53] 47 U.S.C. § 153(41).

[54] Based on a recent order issued by the Hawaii PUC authorizing Sandwich Isles to provide intraLATA and intrastate telecommunications services on lands administered by the DHHL, it appears that Sandwich Isles, at least to some extent, is subject to the jurisdiction of the Hawaii PUC. *See* In the Matter of the Application of Sandwich Isles Communications Inc. for Authorization to Provide IntraLATA and Intrastate Telecommunications Services within and between Hawaiian Home Lands throughout the State of Hawaii Pursuant to Haw. Rev. State. Section 269-16.9, Docket No. 96-0026, Order No. 16078 (Nov. 14, 1997).

[55] We note that Pub. L. 105-125, 111 Stat. 2540 (approved December 1, 1997) recently added subsection (e)(6) to section 214(e) of the Act. Section 214(e)(6) provides that "[i]n the case of a common carrier providing telephone exchange service and exchange access that is not subject to the jurisdiction of a State commission, the Commission shall upon request designate such a common carrier that meets the requirements of paragraph (1) as an eligible telecommunications carrier for a service area designated by the Commission consistent with applicable federal and State law." Because it appears that Sandwich Isles may be subject to the jurisdiction of at least two state agencies (i.e., the Hawaii PUC and DHHL), subsection (e)(6) does not affect our determination regarding the entity that should be responsible for designating eligible telecommunications carriers on the Hawaiian Home Lands. Although this provision does not govern the circumstances here, where the issue is which state agency has jurisdiction to designate carriers as opposed to the absence of any such agency, we think it is appropriate for the Commission to assist in resolving that issue if the parties are unable to resolve it independently.

carrier designated under section 214(e) shall be eligible to receive specific Federal universal service support."[56] In the *Order*, the Commission established January 1, 1998 as the date on which the newly adopted modifications to the existing universal service support mechanisms will take effect. The Commission also established that, consistent with section 214(e)(2), state commissions will make carrier eligibility designations,[57] and that, as of January 1, 1998, only carriers designated as eligible will be eligible to receive universal service support.[58] The Commission further concluded that the Administrator of the universal service support mechanisms shall not disburse funds to a carrier until the carrier has provided to the Administrator a true and correct copy of the decision of a state commission designating that carrier as an eligible telecommunications carrier.[59] In Public Notices released August 14, 1997 and September 29, 1997, the Commission, through the Common Carrier Bureau, alerted state commissions of their obligation to designate eligible telecommunications carriers by January 1, 1998.[60] As provided in the September 29 Public Notice, states must submit to the temporary Administrator by December 31, 1997, a list of carriers designated as eligible and the service areas of such eligible non-rural carriers.

2. Pleadings

22. In its petition for reconsideration, the National Exchange Carrier Association (NECA) asks the Commission to establish specific dates by which state commissions must file their decisions designating eligible telecommunications carriers and to clarify what procedure, if any, the temporary Administrator should follow in the event that carriers that currently receive universal service support are not designated as eligible by their state commission by January 1, 1998.[61] On December 11, 1997, USTA requested that the Commission clarify that designations of eligible telecommunications carriers made by state commissions by March 31, 1998, may be treated as retroactive to January 1, 1998.[62]

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[56] *See* 47 U.S.C. § 254(e).

[57] *Order*, 12 FCC Rcd at 8851-52.

[58] 47 C.F.R. § 54.201(a)(1).

[59] *Order*, 12 FCC Rcd at 8886-87.

[60] Listing of Changes Adopted in the May 8 Order that Will Take Effect January 1, 1998, *Public Notice*, DA 97-1747 (rel. Aug. 14, 1997) (*August 14 Public Notice*); Common Carrier Bureau Announces Procedures for States Regarding Lifeline Consents, Adoption of Intrastate Discount Matrix for Schools and Libraries, and Designation of Eligible Telecommunications Carriers, *Public Notice*, DA 97-1892 (rel. September 29, 1997) (*September 29 Public Notice*).

[61] NECA petition at 2-3.

[62] USTA Petition for Clarification, CC Docket No. 96-45, filed Dec. 11, 1997 (USTA informal comments).

3. Discussion

23. In light of section 254's directive that only carriers designated as eligible pursuant to section 214(e) shall be eligible to receive universal service support, we affirm our previous conclusion that, as of January 1, 1998, the temporary Administrator may not disburse support to carriers that have not been designated as eligible under section 214(e). Thus, if a carrier has not been designated as eligible by January 1, 1998, it may not receive support until such time as it is designated an eligible telecommunications carrier. This applies to all carriers, including those that currently receive universal service support under the existing support mechanisms. We agree with USTA, however, that a state commission that is unable to designate as an eligible telecommunications carrier, by January 1, 1998, a carrier that sought such designation before January 1, 1998, should be permitted, once it has designated such carrier, to file with the Commission a petition for waiver requesting that the carrier receive universal service support retroactive to January 1, 1998.[63] A state commission filing such a petition must explain why it did not designate such carrier as eligible by January 1, 1998 and provide a justification for why providing support retroactive to January 1, 1998 serves the public interest. We encourage relevant carriers to file information demonstrating that they took reasonable steps to be designated as eligible telecommunications carriers by January 1, 1998. We find that it is in the public interest to permit telecommunications carriers that were eligible to receive universal service support on January 1, 1998, but that were not designated as eligible by their state commission by that date, to be permitted to seek retroactive support. Allowing retroactive support will permit consumers served by those carriers to benefit from the support to which those carriers would have been entitled, but for circumstances that prevented the state commission from designating the carriers as eligible for receipt of universal service support prior to January 1, 1998.

24. In light of our conclusion above, we dismiss as moot the portion of USTA's petition requesting that carriers designated as eligible telecommunications carriers by March 31, 1998, be automatically entitled to receive support retroactive to January 1, 1998. Regarding NECA's concern that the *Order* does not specify a date by which state commissions must make their eligible carrier determinations, we note that the Bureau's August 14 and September 29 Public Notices notified state commissions to submit their eligible carrier designations to the temporary Administrator no later than December 31, 1997.

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[63] The deadline for filing petitions for reconsideration in a notice and comment rulemaking proceeding are prescribed in section 405 of the Communications Act of 1934, as amended. *See* 47 U.S.C. § 405(a). The Commission lacks discretion to waive this statutory requirement. *See Virgin Islands Telephone Corp. v. FCC*, 989 F.2d 1231, 1237 (D.C. Cir. 1993); *Reuters Ltd. v. FCC*, 781 F.2d 946, 951-52 (D.C.Cir. 1986). The filing deadline for petitions for reconsideration of the *Order* was July 17, 1997. Therefore, to the extent that USTA's petition, filed December 11, 1997, seeks reconsideration of the *Order*, we will treat it as an informal comment.

IV. RURAL, INSULAR, AND HIGH COST SUPPORT

A. Indexed Cap on High Cost Loop Fund

1. Background

25. The Act mandates that universal service support be explicit[64] and requires that such support be recovered on an equitable and non-discriminatory basis from all providers of interstate telecommunications services.[65] Consistent with this mandate, the Commission adopted a plan for establishing a system of universal service support for rural, insular, and high cost areas that will replace current implicit federal subsidies with explicit support based on the forward-looking economic cost of providing supported services beginning January 1, 1999.[66] Recognizing the unique circumstances facing rural carriers, the Commission concluded that rural carriers should be permitted to shift gradually to a support mechanism based on forward looking economic cost.[67] The starting date for the transition will be determined after further review. The

[64] 47 U.S.C. § 254(e).

[65] 47 U.S.C. § 254(d).

[66] *Order*, 12 FCC Rcd at 8888-89. For non-rural carriers receiving high cost support, the Commission will calculate support based on an estimate of the forward-looking economic costs of providing supported services in those areas. By August 1998, the Commission will select a federal mechanism for estimating these costs. *Order*, 12 FCC Rcd at 8909-10. The Commission has established a multi-step approach to refining and selecting a federal mechanism. Federal-State Joint Board on Universal Service, Forward-Looking Mechanism for High Cost Support for Non-Rural LECs, CC Docket Nos. 96-45 and 97-160, Further Notice of Proposed Rulemaking, FCC 97-256 (rel. Jul. 18, 1997) (*July 18 Further Notice*). The Common Carrier Bureau has released two public notices providing guidance to proponents of cost models on issues raised in the *July 18 Further Notice*. Guidance to Proponents of Cost Models in Universal Service Proceedings: Switching, Interoffice Trunking, Signaling, and Local Tandem Investment, *Public Notice*, DA 97-1912 (rel. Sept. 3, 1997); Guidance to Proponents of Cost Models in Universal Service Proceedings: Customer Location and Outside Plant, *Public Notice*, DA 97-2372 (rel. Nov. 13, 1997). *See infra* for the distinction between rural and non-rural carriers.

[67] *Order*, 12 FCC Rcd at 8889, 8934. Hereinafter we refer to rural carriers as those carriers meeting the definition of a "rural telephone company" in section 3(37). 47 U.S.C. § 153(37). Non-rural carriers are those carriers not meeting this definition. We note that, because a carrier may satisfy the definition of a "rural telephone company" if it provides service to fewer than 50,000 access lines, a carrier meeting this definition does not necessarily serve a geographic area that could be characterized as "rural." Section 3(37) provides that:

> The term "rural telephone company" means a local exchange carrier operating entity to the extent that such entity --
>
> (A) provides common carrier service to any local exchange carrier study area that does not include either --
>
> (i) any incorporated place of 10,000 inhabitants or more, or any part thereof, based on the

Commission directed, however, that in no event would rural carriers transition to a forward looking economic cost mechanism before January 1, 2001.[68]

26. Until an eligible rural or non-rural carrier begins to receive support based upon forward-looking economic cost, the Commission concluded that the carrier will receive support during this transition period based upon the existing support system, with certain modifications.[69] Thus, the *Order* provided that, starting on January 1, 1998, rural carriers will receive support under the existing high cost loop fund,[70] DEM weighting program,[71] and Long

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most recently available population statistics of the Bureau of the Census; or
(ii) any territory, incorporated or unincorporated, included in an urbanized area, as defined by the Bureau of the Census as of August 10, 1993;
(B) provides telephone exchange service, including exchange access, to fewer than 50,000 access lines;
(C) provides telephone exchange service to any local exchange carrier study area with fewer than 100,000 access lines; or
(D) has less than 15 percent of its access lines in communities of more than 50,000 on the date of enactment of the Telecommunications Act of 1996.

[68] *Order*, 12 FCC Rcd at 8889, 8934.

[69] *Order*, 12 FCC Rcd at 8938-39.

[70] The high cost loop fund has operated through the Commission's jurisdictional separations rules, 47 C.F.R. Part 36, to provide assistance to incumbent LECs with higher-than-average local loop costs. The Commission's separations rules currently assign 25 percent of incumbent LECs' loop costs to the interstate jurisdiction. Incumbent LECs with local loop costs exceeding 115 percent of the national average for such costs, however, may allocate additional amounts (generally, 10 percent to 75 percent of the amounts by which such costs exceed the 115 percent threshold) of their local loop costs to the interstate jurisdiction. Prior to the effective date of the rules adopted in the *Order* and *Access Charge Reform Order*, carriers recovered costs assigned to their interstate operations through the interstate access charge structure. For a further discussion of cost recovery methods under the high cost loop fund, see *infra* this section.

[71] "Dial equipment minutes (DEM) of use" is a measure of the holding time of local dial switching equipment for both originating and terminating traffic. 47 C.F.R. Part 36. Prior to the effective date of the universal service rules adopted in the *Order*, DEM weighting assistance was an implicit subsidy recovered through switched access rates charged to interexchange carriers by incumbent LECs serving fewer than 50,000 subscriber lines. *Order*, 12 FCC Rcd at 8892-93. This program has enabled small incumbent LECs to assign a greater proportion of their local switching costs to the interstate jurisdiction than they otherwise would allocate. *Id.* DEM weighting applies independent of, and is unrelated to, the high cost loop fund.

Term Support (LTS) program,[72] as modified in the *Order*.[73] The *Order* provided that non-rural LECs will be eligible, starting on January 1, 1998, to receive support under the modified high cost loop fund and LTS program until January 1, 1999, when these carriers will begin to receive universal service support based on a forward-looking economic cost methodology.[74] Pursuant to the mandate of section 254 that universal service support be explicit and that support be recovered on an equitable and non-discriminatory basis from all providers of interstate telecommunications services, the Commission required that high cost loop support, DEM weighting assistance, and LTS be removed from interstate access charges and recovered from the new universal service support system.[75]

27. Consistent with its decision to continue using the existing universal service support system, with only minor modifications, until a forward-looking economic cost mechanism becomes effective, the Commission elected to retain the indexed cap on the existing high cost loop fund until all carriers receive support based on forward-looking economic cost.[76] The indexed cap, originally adopted in 1993, limits the maximum annual growth in the total

[72] The LTS program supports carriers with above-average loop costs by providing carriers that are members of the NECA common line pool with enough support to enable them to charge a nationwide average carrier common line (CCL) interstate access rate. *Order*, 12 FCC Rcd at 8893. The CCL interstate access rate, also known as the CCL charge, is a per-minute charge that incumbent LECs assess on IXCs. Currently, the LTS program is funded by incumbent LECs that have withdrawn from the NECA common line pool. Such non-pooling incumbent LECs recover the LTS payments they make through their CCL charge to interexchange carriers (IXCs). *Id.*

[73] *Order*, 12 FCC Rcd at 8938-39.

[74] *Order*, 12 FCC Rcd at 8927.

[75] *Order*, 12 FCC Rcd at 8939-42. Prior to the effective date of the rule changes adopted in the Commission's *Order* and *Access Charge Reform Order*, carriers recovered the first 25 percent of their loop costs assigned to their interstate operations through subscriber line charges (SLCs) and CCL charges. The SLC is a flat, monthly charge that incumbent LECs assess directly on end users of telecommunications services. As noted above, the CCL charge is a per-minute charge that incumbent LECs assess on IXCs. Both SLCs and CCL charges are part of the Commission's interstate access charge structure. In the *Access Charge Reform Order*, the Commission reformed the interstate access charge structure by adopting rules that will permit price cap LECs to shift gradually from a cost-recovery mechanism that recovers a significant portion of non-traffic sensitive loop costs through traffic sensitive, per-minute CCL charges to one that recovers these costs through non-traffic sensitive, flat-rated charges. *Access Charge Reform Order* at para. 91. The new cost-recovery mechanism retains the current $3.50 ceiling on the SLC for primary residential and single-line business lines and increases the SLC ceiling on other lines to permit LECs to recover a greater amount of the loop costs assigned to the interstate jurisdiction through flat-rated charges assessed on the end user. To the extent that SLC ceilings prevent price cap LECs from recovering their allowed common line revenues from end users, LECs will recover the shortfall, subject to a maximum charge, through a presubscribed interexchange carrier charge (PICC), a flat, per-line charge assessed on the end-user's presubscribed IXC. *Access Charge Reform Order* at para. 91.

[76] *Order*, 12 FCC Rcd at 8929-30.

amount of support available from the high cost loop fund to the previous year's support amount, increased by an index factor that is equal to the rate of growth in the total number of working loops nationwide for the preceding calendar year.[77] While maintaining the cap as currently calculated, the Commission also established a method for recalculating the cap after January 1, 1999, the date on which non-rural carriers will begin to receive support for high cost loops based on forward-looking costs.[78] Because only rural carriers will continue to receive support under the modified existing system of support after January 1, 1999, the cap will be based, after that date, on the costs of rural carriers, adjusted annually by the average growth in lines of rural carriers during the previous year.[79]

28. The Commission originally adopted the cap because it determined that it would limit fund growth and moderate annual fluctuations in the size of the fund.[80] In the *Order*, the Commission decided to continue using the indexed cap because it would prevent excessive growth in the existing high cost loop fund during the period preceding implementation of a forward-looking support mechanism.[81] The Commission also concluded that rapid growth in high cost loop support could make the change to a forward-looking support mechanism more difficult for rural carriers if the new system provided significantly different levels of support.[82] Based on its experience with the indexed cap on the existing high cost loop fund, the

[77] *See* 47 C.F.R. § 36.601(c). The Commission first adopted an indexed cap on the high cost loop fund in 1993 for a two year period, beginning January 1, 1994, based on the Commission's concern about wide fluctuations in the rate of annual growth of the high cost loop fund. *See* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, *Report and Order*, CC Docket 80-286, 9 FCC Rcd 303 (1993). The cap subsequently was extended for six months, until July 1, 1996. *See* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, *Report and Order*, CC Docket 80-286, 11 FCC Rcd 2538 (1996). On June 6, 1996, the Commission adopted the Joint Board's recommendation to extend the interim cap limiting growth in the existing high cost loop fund until the effective date of the rules the Commission adopted pursuant to section 254 of the Act and the Joint Board's recommendation. *See* Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Report and Order*, 11 FCC Rcd 7920 (1996).

[78] *Order*, 12 FCC Rcd at 8940.

[79] *Id. See also* 47 C.F.R. §§ 36.601(c), 36.622(c) and (d).

[80] *See* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, *Report and Order*, CC Docket 80-286, 9 FCC Rcd 303, 305 (1993). Prior to adoption of the indexed cap, the high cost loop fund had grown by approximately 60 percent in eight years, with annual rates of growth ranging from one percent to more than 19 percent. At that time, the Commission had proposed adopting a new high cost assistance program, and it anticipated that the cap would ease carriers' transition to the planned high cost assistance program. *Id.* at 305-06.

[81] *Order*, 12 FCC Rcd at 8930, 8940.

[82] *Order*, 12 FCC Rcd at 8940. By moderating potentially erratic growth in the high cost loop fund, the Commission found that continued use of the indexed cap should ease carriers' transition to a forward-looking economic cost mechanism, under which annual support amounts will become more predictable. *See id.*

Commission found, in the *Order*, that the cap "effectively limits overall growth of the fund, while protecting individual carriers from experiencing extreme reductions in support."[83]

2. Pleadings

29. Several petitioners challenge the Commission's continued imposition of a cap on the existing high cost loop fund on the basis that the cap violates the Act's requirement that universal service support be "sufficient."[84] Western Alliance claims that continuation of the indexed cap after the effective dates of sections 254(b)(5) and 254(e) of the Act is unlawful. Because there was no statutory requirement that universal service support be "sufficient" when the indexed cap was originally adopted, Western Alliance asserts that the cap is an "arbitrary reduction" of an eligible carrier's universal service support below the amount of support deemed "sufficient" under the Commission's rules.[85] RTC asserts that the Act's requirement of "sufficient" support does not justify continued application of the cap during the interim period while the Commission is developing a forward-looking economic cost mechanism. RTC claims that carriers should not be subject to the cap on the "mere assumption" that the Commission's efforts will lead to a forward-looking cost mechanism that "reduces support but still complies with the statute's ‘sufficient' and ‘predictable' requirement."[86]

30. In objecting to continuation of the indexed cap on high cost loop support, several petitioners argue that the indexed cap on the existing high cost loop fund also will operate to cap LTS and DEM weighting support levels.[87] Western Alliance claims that if the cap is not recalculated as of January 1, 1998, existing LTS and DEM weighting support for rural carriers will be "virtually eliminated by the indexed USF cap."[88] Petitioners opposing continuation of the indexed cap on high cost loop support urge the Commission to repeal the cap or, at a minimum, to adjust the cap to account for increases in LTS and DEM weighting support and to account for the addition of new rural carriers and new service areas not counted the previous year.[89]

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[83] *Order*, 12 FCC Rcd at 8930, 8940.

[84] Alaska Telephone petition at 3; RTC petition at 18-20; Western Alliance petition at 11-12; USTA petition at 16-18 (also arguing cap is contrary to Act's principle that the fund be "predictable").

[85] Western Alliance petition at 18-19.

[86] RTC petition at 19.

[87] Alaska Telephone petition at 3; RTC petition at 18-20; Western Alliance petition at 11-12; USTA petition at 16-17.

[88] Western Alliance petition at 12.

[89] RTC petition at 19-20; USTA petition at 16-17.

31. Several petitioners also claim that continued imposition of the cap is an arbitrary decision insofar as the cap will not accommodate certain legitimate cost increases for some carriers.[90] RTC charges that the cap excludes legitimate cost increases associated with new high cost loops and fails to reflect the addition of new eligible LECs, such as those in Guam.[91] Alaska Telephone asserts that the indexed cap "assumes that loop growth and changes in cost characteristics will be uniform throughout the whole country" and fails to take into account regional diversity, differing growth rates, disparate cost-of-living indexes, and the occurrence of natural disasters.[92] Western Alliance claims that increases in costs due to infrastructure upgrades and natural disasters for some carriers will reduce the proportion of support recovered by all eligible carriers.[93] RTC contends that the Commission's claim that the cap will prevent excessive growth in the size of the fund is "speculation" because the Commission fails to define "excessive growth" and ignores the cap's impact on quality of service.[94]

32. In their oppositions to these petitions, several parties support continuation of the indexed cap on the existing high cost loop fund.[95] AT&T maintains that the indexed cap applies only to the high cost loop component of universal service support and that LTS and DEM weighting support will be permitted to grow based on other provisions in the Commission's Part 54 rules. AT&T disputes RTC's suggestion that the cap is arbitrary and argues that the Commission's decision to continue the indexed cap is a prudent means of preventing excessive growth in the size of the fund.[96] AT&T claims that the successful operation of the cap is shown by the apparent absence of waiver requests that have been filed with the Commission seeking relief from harm allegedly caused by the cap, despite the fact that carriers experiencing significant adverse impacts were encouraged to submit waiver requests.[97] AT&T notes that the

[90] Alaska Telephone petition at 3; RTC petition at 18-19; Western Alliance petition at 11-12.

[91] RTC petition at 18, 20 (urging that the cap be recalculated to accommodate new high cost loops and new eligible carriers); *cf.* USTA petition at 17 (noting that the cap will need to be adjusted every year to include new recipients, but complaining that this "volatility will make the fund unpredictable, contrary to the principles of the Act.").

[92] Alaska Telephone petition at 3.

[93] Western Alliance at 11.

[94] RTC petition at 18-19.

[95] AT&T opposition at 12; Bell Atlantic opposition at 6; Airtouch opposition at 22.

[96] AT&T opposition at 12.

[97] AT&T opposition at 13 n.13.

waiver process remains open to any party that is significantly harmed by the cap.[98] Bell Atlantic asserts that petitioners have not demonstrated harm to any ratepayer due to the operation of the indexed cap and that petitioners merely posit hypothetical scenarios under which costs could rise sharply.[99] Bell Atlantic therefore argues that there is no justification for removing the cap for all carriers, but suggests that unforeseen circumstances may warrant revisiting the cap for a carrier or group of carriers that can demonstrate actual harm.[100]

33. In reply, RTC claims that supporters of continuation of the cap did not refute arguments that extending the cap is unlawful and contrary to the public interest.[101] USTA agrees with RTC that the Commission should require the cap to be recalculated each year to ensure that the loop count includes all local service providers. USTA agrees with AT&T that the cap applies only to the high cost loop component of universal service support, and asks the Commission to clarify that the cap does not apply to LTS and DEM weighting support.[102]

3. Discussion

34. We affirm the Commission's decision to retain the indexed cap on high cost loop support until all carriers receive support based on a forward-looking economic cost mechanism. For the reasons set forth below, we also reject petitioners' requests that we provide further adjustments to the cap beyond the adjustments that are required to occur, beginning on January 1, 1999, under our current rules.[103] As an initial matter, we are not persuaded by arguments that continuation of the indexed cap on high cost loop support will result in support that is not "sufficient." Much of petitioners' concern about the sufficiency of the modified existing system of universal service support appears to be based on their misapprehension that the indexed cap will operate after January 1, 1998 not merely to limit the growth of the high cost loop fund, but also to limit the growth of the modified DEM weighting and LTS programs. In light of this apparent confusion, we clarify here that the indexed cap on the high cost loop fund will not operate to cap support under the modified DEM weighting or LTS programs. Rather, local switching support and LTS will be calculated and permitted to increase based on the formulas

[98] AT&T opposition at 13 n.13.

[99] Bell Atlantic opposition at 7-8.

[100] *Id.*

[101] RTC reply at 4-5.

[102] USTA reply at 6.

[103] 47 C.F.R. § 36.601(c).

provided in sections 54.301 and 54.303, respectively.[104]

35. Section 36.601(c) of our rules sets forth the method for calculating the indexed cap and clearly provides that this limitation applies only to loop-related costs, not local switching support or long term support.[105] In addition, section 36.601(a) states that:

> [t]he term Universal Service Fund in subpart F refers only to the support for *loop-related costs* included in § 36.621. The term Universal Service in Part 54 refers to the comprehensive discussion of the Commission's rules implementing section 254 of the Communications Act of 1934, as amended . . . ."[106]

This clarification should alleviate any concern that the cap may result in insufficient support to the extent that these concerns are based on the erroneous premise that the indexed cap's limitation on growth of the high cost loop fund will limit the growth of the modified support programs adopted pursuant to Part 54 of our rules.

36. Petitioners have presented no new evidence that would lead us to depart from the Commission's earlier finding that the indexed cap on the high cost loop fund is a reasonable means of limiting the overall growth of the fund. We are not convinced that, simply because the cap was adopted prior to the imposition of a "sufficiency" requirement, the application of a cap necessarily fails to provide sufficient support. To the contrary, we agree with AT&T that the fact that no waiver requests have been filed by incumbent LECs during the more than three years that the indexed cap has been in effect suggests that the cap does not prevent carriers from receiving sufficient support. Moreover, parties have failed to present evidence, beyond mere generalizations, that the cap will result in insufficient support in the future. Absent specific evidence that the cap as modified in response to implementation of section 254 will likely result in insufficient support, which petitioners have not offered, we conclude that the cap is consistent with our obligation to ensure that support is sufficient.

37. We also are not persuaded by petitioners' arguments that the indexed cap on the high cost loop fund should be eliminated or recalculated. Contrary to RTC's assertion that the indexed cap does not take account of cost increases due to the addition of new high cost loops or new eligible carriers, we note that our rules provide for annual adjustments that will reflect such

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[104] 47 C.F.R. §§ 54.301, 54.303.

[105] 47 C.F.R. § 36.601(c) ("Limitations imposed by this subsection shall apply only to amounts calculated pursuant to this subpart F.").

[106] 47 C.F.R. § 36.601(a) (emphasis added).

growth. Specifically, section 36.601(c) provides:

> Beginning January 1, 1999, the total loop cost expense adjustment shall not exceed the total amount of the loop cost expense adjustment provided to rural carriers for the immediately preceding calendar year, *adjusted to reflect the rate of change in the total number of working loops of rural carriers* during the [preceding] calendar year . . . .[107]

Thus, both new high cost loops that eligible rural carriers add during the previous calendar year as well as high cost loops of newly eligible carriers that did not qualify as rural carriers in the previous calendar year will be factored into the calculation of the rate of change in the total number of working loops of rural carriers, pursuant to section 36.601(c). Accordingly, we find no basis for making additional adjustments to the indexed cap, beyond those already required by section 36.601(c).

38. We are similarly unpersuaded by Alaska Telephone and Western Alliance that the indexed cap on the high cost loop fund is unlawful because it fails to account for differences among carriers due to differing regional growth rates, infrastructure upgrade schedules, repair of disaster damage, or other circumstances that may be unique to particular carriers. We agree with Bell Atlantic that petitioners' claims of harm by operation of the cap under the new system of support are speculative. As noted by AT&T, a waiver process has been and remains available to carriers that may experience a significant adverse impact by operation of the cap.[108] We note again that the fact that no carrier has applied for relief under the Commission's waiver process or otherwise sought relief from the cap since it was first implemented in 1994 suggests that carriers have not experienced undue hardship because of the cap.[109]

39. We therefore affirm the Commission's previous finding that the cap is a reasonable means of limiting the overall growth of the high cost loop fund, and thus protecting contributors from excessive universal service contribution requirements, while allowing the high cost loop fund to grow to support the growth in lines served by carriers in high cost areas.

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[107] 47 C.F.R. § 36.601(c) (emphasis added).

[108] 47 C.F.R. § 1.3; *see also* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, *Report and Order*, CC Docket 80-286, 9 FCC Rcd 303, 305 (1993) ("[I]f circumstances change, the Joint Board encouraged recipients who would experience a significant adverse impact per loop per month [because of the indexed cap] to submit waiver requests, and we support that means of addressing any unforeseeable problems that may occur during the interim period [that the indexed cap is in effect]").

[109] 47 C.F.R. § 1.3.

B. DEM Weighting Assistance (Local Switching Support)

1. Calculation of Local Switching Support Based on Projections of Costs

a. Background

40. In 1987 the Commission created the Dial Equipment Minutes (DEM) weighting assistance program to provide additional assistance, apart from the assistance provided through the high cost loop fund, to smaller telephone companies.[110] Under the DEM weighting program a carrier serving 50,000 or fewer access lines may allocate a greater portion of its local switching costs to the interstate jurisdiction by multiplying (or "weighting") its interstate minutes by a factor, up to three, depending on the number of lines served. Thus, in the past, the DEM weighting program has shifted local switching costs from the intrastate jurisdiction to the interstate jurisdiction. The additional switching costs allocated to the interstate jurisdiction have been recovered from IXCs through local access charges for switching.[111]

41. In the *Order*, the Commission altered the recovery mechanism for local switching costs allocated to the interstate jurisdiction. The Commission found that DEM weighting was an implicit subsidy and, therefore, inconsistent with section 254(e) of the Act.[112] In recognition of section 254(e)'s directive to eliminate implicit support, the Commission replaced the local switching support that carriers had received through DEM weighting with explicit support from the new system of federal universal service support.[113] Consistent with this change, beginning January 1, 1998, a carrier formerly eligible to use DEM weighting will no longer be permitted to recover through access charges the portion of its local switching costs that are allocated to the interstate jurisdiction via the DEM weighting assistance program. Instead, the carrier's local switching access charges will be set using measured interstate DEM, and the portion of costs attributable to DEM weighting will be recovered from the new universal service support

[110] MTS and WATS Market Structure, CC Docket Nos. 78-72, 80-286, 86-297, *Report and Order*, 2 FCC Rcd 2639, 2641-2642 (1987). Under the current jurisdictional separations rules, LECs allocate their local switching costs between the state and interstate jurisdictions based on relative dial equipment minutes.

[111] For a further discussion of the DEM weighting assistance program, *see Order*, 12 FCC Rcd at 8892-93.

[112] *Order*, 12 FCC Rcd at 8892-93.

[113] *Order*, 12 FCC Rcd at 8940-41 (replacing DEM weighting subsidy program with section 254 program). *See also* Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charges, CC Docket Nos. 96-262, 94-1, 91-213, 95-72, *Order on Reconsideration*, FCC 97-247 (rel. July 10, 1997) (*Access Charge Reform Reconsideration Order*) at paras. 5-6. As required by section 254(d), the new program will be funded by providers of interstate telecommunications services. 47 U.S.C. § 254(d).

system.[114] Under the modified DEM weighting assistance program, the amount of local switching support that a qualifying carrier will receive will be calculated by multiplying the carrier's annual unseparated local switching revenue requirement by a local switching support factor. This local switching support factor will equal the difference between the 1996 weighted and unweighted interstate DEM factors, adjusted, if necessary, in successive years to reflect any increase in access lines.[115] The *Order* did not specify whether support for local switching costs under the modified DEM weighting assistance program will be based on projections of carriers' unseparated local switching revenue requirement or whether, as is the case under the existing high cost loop fund, support will be based on historical cost data.

b. Pleadings

42. Alaska Telephone and Western Alliance contend that the Commission's decision to remove the DEM weighting assistance program from the access charge system and transfer it to the new universal service system of support beginning January 1, 1998 will create a two-year lag in the receipt of DEM weighting assistance.[116] Petitioners observe that the current DEM weighting assistance program provides for the recovery of supported costs through interstate access charges, calculated on the basis of current cost data. Because local switching support will be recovered under the new universal service system of support, beginning January 1, 1998,

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[114] *Order*, 12 FCC Rcd at 8940-41; *Access Charge Reform Reconsideration Order* at paras. 5-6.

[115] 47 C.F.R. § 54.301. Section 54.301 was amended by the Accounting and Audits Division of the Commission's Common Carrier Bureau on December 3, 1997. Federal-State Joint Board on Universal Service and Changes to the Board of Directors of the National Exchange Carrier Association, Inc., CC Dockets. 96-45, 97-21, *Errata*, DA 97-2477 (Comm. Carr. Bur., Acct. & Audits Div. rel. Dec. 3, 1997) (*Universal Service Rules Errata*). As corrected, section 54.301 currently states:

> Beginning January 1, 1998, eligible rural telephone company study areas with 50,000 or fewer access lines shall receive support for local switching costs, defined as Category 3 local switching costs under Part 36, using the following formula: the carrier's annual unseparated local switching revenue requirement shall be multiplied by the local switching support factor. The local switching support factor shall be defined as the difference between the 1996 weighted interstate DEM factor, calculated pursuant to § 36.125(f) of this chapter, and the 1996 unweighted interstate DEM factor. If the number of a study area's access lines increases such that, under § 36.125(f) of this chapter, the weighted interstate DEM factor for 1997 or any successive year would be reduced, that lower weighted interstate DEM factor shall be applied to the carrier's 1996 unweighted interstate DEM factor to derive a new local switching support factor. Beginning January 1, 1998, the sum of the unweighted interstate DEM factor and the local switching support factor shall not exceed .85. If the sum of those two factors would exceed .85, the local switching support factor must be reduced to a level that would reduce the sum of the factors to .85.

[116] Alaska Telephone petition at 4; Western Alliance petition at 11.

petitioners assume that the Commission intended local switching support to be calculated on the basis of historical costs, which is the method used to calculate support under the existing high cost loop fund.[117] Petitioners contend that the Commission's determination to calculate local switching support based on historical costs will have an adverse impact on the cash flow of small carriers by creating a two-year lag in the recovery of local switching support.

c. Discussion

43. Although the Commission removed the DEM weighting assistance program from the access charge system and transferred it to the new universal service system of support, the Commission did not alter significantly the level of support received by carriers under this program. Indeed, in adopting the modifications to the existing support mechanisms, the Commission was persuaded that it should act more cautiously with respect to small rural carriers.[118] Therefore, the DEM weighting assistance program will continue to be administered and calculated separately from the existing high cost loop fund. Specifically, support payments for these local switching costs will be based on projections of annual costs, and, therefore, payments will not be lagged in the manner prescribed by our rules governing the existing high cost loop fund.[119]

44. Under the modified DEM weighting assistance program, a carrier will be eligible to receive local switching support based on the carrier's projected annual unseparated local switching revenue requirement for the upcoming calendar year, beginning January 1, 1998, and each year thereafter that DEM weighting assistance continues.[120] We amend section 54.301 by adding the word "projected" to the first sentence of that rule to clarify that support for local switching costs will be based on projections of costs and not historical cost data. As reflected in Appendix A hereto, section 54.301 is amended to read in relevant part:

> Beginning January 1, 1998, an incumbent local exchange carrier that has been designated an eligible telecommunications carrier and that serves a study area with 50,000 or fewer access lines shall receive support for local switching costs using the following

[117] Alaska Telephone petition at 4; Western Alliance petition at 11.

[118] *See, e.g., Order*, 12 FCC Rcd at 8938-39.

[119] As discussed below, we now adopt in this Order a "true-up" mechanism that will adjust the support amounts based on projected costs to reflect historical costs once the necessary data becomes available. This adjustment will occur within 15 months of the conclusion of each study period and will not result in delayed payments to carriers.

[120] Insofar as the *Order* did not specify a method for calculating the unseparated local switching revenue requirement, below we amend section 54.303 to provide the proper method of calculating that revenue requirement.

> formula: the carrier's *projected* annual unseparated local switching revenue requirement shall be multiplied by the local switching support factor.[121]

Thus, the Commission's determination to remove the DEM weighting assistance program from the access charge system and transfer it to the new universal service system of support will not create a two-year lag in the recovery of local switching investment, as argued by petitioners.

45. We also, on our own motion, amend section 54.301 to clarify that, to receive local switching support, an incumbent LEC must satisfy the requirements of an eligible telecommunications carrier.[122]

2. Calculating the Annual Unseparated Local Switching Revenue Requirement

a. Background

46. As explained above, under the modified DEM weighting assistance program, the amount of local switching support that an eligible carrier will receive beginning January 1, 1998, will be calculated by multiplying the carrier's projected annual unseparated local switching revenue requirement by a local switching support factor.[123] Section 54.301 of the Commission's rules sets forth the method for calculating the local switching support factor, but does not specify the method for calculating the annual unseparated local switching revenue requirement.[124]

47. In its October 31, 1997 report containing projections of demand for the modified DEM weighting assistance program, USAC reported that 1,092 study areas with 50,000 or fewer access lines are represented in the NECA traffic sensitive pool.[125] The report stated that an

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[121] 47 C.F.R. § 54.301(a)(1) (emphasis added).

[122] As reflected in the blocked text above, we replace the term "eligible rural telephone company" with the term "an incumbent local exchange carrier that has been designated an eligible telecommunications carrier" in section 54.301(a)(1). Further, to make our rules easier to read, we amend part 54.301 by adding subsections that make no substantive changes other than those explicitly adopted herein, as reflected in Appendix A.

[123] *See supra* section IV.B.1.a.

[124] 47 C.F.R. § 54.301.

[125] Universal Service Administrative Company, Federal Universal Service Programs-Fund Size Projections and Contribution Base for First Quarter 1998 at 7 (filed Oct. 31, 1997) (*USAC Universal Service Oct. 1997 Filing*). Although most carriers that qualify for DEM weighting participate in NECA pools, pool participation is not a condition of receiving DEM weighting assistance. For carriers that participate in the NECA traffic sensitive pool, the weighted

additional 196 study areas with fewer than 50,000 access lines are not represented in this pool.[126] The report stated that, when the Commission adopts a mechanism for computing unseparated local switching support, "USAC will issue a data request to obtain actual support requirements from the individual study areas that qualify for local switching support."[127] The report also stated that NECA had devised a formula for calculating the unseparated local switching revenue requirement for average schedule companies.[128]

b. Pleadings

48. GVNW and NECA comment that the Commission's rules do not provide a method for calculating a carrier's annual unseparated local switching revenue requirement.[129] Noting that carriers currently use various methods for determining the unseparated local switching revenue requirement, GVNW lists five possible methods.[130] Due to its simplicity, GVNW recommends a method for calculating the annual local switching revenue requirement that is accomplished by dividing the interstate local switching revenue requirement by the interstate DEM weighting factor that is used to assign the local switching investment to the interstate jurisdiction under our Part 36 rules.[131] NECA recommends a method for calculating the unseparated local switching revenue requirement that is similar to GVNW's fifth proposal and similar to the method NECA currently uses to calculate high cost loop assistance and assign

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DEM costs have been allocated to the switching rate element of NECA's traffic sensitive rate. If a carrier receiving DEM weighting assistance is not a member of the traffic sensitive pool, that carrier will recoup these weighted DEM charges through its own access rates.

[126] *USAC Universal Service Oct. 1997 Filing* at 8.

[127] *USAC Universal Service Oct. 1997 Filing* at 9 n.19.

[128] *USAC Universal Service Oct. 1997 Filing* at 7, Exh. 1.

[129] GVNW petition at 12-14; NECA petition at 8.

[130] GVNW petition at 13-14. The five possible methods for calculating the unseparated local switching revenue requirement offered by GVNW include the following: (1) Perform a special Part 36 study using the interstate rate of return and isolate the costs associated with local switching investment; (2) Divide the interstate local switching revenue requirement by the interstate local switching factor that was used to assign the portion of interstate investment; (3) Perform a Part 69 study on the unseparated costs subject to separations; (4) Divide the interstate local switching revenue requirement by the interstate switching investment to develop an annual carrying charge and then multiply the total unseparated local switching investment by the annual charge factor to determine the unseparated local switching revenue requirement; (5) Adopt a rule that requires the use of specific Part 32 accounts to determine the unseparated local switching revenue requirement. This final method would be similar to the process currently being used by NECA to determine the unseparated loop cost by study area for administration of the existing high cost loop fund. *Id.*

[131] GVNW petition at 13.

interstate costs to the local switching rate element under the Commission's Part 69 rules. NECA's proposal is based on specified account and cost data that carriers maintain pursuant to the Commission's Part 32 rules.[132] NECA asserts that the use of Part 32 account data as detailed in NECA's October 30, 1997 and December 4, 1997 letters represents the most accurate method of calculating the unseparated local switching revenue requirement.[133]

c. Discussion

49. We adopt the method of calculating the annual unseparated local switching revenue requirement proposed in NECA's *ex parte* letters because it provides the most accurate calculation of the local switching revenue requirement. Under this method, a carrier's annual unseparated local switching revenue requirement will be calculated pursuant to a formula that relies upon specified account and cost data that carriers maintain pursuant to the Commission's Part 32 rules. Thus, as reflected in our amendments to Part 54 in Appendix A hereto, we direct the Administrator to use the Part 32 account data as specified in NECA's October 30th, 1997 and December 4, 1997 letters to determine the unseparated local switching revenue requirement. Consistent with our adoption of a methodology that relies upon Part 32 account data, we authorize the Administrator to issue a data request annually to the carriers that serve study areas with 50,000 or fewer access lines but that are not members of the NECA traffic sensitive pool in order to obtain the relevant Part 32 data from these carriers.[134] Because the Administrator requires data to calculate local switching support in 1998 from carriers that do not participate in the NECA common line pool, we direct the Administrator to issue a data request to those carriers as soon as practicable after the release of this Order. We note that, as with all high cost support, a competitive local exchange carrier will receive the same amount of local switching support formerly received by an incumbent LEC if the competitive local exchange carrier begins to serve a customer formerly served by an incumbent LEC receiving local switching support for that customer.[135]

50. We conclude that GVNW's proposal to calculate the local switching revenue requirement by dividing the interstate local switching revenue requirement by the interstate DEM weighting factor that is used to assign the local switching investment to the interstate jurisdiction

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[132] Letter from Robert Haga, NECA, to William F. Caton, FCC, dated October 30, 1997, attachment. *See* 47 C.F.R. Part 32.

[133] Letter from Robert Haga, NECA, to William F. Caton, FCC, dated October 30, 1997, attachment; Letter from Robert Haga, NECA, to Magalie Roman Salas, FCC, dated December 4, 1997, attachment.

[134] This information collection is subject to the approval of the Office of Management and Budget.

[135] *See Order*, 12 FCC Rcd at 8932-34, 8944-45; 47 C.F.R. § 54.307.

under Part 36 of our rules would not provide as accurate a measure of the unseparated local switching revenue requirement as the methodology we adopt. If all local switching expenses and investment used to determine the revenue requirement for the local switching rate element were allocated between the interstate and intrastate jurisdictions on the basis of weighted DEM, the formula suggested by GVNW would produce an accurate calculation of the unseparated local switching revenue requirement. Weighted DEM, however, is only one of several mechanisms used to allocate local switching expenses and investment between the interstate and intrastate jurisdictions for purposes of determining local switching access charges. The Commission's rules prescribe different allocators for other local switching expenses and related investment, such as those associated with general support facilities. We conclude that the approach suggested by NECA, because it allocates local switching expenses and related investment in a manner that is consistent with the allocation methods prescribed under Parts 36 and 69 of our rules, provides a more accurate method for calculating the unseparated local switching revenue requirement. Because all carriers, including small carriers, already maintain the information necessary to calculate the local switching revenue requirement and because carriers must already submit similar information to the Administrator for high cost loop support, we conclude that any additional burden placed on carriers will be small, and that the benefits of using a more accurate method will outweigh any additional burden placed on carriers.

51. In its October 31, 1997 report containing projections of demand for the modified DEM weighting assistance program, USAC reported that NECA had devised a formula for calculating the unseparated local switching revenue requirement for average schedule companies.[136] For average schedule companies, local switching support will be calculated in accordance with a formula that the Administrator will submit annually to the Commission for review and approval. The formula submitted by the Administrator will be designed to produce disbursements to an average schedule company to simulate the disbursements that would be received pursuant to section 54.301 by a company that is representative of average schedule companies. We delegate to the Chief, Common Carrier Bureau the authority to review, modify, and approve the formula submitted by the Administrator.

3. True-up Mechanism for Adjusting Local Switching Revenue Requirement

a. Background

52. As noted above, DEM weighting support payments under the modified DEM weighting assistance program will continue to be based on projections of costs, not on historical

[136] *USAC Universal Service Oct. 1997 Filing* at 7, Exh. 1.

cost data.[137] The Commission's rules are silent as to whether adjustments to the local switching support should be made to reflect carriers' historical switching costs.

b. Pleadings

53. Given that the Administrator will be relying on projections of costs to determine DEM weighting support for 1998, NECA asks the Commission to provide a mechanism for correcting errors resulting from the use of projected costs.[138] NECA points out that the historical 1998 local switching revenue requirement will not be known until cost studies are completed in late 1999. NECA notes that its current pooling procedures permit carriers to recover historical, or "trued-up," interstate costs from the NECA traffic sensitive pool for a period of up to 24 months after the month the projected costs are submitted to NECA.[139] NECA asserts that, in order to ensure that the modified DEM weighting assistance program is neither over- nor under-funded, there will be an ongoing need to adjust support levels in the future to reflect historical costs in current or prior funding years.[140] NECA proposes that projected local switching support be reconciled with historical local switching costs within 15 months from the end of the relevant study period.[141]

c. Discussion

54. We agree with NECA that the Administrator should adjust DEM weighting support levels to correct errors that may result from the use of projected local switching costs. Accordingly, we direct the Administrator to adjust annually the levels of local switching support projected for each study period to reflect the historical support requirements determined from the data filed by the carrier for that study period.[142] As a result, a carrier's local switching support

[137] *See supra* section IV.B. Section 54.301 of the Commission's rules provides that, beginning January 1, 1998, local switching support will be calculated by multiplying an eligible carrier's projected annual unseparated local switching revenue requirement by the local switching support factor, which is defined as the difference between the 1996 weighted and unweighted interstate DEM factors, adjusted thereafter, if necessary, to reflect access line growth. 47 C.F.R. § 54.301.

[138] NECA petition at 5.

[139] NECA petition at 5 n.14.

[140] NECA petition at 7. *See also* Letter from Robert Haga, NECA, to William F. Caton, FCC, dated October 30, 1997 (asserting that a true-up mechanism is necessary to maintain the accuracy and integrity of the local switching support payments from the modified universal service support programs).

[141] Letter from Robert Haga, NECA, to William F. Caton, FCC, dated October 30, 1997.

[142] To illustrate, the amount a carrier would otherwise receive for any given year will be increased or decreased by the "true-up" amount.

will not be delayed until historical data are available, but, after the adjustment, such support will accurately reflect a carrier's historical costs. As proposed by NECA, we conclude that all such adjustments must be made within 15 months of the conclusion of the relevant study period.[143] We emphasize that, unlike the current high cost loop data submissions, all carriers must submit accurate, historical data when they become available and that the Administrator must increase or decrease a carrier's subsequent payments by the amount that the cost projection for that carrier differs from the costs which are in fact incurred.[144]

55. We note that local switching support also may be affected by changes in the weighting factor resulting from the number of lines served by a carrier. As provided in section 54.301 of the Commission's rules, "[i]f the number of a study area's access lines increases such that, under § 36.125(f) of this chapter, the weighted interstate DEM factor . . . would be reduced, that lower weighted interstate DEM factor shall be applied to the carrier's 1996 unweighted interstate DEM factor to derive a new local switching support factor."[145]

C. Long Term Support (LTS)

1. LTS Background

56. Currently the Commission's separations rules assign 25 percent of incumbent LECs' loop costs to the interstate jurisdiction.[146] Incumbent LECs have previously recovered these interstate allocated loop costs through subscriber line charges (SLCs) and carrier common line (CCL) charges.[147] Prior to 1989, all incumbent LECs were required to participate in the

[143] Thus, for example, for the 1998 calendar year, the true-up period will extend for 15 months beyond the end of 1998, until April 1, 2000.

[144] We note that the Commission has previously designated for investigation NECA's resizing adjustment for high cost loop support. 1997 Annual Access Tariff Filings, National Exchange Carrier Association Universal Service Fund and Lifeline Assistance Rates Transmittal No. 759, CC Docket No. 97-149, *Memorandum Opinion and Order*, DA 97-1350 at para. 73 (Comm. Carr. Bur. rel. June 27, 1997). The true-up adjustment we are adopting for local switching support does not raise the same concerns as the high cost loop adjustment because the submission of historical data is mandatory, and carriers' payments will increase or decrease consistent with the historical data submitted. *Compare* 47 C.F.R. § 36.612 *with* 47 C.F.R. § 54.301(e).

[145] 47 C.F.R. § 54.301(a)(2)(ii).

[146] 47 C.F.R. § 36.154(c). The jurisdictional separations process divides between the state and federal jurisdictions the costs of those portions of the incumbent LECs' telephone plant that are used for interstate and intrastate services. Each jurisdiction then specifies how rate-regulated incumbent LECs may recover the costs assigned to that jurisdiction.

[147] *See supra* section IV.A.1.

common line pool administered by NECA and were also required to charge IXCs a CCL charge equal to the average rate of all pool members.[148] When individual incumbent LECs were allowed to leave the pool in 1989, they were required to contribute to the pool in order to prevent the CCL charges of incumbent LECs that remained in the pool from rising significantly above the national average.[149] The incumbent LECs that have left the pool since 1989 are predominantly the larger, lower-cost incumbent LECs and those that have remained in the pool typically are smaller, higher-cost incumbent LECs.[150] The incumbent LECs that contribute to LTS recover the cost of their payments by increasing their own CCL charges.[151] The incumbent LECs that remain in the pool are able to set their CCL charge at the nationwide average CCL rate because the LTS payments make up the difference between the pool participants' carrier common line revenue requirement and the revenue received from the pool's CCL charges.

57. In the *Order*, the Commission concluded that the former LTS program is inconsistent with the Act's requirements that support be collected from all providers of interstate telecommunications services on a non-discriminatory basis[152] and be available to all eligible telecommunications carriers.[153] Accordingly, the Commission removed the LTS program from the access charge system.[154] The Commission found, however, that the LTS program serves the public interest by reducing the amount of loop costs that high cost LECs must recover from IXCs

[148] The Commission adopted a schedule in 1987 which allowed incumbent LECs to withdraw from the pool no later than June 1989. MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, CC Docket Nos. 78-72, 80-286, *Report and Order*, 2 FCC Rcd 2953, 2956-58 (1987) (*1987 Part 67 Order*); *Order*, 12 FCC Rcd at 9163. NECA administers the current national loop-cost pool, and files a CCL tariff for pool participants.

[149] *1987 Part 67 Order*, 2 FCC Rcd 2953, 2956-58. Once incumbent LECs withdraw from the pool, they may not choose to participate in the pool at a later date. MTS and WATS Market Structure, Amendment of Part 67 of the Commission's Rules and Establishment of a Joint Board, CC Docket Nos. 78-72, 80-286, *Memorandum Opinion and Order on Reconsideration and Order Inviting Comments*, 3 FCC Rcd at 4557 n.17 (1988) (*Part 67 Reconsideration Order*).

[150] *See* FEDERAL AND STATE STAFF FOR THE 80-286 FEDERAL-STATE JOINT BOARD, MONITORING REPORT, CC Docket 87-339 at 651 (1997). By leaving the pool, a carrier would gain the flexibility to set its own CCL rate. A carrier's desire to convert to price cap company status also may influence that carrier's decision to leave the pool.

[151] *Order*, 12 FCC Rcd at 9163.

[152] 47 U.S.C. § 254(d).

[153] 47 U.S.C. § 254(e). Under the former LTS system, only incumbent LECs participating in the NECA CCL tariff could receive LTS support and only incumbent LECs that did not participate in the NECA CCL tariff made LTS payments. *Order*, 12 FCC Rcd at 9164-65.

[154] *Order*, 12 FCC Rcd at 9164-65 and n.1946.

through CCL charges and thereby facilitating interexchange service in high cost areas consistent with the express goals of section 254.[155] The Commission therefore concluded that eligible telecommunications carriers should receive support comparable to LTS from the new universal service support system.[156]

58. The Commission determined that support will be computed for each incumbent LEC currently receiving LTS, based on the level of LTS that the carrier would receive under the existing LTS program, adjusted to reflect the annual percentage change in the actual nationwide average cost per loop in 1998 and 1999 and adjusted, thereafter, by an inflation factor.[157] Section 54.303 of the Commission's rules provides that LTS will equal the difference between the projected CCL revenue requirement of NECA common line tariff participants and the projected revenue recovered by the NECA CCL charge, calculated pursuant to section 69.105(b) of the Commission's rules.[158] Section 69.105(b) currently sets the NECA pool rate at the average of price-cap incumbent LECs' CCL charges.[159] After January 1, 1998, however, the pool rate will no longer be calculated in this manner.[160] On October 8, 1997, the Commission granted NECA's

[155] *Order*, 12 FCC Rcd at 9165.

[156] *Order*, 12 FCC Rcd at 9164-65.

[157] *Order*, 12 FCC Rcd at 8942. Beginning January 1, 2000, LTS will be adjusted to reflect the annual percentage change in the Department of Commerce's Gross Domestic Product-Chained Price Index (GDP-CPI). 47 C.F.R. § 54.303.

[158] 47 C.F.R. § 54.303. Section 54.303 was amended in an errata released by the Accounting and Audits Division of the Commission's Common Carrier Bureau on December 3, 1997. *Universal Service Rules Errata*. As corrected, section 54.303 currently states:

> Beginning January 1, 1998, eligible telephone companies that participate in the association Carrier Common Line pool and competitive eligible local telecommunications carriers will receive Long Term Support. Long Term Support shall be the equivalent of the difference between the projected Carrier Common Line revenue requirement of association Common Line tariff participants and the projected revenue recovered by the association Carrier Common Line charge as calculated pursuant to § 69.105(b)(2) of this chapter. For calendar years 1998 and 1999, the Long Term Support for each eligible service area shall be adjusted each year to reflect the annual percentage change in the actual nationwide average loop cost as filed by the Administrator in the previous calendar year, pursuant to § 36.622 of this chapter. Beginning January 1, 2000, the Long Term Support shall be adjusted each year to reflect the annual percentage change in the Department of Commerce's Gross Domestic Product-Chained Price Index (GDP-CPI).

[159] 47 C.F.R. § 69.105(b).

[160] *See Order*, 12 FCC Rcd at 9165, 9169-70. In the *Order*, the Commission observed that the replacement of LTS with per-line support from the new universal service support system would require changes to our rules governing calculation of CCL charges and would be addressed in the access charge reform proceeding. *Id.* In the *Access Charge*

petition for waiver of section 69.105(b)(2)-(3) for purposes of calculating the NECA pool rate that will become effective January 1, 1998.[161] In granting NECA's petition for waiver of section 69.105(b)(2)-(3), the Commission made no change to section 69.105(b), which sets forth the method of calculating the NECA CCL charge.

2. Technical Amendments to Section 54.303 Governing Calculation of LTS

a. Pleadings

59. GVNW asserts that the method for calculating LTS for 1998 under section 54.303 is unclear.[162] GVNW identifies three possible methods for calculating 1998 LTS that would be supported by the current rule.[163] No party commented on GVNW's petition with respect to this issue. In addition, NECA asserts that the reference to "average loop cost" in section 54.303 of the Commission's rules is unclear because it could be read to refer only to changes in loop costs, not numbers of loops.[164] NECA suggests that the proper calculation should reflect both the percentage change in actual nationwide average loop costs and the numbers of working loops for

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Reform Order, the Commission postponed making conforming revisions to section 69.105(b) regarding the CCL rate calculation for NECA tariff participants based on its plan to address this issue in a proceeding on access charge reform for small, non-price cap LECs. *Access Charge Reform Order* at paras. 374-77. NECA subsequently petitioned the Commission to revise our rules governing the calculation of NECA CCL rates without waiting for conclusion of the other proceeding or, in the alternative, to issue an order waiving section 69.105(b)(2)-(3) for NECA's common line pool participants, so as to allow NECA to reflect revised LTS formula amounts in its CCL tariff rates effective January 1, 1998. On October 8, 1997, the Commission adopted the *Access Charge Reform Second Reconsideration Order*, which, in relevant part, granted NECA's waiver request on the condition that NECA compute the CCL charge as set forth therein. Access Charge Reform, *et al.*, CC Docket No. 96-262, *et al., Second Order on Reconsideration and Memorandum Opinion and Order*, FCC 97-368 at paras. 4, 89 (rel. Oct. 9, 1997) (*Access Charge Reform Second Reconsideration Order*).

[161] *Access Charge Reform Second Reconsideration Order* at para 89.

[162] GVNW petition at 14-16.

[163] GVNW petition at 14-16. GVNW proposes the following possibilities: (1) Adopt the NECA total common line pool method under which the percentage of the NECA pool LTS to the total common line pool would be applied to each participant's total common line requirement to determine that participant's LTS for the year; (2) Develop the ratio of LTS support to the CCL requirement using the CCL requirement rather than the total common line requirement, thus excluding the end user common line portion of the CCL requirement; (3) Calculate each participant's LTS support for 1997 by starting with its total common line revenue requirement for 1997, subtracting out the amount of revenue received for 1997 from SLCs and from CCL charges. *Id.*

[164] NECA petition at 7.

all eligible telecommunications carriers.[165] No party commented on NECA's petition with respect to this issue.

b. Discussion

60. In response to GVNW's petition, we amend section 54.303 of our rules, as set forth below, to specify how LTS will be calculated for 1998. First, we clarify that currently, and until January 1, 1998, LTS support is based on the difference between the NECA common line pool revenue requirement and the sum of the revenues obtained from charging a nationwide CCL rate calculated pursuant to section 69.105(b)(2) and the revenues obtained through SLCs.[166] This clarification is necessary because the *Order* and section 54.303 failed to account for the portion of the common line revenue requirement that is recovered through end user common line charges, or SLCs. We therefore amend section 54.303 to include "end user common line charges."

61. We also clarify the procedure by which LTS support will be calculated after January 1, 1998. Prior to the modifications adopted in the *Order*, NECA calculated LTS using revenue requirement projections calculated pursuant to section 69.105(b)(2) of our rules. After January 1, 1998 we will no longer use these annual projections. Instead, we will index 1997 levels of support to reflect annual changes in loop costs. Specifically, in 1998 and 1999 LTS support will be calculated by adjusting previous support levels by the annual percentage change in the actual nationwide average cost per loop, and beginning January 1, 2000, LTS will be adjusted to reflect the annual percentage change in the Department of Commerce's GDP-CPI.[167] Thus, under the modified LTS program adopted in the *Order*, the Administrator will make an initial, one-time calculation of projected 1997 LTS revenue requirements of eligible carriers in service areas served by incumbent LECs that currently participate in the NECA common line pool. These projected 1997 LTS revenue requirements will be adjusted according to a rate of change that will reflect annual changes in loop costs as prescribed by section 54.303.

62. Because LTS levels for 1998 and beyond will be based on 1997 projections, we conclude that the methodology for calculating the NECA CCL charge contained in section 69.105(b)(2) should be used only for the 1997 projections. Therefore, section 54.303 now directs the Administrator to calculate only the base-level of LTS using the projected revenue recovered

[165] NECA petition at 7.

[166] The NECA CCL charge calculation set forth in the *Access Charge Reform Second Reconsideration Order* reflects that the CCL charge, rather than LTS, will be a residual amount as of January 1, 1998. *Access Charge Reform Second Reconsideration Order* at para. 89. This proposal is similar to GVNW's third proposal. *See* GVNW petition at 15-16.

[167] 47 C.F.R. § 54.303.

by the CCL charge in 1997 as calculated pursuant to section 69.105(b)(2) of our rules. Consistent with these clarifications, we amend section 54.303 to specify that the Administrator will calculate the unadjusted base-level of LTS for 1998 by calculating the difference between the projected Common Line revenue requirement of NECA Common Line tariff participants projected to be recovered in 1997 and the sum of end user common line charges and the 1997 projected revenue recovered by the CCL charge as calculated pursuant to section 69.105(b)(2) of our rules.[168] As reflected in Appendix A hereto, section 54.303 is amended to read in relevant part:

> *To calculate the unadjusted base-level of* Long Term Support *for 1998* the Administrator shall calculate the difference between the projected Common Line revenue requirement of association Common Line tariff participants *projected to be recovered in 1997* and the sum of *end user common line charges and* the *1997* projected revenue recovered by the association Carrier Common Line charge as calculated pursuant to § 69.105(b)(2) of this chapter.[169]

63. In the *Order*, the Commission stated that an eligible carrier's LTS will be based on the LTS received for the preceding calendar year, adjusted in 1998 and 1999 to reflect the percentage increase in the nationwide "average loop cost."[170] We are persuaded by NECA's comments that the phrase "average loop cost" in section 54.303 could be misinterpreted and that it would be preferable to use the terminology used elsewhere in our rules, i.e., "average unseparated loop cost per working loop." Accordingly, we also amend section 54.303 by striking the phrase "average loop cost" and replacing it with "average unseparated loop cost per working loop." As reflected in Appendix A hereto, section 54.303 is amended to instruct the Administrator to adjust the levels of LTS for 1998 and 1999 to "reflect the annual percentage change in the actual nationwide *average unseparated loop cost per working loop*."[171]

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[168] We note, however, that beginning January 1, 1998, the Administrator will no longer rely upon section 69.105(b)(2) to calculate the NECA CCL charges. Subsequently, as indicated in the *Order*, LTS support will be adjusted to reflect the annual percentage change in the actual nationwide average cost per loop in 1998 and 1999 and adjusted, thereafter, by an inflation factor. *Order*, 12 FCC Rcd at 8942. Beginning January 1, 2000, LTS will be adjusted to reflect the annual percentage change in the Department of Commerce's GDP-CPI. 47 C.F.R. § 54.303.

[169] 47 C.F.R. § 54.303 (emphasis added).

[170] *Order*, 12 FCC Rcd at 8942. As discussed in detail below, a competitive eligible telecommunications carrier is eligible to receive universal service support to the extent that the competitive eligible telecommunications carrier captures an incumbent LEC's subscriber lines or serves new subscribers in the incumbent LEC's service area. *See* 47 C.F.R. § 54.307(a).

[171] 47 C.F.R. § 54.303 (emphasis added).

64. On our own motion, we also amend section 54.303 to clarify that an incumbent LEC that participates in the NECA common line pool also must satisfy the requirements of an eligible telecommunications carrier in order to receive LTS. Accordingly, section 54.303 is amended to read in relevant part:

> Beginning January 1, 1998, an *eligible telecommunications carrier* that participates in the association Common Line pool *shall* receive Long Term Support.[172]

3. Calculation of LTS Levels Based on Projections of Costs

a. Pleadings

65. Alaska Telephone and Western Alliance contend that the Commission's decision to remove the LTS program from the access charge system and transfer it to the new system of universal service support, beginning January 1, 1998, will create a two-year lag in the receipt of LTS.[173] Petitioners observe that the current LTS program provides for the recovery of supported costs through interstate access charges, calculated on the basis of current cost data. Because LTS will be recovered under the new universal service support system, beginning January 1, 1998, petitioners assume that the Commission intended LTS to be calculated on the basis of historical costs, which is the method used to calculate support under the existing high cost loop fund.[174] Petitioners contend that the Commission's determination to calculate LTS based on historical costs will impact adversely the cash flow of small carriers by creating a two-year lag in the recovery of LTS supported costs. No party commented on Alaska Telephone's and Western Alliance's petitions with respect to this issue.

b. Discussion

66. The Commission's determination to remove the LTS program from the access charge system and transfer it to the new support system will not create a two-year lag in the recovery of LTS supported costs, as argued by petitioners. In 1998, support payments provided to eligible carriers under the modified LTS program will be based not on historical cost data, which is the method of calculating support under the existing high cost loop fund, but, instead,

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[172] 47 C.F.R. § 54.303 (emphasis added). To make our rules easier to read, we also amend part 54.303 by adding subsections that make no substantive changes other than those explicitly adopted here, as reflected in Appendix A.

[173] Alaska Telephone petition at 4; Western Alliance petition at 11.

[174] Alaska Telephone petition at 4; Western Alliance petition at 11.

will be based on 1997 projections. Section 54.303, as modified above, now explicitly states that LTS support in the first year will be calculated based on the difference between the 1997 *projected* common line revenue requirement of NECA pool participants and the projected revenue recovered by the 1997 NECA CCL charge and SLCs.[175] Beginning January 1, 1998, LTS payments will be adjusted for all recipients based on average rates of change as provided in section 54.303.[176] Because support will be based on projections using a rate of change, historical data will no longer be used and there will be no basis for delaying LTS payments.

4. True-up Mechanism to Adjust Base-Level of LTS

a. Pleadings

67. Noting that the new universal service rules require the Administrator to rely on cost projections to determine the LTS levels for 1998, NECA asks the Commission to provide a mechanism for correcting errors resulting from the use of these cost projections.[177] NECA points out that, although our rules provide that LTS be calculated using 1997 LTS levels, beginning January 1, 1998, final data for calculating 1997 LTS amounts will not be available until cost studies for 1997 are completed during calendar year 1998.[178] NECA's current pooling procedures permit carriers to recover "trued-up" interstate costs from the common line pool for a period of up to 24 months after the month the projected costs are submitted to NECA.[179] NECA urges the Commission to adopt a true-up mechanism in order "to maintain the accuracy and integrity" of LTS payments under the modified LTS program.[180] NECA proposes that the 1998 LTS projections be reconciled with historical LTS requirements within 15 months from the end of the 1997 study period.[181] No party commented on NECA's petition with respect to this issue.

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[175] 47 C.F.R. § 54.303.

[176] Specifically, in 1998 and 1999 LTS will be adjusted by the annual percentage change in the average unseparated loop cost per working loop. Beginning January 1, 2000, LTS will be adjusted to reflect the annual percentage change in the Department of Commerce's Gross Domestic Product-Chained Price Index (GDP-CPI). *See* 47 C.F.R. § 54.303.

[177] NECA petition at 5. As clarified above, section 54.303 of the Commission's rules provides that initial levels of LTS will be calculated based on the difference between the 1997 *projected* common line revenue requirement of NECA common line pool participants and projected revenues recovered by the 1997 NECA CCL charge and SLCs.

[178] NECA petition at 5 n.14.

[179] NECA petition at 5 n.14.

[180] Letter from Robert Haga, NECA, to William F. Caton, FCC, dated October 30, 1997.

[181] *Id.*

b. Discussion

68. Pursuant to section 54.303, the unadjusted base-level of LTS initially will be calculated using 1997 projections. To ensure that the modified LTS program is funded at appropriate levels, however, we direct the Administrator to adjust the base-level of LTS to reflect historical 1997 costs once those data become available to the Administrator. As proposed by NECA, we conclude that this adjustment should be made within fifteen months of the conclusion of the 1997 calendar year.[182] We emphasize that, unlike the current high cost loop data submissions, all carriers must submit historical cost data for 1997. We direct the Administrator to increase or decrease a carrier's LTS payment to reflect 1997 costs that in fact incurred no later than 15 months after the end of the 1997 calendar year.[183] We note that, unlike the DEM weighting assistance program, which will require ongoing adjustments, the adjustment that we direct the Administrator to make to the LTS program will be needed only to adjust the base-level of LTS.

5. Membership in NECA Common Line Pool a Requirement for LTS

a. Pleadings

69. Several petitioners request that the Commission eliminate the requirement that rural carriers participate in the NECA common line pool in order to receive LTS or clarify that the Commission did not intend to require participation in the pool as a condition for receiving LTS.[184] USTA argues that there is no compelling reason to require continued membership in the pool once the Administrator establishes a carrier's LTS amount, which is based on pool membership as of January 1, 1998.[185] USTA argues further that revising the rule to permit telephone companies to exit the pool without losing LTS would be consistent with the Commission's determination that LTS is designed to protect customers from abrupt increases in the NECA CCL rate.[186] ALLTEL contends that, with the "de-linkage" of LTS from interstate

[182] Thus, for example, the true-up period will extend for 15 months beyond the end of 1997, or April 1, 1999.

[183] Like the true-up mechanism we adopt for local switching support, the LTS true-up mechanism does not raise the same concerns as the current high cost loop adjustment that has been designated for investigation by the Commission. *See* 1997 Annual Access Tariff Filings, National Exchange Carrier Association Universal Service Fund and Lifeline Assistance Rates Transmittal No. 759, CC Docket No. 97-149, *Memorandum Opinion and Order*, DA 97-1350 at para. 73 (Comm. Carr. Bur. rel. June 27, 1997). *See supra* section IV.B.3.c.

[184] *See, e.g.*, ALLTEL petition at 2-4; GVNW petition at 16; USTA petition at 12-13.

[185] USTA petition at 12.

[186] *Id.*

access charges, membership in the NECA common line pool is an arbitrary requirement.[187] ALLTEL argues that, if the Commission determines to provide LTS to rural incumbent LECs that are outside the pool, the Commission will enable rural incumbent LECs that achieve efficiencies, relative to other pool members, to leave the pool and reflect those efficiencies in the interstate rates charged to their access customers.[188]

70. GVNW argues that, in order to preserve competitive neutrality between an incumbent LEC and a competitive eligible telecommunications carrier that serves customers in the incumbent LEC's service area, the incumbent LEC should continue to receive LTS after it exits the pool.[189] GVNW asserts that denying LTS to the exiting incumbent LEC in this situation would not be competitively neutral because, according to GVNW, the competitive carrier would continue to receive LTS based on the incumbent LEC's prior level of support, even though the incumbent LEC could no longer receive LTS.[190]

71. If the Commission determines that non-pooling rural incumbent LECs are not eligible for LTS, GVNW argues, it would be reasonable for the Commission to permit non-pooling rural incumbent LECs to receive support based on forward-looking economic cost given that non-rural LECs will be eligible to receive universal service support based on forward-looking economic cost beginning January 1, 1999.[191] ALLTEL argues that rural incumbent LECs that have left the NECA pool should be permitted to receive LTS beginning January 1, 1998, on a per-line basis equal to the pooling companies' per-line LTS and, after January 1, 1999, such companies should have the option of using proxy models on a study area by study area basis to determine their universal service support.[192]

72. AT&T opposes petitioners' request that the Commission make LTS payments available to all rural LECs irrespective of NECA common line pool participation.[193] AT&T argues that an incumbent LEC's decision to leave the pool is likely due to the fact that the incumbent LEC has achieved efficiencies that render the incumbent LEC a contributor to the

[187] ALLTEL petition at 3.

[188] *Id.*

[189] GVNW petition at 16.

[190] *Id.*

[191] GVNW petition at 16.

[192] ALLTEL petition at 4-6.

[193] AT&T opposition at 11.

pooled revenue requirement rather than a receiver.[194] Therefore, the purpose of LTS payments, namely, to permit carriers with higher-than-average loop costs that are NECA common line pool members to charge nationwide average interstate rates, no longer applies to incumbent LECs that have elected to exit the pool.[195] AT&T argues further that, to ensure competitive neutrality, if an incumbent LEC leaves the pool and loses its LTS, support should be withdrawn from any competitive eligible telecommunications carrier receiving support in the incumbent LEC's territory.

73. In reply, USTA reiterates its view that there is no reason why incumbent LECs should be required to remain in the NECA common line pool to receive support, but concurs with AT&T that, if an incumbent LEC loses LTS, so should any eligible telecommunications carrier receiving LTS in the incumbent's territory.[196]

b. Discussion

74. We reiterate that an incumbent LEC's continued membership in the NECA common line pool is required for the incumbent LEC or any competitive eligible telecommunications carrier serving that incumbent LEC's former customers to receive payment of support comparable to LTS in a given service area.[197] As we stated in the *Order*, we ultimately intend to determine universal service support for all carriers using a forward-looking economic cost model because such a model will require carriers to operate efficiently and will facilitate the move to competition in all telecommunications markets.[198] We decided, however, that we would "retain many features of the current support mechanisms" in order to provide rural LECs, generally the recipients of LTS, sufficient time to adjust to any changes in universal service support, particularly a move to a forward-looking economic cost model for determining universal service support.[199] Although we made some adjustments to the calculation and distribution scheme of LTS in the *Order*, we specifically continued this support mechanism,

[194] AT&T opposition at 11.

[195] AT&T opposition at 11 n.12.

[196] USTA reply at 7.

[197] We note that new local exchange carriers, such as those serving formerly unserved areas, may become members of NECA by petitioning the Commission. *See, e.g.,* Guam Telephone Authority Petition for Declaratory Ruling to Participate in the National Exchange Carrier Association, CCB/CPD File No. 96-29, *Order*, DA 97-1007 (Comm. Carr. Bur. rel. May 12, 1997) (granting Guam Telephone Authority's request to become a member of NECA).

[198] *Order*, 12 FCC Rcd at 8934-35.

[199] *Order*, 12 FCC Rcd at 8938-39.

finding that such payments would serve the public interest "by reducing the amount of loop cost that high cost LECs must recover from IXCs through CCL charges and thereby facilitating interexchange service in high cost areas consistent with the express goals of section 254."[200] Thus, we wish to maintain the current support structure, as modified, for recipients of LTS until we are able to devise a forward-looking economic cost model to determine universal service support appropriate for such carriers. We find that broadening the scope of the LTS mechanism at this time beyond the boundaries established in the *Order* would hinder the achievement of our goal to move toward competition in all telecommunications markets.

75. In addition, we note that a number of companies that have chosen to leave the NECA common line pool in the past generally have done so because their costs have decreased such that they can charge a lower CCL interstate access rate than the NECA CCL rate and recover their costs without LTS support.[201] Thus, it is not clear how providing those carriers with modified LTS would further the goal of universal service. Although we recognize that other considerations may influence a carrier's decision to exit the pool, we can only presume that any carrier that has left did so after balancing all factors and determining that it could forego the receipt of LTS. Accordingly, we decline to reinstate LTS to such carriers and we deny ALLTEL's petition to the extent that it asks that rural incumbent LECs that have left the NECA pool be eligible to receive LTS under the new LTS program.[202]

76. Moreover, as to the requests of current LTS recipients that they be allowed to continue to receive LTS upon exiting the NECA pool, we reiterate that we wish to maintain the current LTS program as modified until we move to the use of a forward-looking economic cost model for determining universal service support for such carriers. Further, providing such support to carriers that leave the NECA pool could undermine the pool's usefulness in permitting participants to share the risk of substantial cost increases related to the CCL charge by pooling their costs and, thereby, charging an averaged CCL rate close to that charged by other carriers. This operation of the pool, like LTS payments, serves section 254's goal of facilitating interexchange service in high cost areas. Accordingly, we decline to permit a carrier leaving the pool to continue to receive LTS in the future.

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[200] *Order*, 12 FCC Rcd at 9165.

[201] Once incumbent LECs withdraw from the pool, they may not choose to participate in the pool at a later date. *Part 67 Reconsideration Order*, 3 FCC Rcd 4543 at 4557, n.17 (1988).

[202] We note that under the existing LTS program, our rules require incumbent LECs that withdraw from the pool to contribute to the support of the remaining pool members. *See Order*, 12 FCC Rcd at 8893 n.534. As determined in the *Order*, such non-pooling incumbent LECs will no longer be required to pay into the pool after January 1, 1998. *Order*, 12 FCC Rcd at 9169. Therefore, although incumbent LECs that do not participate in the pool will not be eligible to *receive* LTS under the new support system, they will benefit from a significant reduction in the support they will be required to pay.

77. We reject GVNW's argument that, in order to preserve competitive neutrality, an incumbent LEC exiting the pool must continue to receive LTS. Rather, we agree with AT&T and USTA that competitive neutrality can be achieved by withdrawing LTS from any competitive eligible telecommunications carrier receiving support in the exiting incumbent LEC's service area. Pursuant to section 54.307 of the Commission's rules, a competitive eligible telecommunications carrier is eligible to receive universal service support to the extent that it captures an incumbent LEC's subscriber lines or serves new subscribers in the incumbent LEC's service area.[203] Having determined that an incumbent LEC exiting the NECA common line pool will lose LTS, we also determine that a competitive eligible telecommunications carrier that receives LTS for serving subscribers in an incumbent LEC's service area similarly will lose LTS when the incumbent LEC exits the NECA common line pool.

78. GVNW also requests that, if the Commission determines that a non-pooling rural incumbent LEC is not eligible to receive LTS, such carrier should be permitted to receive universal service support using forward-looking economic cost.[204] In the *Order*, the Commission determined that rural carriers will begin receiving universal service support based on forward-looking economic cost principles when we have found, based on a fully developed record, that a forward-looking economic cost mechanism for rural carriers will produce results that are sufficient and predictable.[205] Because rural carriers generally serve fewer subscribers than large incumbent LECs, serve more sparsely populated areas, and generally do not benefit as much from economies of scale and scope, the Commission determined that rural carriers will receive support based on embedded cost for at least three years and gradually shift to a forward-looking economic cost mechanism.[206] Moreover, because the cost models in the record of this proceeding produced a higher margin of error for rural carriers, the Commission concluded that rural carriers should not begin their transition to the use of a forward-looking economic cost

[203] 47 C.F.R. § 54.307(a). In the *Order*, the Commission concluded that, starting January 1, 1998, universal service support for high cost, rural and insular areas would be portable such that a competitive eligible telecommunications carrier that wins a customer from an incumbent LEC will receive the same level of universal service support for that customer as the incumbent LEC would have been eligible to receive for serving that customer. *Order*, 12 FCC Rcd at 8932-34, 8944-46. The Commission reasoned that providing support directly to a competitive carrier would foster opportunities for competition in rural and non-rural areas. *Id.* at 8932-33. 8944. In the event that competitive eligible telecommunications carriers capture a substantial number of customers in any support area, the Commission may re-evaluate its decision to permit such carriers that are not members of the common line pool to receive LTS.

[204] *See* GVNW petition at 16.

[205] *Order*, 12 FCC Rcd at 8917.

[206] *Order*, 12 FCC Rcd at 8936.

mechanism when the non-rural incumbent LECs transition to their new mechanism in 1999.[207] Because we have not yet developed a forward-looking economic cost mechanism that accurately predicts forward-looking economic costs for rural carriers, we cannot ensure that rural carriers would receive appropriate levels of support if we allowed them to receive support calculated using the forward-looking economic cost mechanism for non-rural carriers. Accordingly, we deny petitioners' request to permit rural carriers to receive universal service support, beginning January 1, 1999, based on the forward-looking economic cost mechanism that we adopt for non-rural carriers.

D. Support for Competitive Eligible Telecommunications Carriers

1. Background

79. In the *Order*, the Commission concluded that, starting January 1, 1998, universal service support for high cost, rural, and insular areas would be portable such that a competitive eligible telecommunications carrier that wins a customer from an incumbent LEC will receive the same level of universal service support for that customer as the incumbent LEC would have been eligible to receive for serving that customer.[208] The Commission reasoned that paying the per-line support directly to the competitive eligible telecommunications carrier for the lines it captures or for new customer lines that it serves would foster opportunities for competition in rural and non-rural study areas.[209] Section 54.307 of the Commission's rules specifies the method for calculating DEM weighting assistance, LTS, and high cost loop support for an incumbent LEC as well as for a competitive eligible telecommunications carrier that captures lines from the incumbent LEC or serves new subscriber lines within the incumbent LEC's service

[207] *Order*, 12 FCC Rcd at 8943. To ensure that the concerns of rural carriers will be thoroughly addressed, in the *Order* the Commission encouraged the Joint Board to establish a task force to study the development and impact of a support mechanism incorporating forward-looking economic cost principles for rural carriers. *Order*, 12 FCC Rcd at 8917. The creation of the Rural Task Force was announced on September 17, 1997. *See* Federal-State Joint Board on Universal Service Announces the Creation of a Rural Task Force, Solicits Nominations for Membership on Rural Task Force, CC Docket 96-45, *Public Notice*, FCC 97J-1 (rel. Sept. 17, 1997) (*Rural Task Force Public Notice*). In the *Order*, the Commission determined that we would commence a proceeding by October 1998 to establish a system of universal service support for rural carriers based on forward-looking economic cost, at which time we expect to have received the Joint Board's report evaluating the recommendations of the Rural Task Force. *See Order*, 12 FCC Rcd at 8917; *Rural Task Force Public Notice* at 2.

[208] *Order*, 12 FCC Rcd at 8932-34, 8944-46. We note that, to receive universal service support formerly received by an incumbent LEC, a competitive carrier must be designated, by a state commission, as an eligible telecommunications carrier pursuant to section 214(e). 47 U.S.C. § 214(e). Before designating an additional eligible telecommunications carrier in a service area served by a rural carrier, however, a state commission must "find that the designation is in the public interest." 47 U.S.C. § 214(e)(2).

[209] *Order*, 12 FCC Rcd at 8932-33, 8944.

area.[210] Section 54.307(a)(3) provides that a competitive eligible telecommunications carrier that provides the services supported by the new universal service support system through the use of switching functionalities or loops that are purchased as unbundled network elements will receive support based on the lesser of the unbundled network element price or the incumbent LEC's per-line support.[211]

2. Pleadings

80. Air Touch requests clarification regarding the portability of support under the modified high cost loop fund and modified DEM weighting assistance program. Airtouch asserts that neither section 36.601, which sets forth the method for calculating high cost loop support, nor section 54.301, which sets forth the method for calculating DEM weighting assistance, provides that a competitive eligible telecommunications carrier that serves a customer in an incumbent LEC's service area will receive high cost loop support or local switching support for serving that customer. By contrast, AirTouch notes that section 54.303, which sets forth the method for calculating LTS, explicitly states that a competitive eligible telecommunications carrier will receive LTS.[212]

3. Discussion

81. We clarify the Commission's finding that, beginning January 1, 1998, high cost loop support, DEM weighting assistance, and LTS will be portable to any competitive local exchange carrier that has been designated as an eligible telecommunications carrier. Section 54.307(a)(1) of our rules, which encompasses all three types of support currently received by incumbent LECs, provides that "[a] competitive eligible telecommunications carrier shall receive support for each line it serves based on the support the incumbent LEC receives for each line."[213] Section 54.307(a)(2) sets forth the method for calculating per-line support that will be paid to a competitive eligible telecommunications carrier for each line that it serves in an incumbent LEC's service area. Section 54.307(a)(3) provides the method for calculating the level of support that a competitive eligible telecommunications carrier that uses switching functionalities or loops that are purchased as unbundled network elements will receive.[214] AirTouch correctly notes that

[210] 47 C.F.R. § 54.307.

[211] 47 C.F.R. § 54.307(a)(3).

[212] Air Touch petition at 9 (citing 47 C.F.R. § 54.303).

[213] 47 C.F.R. § 54.307(a)(1).

[214] 47 C.F.R. § 54.307(a)(3).

section 54.303, which establishes the method for calculating LTS, explicitly states that a competitive eligible telecommunications carrier will receive LTS.[215] In order to eliminate the apparent ambiguity in our rules governing portability, we amend the first sentence of section 54.303 to eliminate any reference in that section to competitive carriers' eligibility to receive LTS. We adopt this amendment based on our conclusion that section 54.307, which sets forth the method for calculating the amount of high cost loop support, DEM weighting assistance, and LTS that a competitive carrier may receive, specifies the support that competitive eligible telecommunications carriers are entitled to receive and, therefore, the reference to competitive carriers in section 54.303 is not needed.

E. Impact on Incumbent LEC of Losing Access Lines to Competitive Eligible Telecommunications Carriers

1. Background

82. In the *Order*, the Commission concluded that a competitive eligible telecommunications carrier "shall receive universal service support to the extent that it captures subscribers' lines formerly served by an incumbent LEC receiving support or new customer lines in that incumbent LEC's study area" and that the incumbent LEC "will continue to receive support for the customer lines it continues to serve."[216] Section 54.307 of the Commission's rules provides that the level of per-line support paid to a competitive eligible telecommunications carrier will be calculated by dividing the amount of the incumbent LEC's universal service support by the total number of lines the incumbent LEC serves in the study area.[217]

2. Pleadings

83. GCI seeks clarification that an incumbent LEC that loses customers to a competitive eligible telecommunications carrier will lose the support that the incumbent LEC formerly received for serving that customer.[218] GCI contends that section 54.307(a)(2)'s directive that the incumbent LEC's per-line support be based on the incumbent LEC's most recent annual loop count, without providing for a corresponding reduction in the amount of support received by the incumbent LEC if it loses a customer due to competition, gives the incumbent LEC a competitive advantage over the incumbent LEC's competitors.[219] No party commented on GCI's

[215] 47 C.F.R. § 54.303.

[216] *Order*, 12 FCC Rcd at 8932-33.

[217] 47 C.F.R. § 54.307(a)(2).

[218] GCI petition at 4-5.

petition with respect to this issue.

3. Discussion

84. We clarify here that, if an incumbent LEC loses a customer to a competitive eligible telecommunications carrier, the incumbent LEC will lose some or all of the per-line level of support that is associated with serving that customer.[220] If the competitive eligible telecommunications carrier uses network elements purchased pursuant to section 51.307 to provide the supported services, the reduction in the amount of support received by the incumbent LEC is specified in section 54.307(a)(3) of the Commission's rules. That section provides that "[t]he [incumbent] LEC . . . shall receive the difference between the level of universal service support provided to the competitive eligible telecommunications carrier and the per-customer level of support previously provided to the [incumbent] LEC."[221] Section 54.307(a)(4) of our rules provides that a competitive eligible telecommunications carrier that provides the supported services using *neither* unbundled network elements nor wholesale service purchased pursuant to section 251(c)(4) will receive the full amount of universal service support previously provided to the incumbent LEC for that customer.[222] That section, however, does not provide a corresponding reduction in the amount of support received by the incumbent LEC. Accordingly, we amend section 54.307(a)(4) to clarify that, when a competitive eligible telecommunications carrier receives support for a customer pursuant to section 54.307(a)(4), the incumbent LEC will lose the support it previously received that was attributable to that customer.

F. Corporate Operations Expenses

1. Background

85. In the *Order*, the Commission adopted a formula to limit the amount of corporate operations expenses that a carrier may recover through the existing high cost loop support mechanisms.[223] This formula was developed to "ensure that carriers use universal service

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[219] GCI petition at 4-5.

[220] We note that to receive per-line support, the competitive eligible telecommunications carrier must provide the supported services using its own facilities, which includes using network elements purchased pursuant to 47 C.F.R. § 51.307. If the competitive eligible telecommunications carrier provides the supported services using wholesale service purchased pursuant to section 251(c)(4) of the Act, the incumbent LEC whose service is being resold would receive the per-line support for customers served by the competitive carrier pursuant to section 251(c)(4).

[221] 47 C.F.R. § 54.307(a)(3).

[222] 47 C.F.R. § 54.307(a)(4).

[223] *Order*, 12 FCC Rcd at 8930-32. Corporate operations expenses include all of the expenses listed in sections

support only to offer better service to their customers through prudent facility investment and maintenance consistent with their obligations under section 254(k)."[224] Based on comments in both the Docket No. 96-45 and the preceding universal service docket, Docket No. 80-286, the Commission decided to "limit universal service support for corporate operations expense to a reasonable per-line amount, recognizing that small study areas, based on the number of lines, may experience greater amounts of corporate operations expense per line than larger study areas."[225] The maximum allowable corporate operations expense formula was based on a staff analysis of data submitted by NECA.[226]

86. In the *July 10 Order*, the Commission made two modifications to this formula.[227] First, the Commission established a floor on the monthly corporate operations expense cap at $9,505, to allow carriers with relatively few working loops to receive sufficient support to recover initial or fixed corporate operations expenses.[228] The second change addressed a feature of the original formula under which the cap on support for corporate operations expense for carriers whose working loops are within a certain range did not increase with the number of working loops. The revision added another component to the model to ensure that the cap on support for corporate operations expenses does not decrease as the number of working loops increases. Based on these changes on the original model, the formula was defined in the following manner:

> for study areas with 6,000 or fewer working loops the amount per working loop shall be [$27.12 - (0.002 x the number of working loops)] x 1.15 or [1.15 x $8,266/the number of working loops], whichever is greater;

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

[224] *See Order*, 12 FCC Rcd at 8930-31.

[225] *See Order*, 12 FCC Rcd at 8930-31.

[226] This formula, allowing corporate operations expense per line to depend upon the number of access lines, was based on a linear spline regression model that forces two line segments with different slopes to intersect. The model had declining costs per line as access lines increase to 10,000 and constant costs per line for companies with more than 10,000 lines.

[227] *July 10 Order*, 12 FCC Rcd at 10102-05.

[228] When the $9,505 monthly figure is converted to an annual figure, the annual minimum corporate expense cap is $114,071.

for study areas with more than 6,000 but fewer than 17,988 working loops, the amount per working loop shall be ($72,024/the number of working loops + 3.12) x 1.15;

for study areas with 17,988 or more working loops, the amount per working loop shall be $7.12 x 1.15.[229]

2. Pleadings

87. Several parties representing the interests of small incumbent LECs submitted petitions requesting that the Commission reconsider its decision to place a limit on the recovery of corporate operations expenses.[230] Additionally, three parties filed petitions for reconsideration after the Commission modified the corporate operations expenses limitation in its *July 10 Order*.[231] Specifically, these parties argue that, contrary to the Commission's finding in the *Order*, corporate operations expenses are part of providing universal service,[232] and are not discretionary.[233] Additionally, the petitioners assert that this policy ignores Congress's intent to

[229] 47 C.F.R. § 36.621.

[230] Alaska Telephone Association petition at 4; Fidelity Telephone Co. petition at 3-4; GVNW petition at 10-12; RTC petition at 19-20; USTA petition at 10; Western Alliance petition at 8-9. At least one petitioner raised issues that were addressed in the Commission's *July 10 Order*. GVNW petition at 9-10 (stating that the absolute amount of corporate operations expenses declines as the company size increases from 6,850 loops to 10,000 loops and that at 12,900 loops the allowance returns to that of a 6,700 loop company). We note that petitions for reconsideration were due on July 17, 1997, and that the Commission's Order on Reconsideration was released to the public on July 10, 1997. Thus, some petitions for reconsideration raised issues that were addressed several days earlier in the *Order on Reconsideration*.

[231] Rural Telephone Coalition petition to July 10 Order; Western Alliance petition to July 10 Order; U S West petition to July 10 Order.

[232] Alaska Telephone Association petition at 4; USTA petition at 10; Western Alliance petition at 8-9 (citing Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, *Recommended Decision and Order*, 5 FCC Rcd 7578, 7579 (1990) and Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, *Report and Order*, 6 FCC Rcd 2936 (1991)); *accord* Virgin Islands Telephone Company reply at 7-8; *see also* RTC petition to July 10 Order at 2-3, 4 (stating that the Commission's reasoning that corporate operations expenses result from managerial priorities is insufficient because this is true of all spending, including purchase of network plant and facilities and stating that nothing in section 254 limits support to physical facilities).

[233] Western Alliance petition to July 10 Order at 6-7 (stating that only accounts 6722(a) and (b) are discretionary); RTC petition to July 10 Order at 3-4 (stating that compliance with cost separation studies, revenue requirement and settlement calculations, special Commission data requests external audits, and service cost filings are not discretionary).

limit burdens on small, rural, and insular carriers and, in fact, disproportionately burdens smaller incumbent LECs;[234] that the decision not to allow a transition period is inconsistent with prior Commission determinations;[235] that reductions in support will lead to increases in price for local service and therefore universal service support is not "sufficient";[236] that, because of increased regulatory activity stemming from the 1996 Act, corporate operations expenses are increasing, not decreasing;[237] that reasonableness of corporate operations expenses cannot be judged by statistical analysis, but must be judged according to each incumbent LEC's "own specific history and environment";[238] that federal regulatory expenses should not be included within the limitation to ensure that small companies will be able to adequately participate in the federal regulatory process;[239] and that the Commission has contradicted its stated intention to provide universal service support to rural LECs based on embedded costs and to defer using proxy models for rural carriers until January 1, 2001.[240] RTC argues that the Commission did not satisfy the requirements of the Regulatory Flexibility Act to consider alternatives to the cap.[241] RTC asserts that the Commission should not assume that up to 35 percent of all recipients are incurring expenses beyond a "range of reasonableness."[242]

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[234] Alaska Telephone Association at 4-5; GVNW petition at 10-11; Western Alliance at 10; Virgin Islands Tel. Co. July 10 reply at 8-9 (citing 47 U.S.C. § 254(b)(3)'s reference to insular areas)

[235] Fidelity petition at 3, 5 (stating that the Commission found that rural LECs require ample time to adjust to any changes in support calculations and favoring a three year transition period).

[236] Fidelity petition at 4; *see also* Virgin Islands Tel. Co. at 9; Virgin Islands July 10 reply at 10 (citing 47 U.S.C. § 254(b)(5)'s directive that support be "specific, predictable, and sufficient").

[237] Fidelity petition at 4; RTC petition at 19; Western Alliance petition at 8-9; *see also* TCA reply at 4-5 (referencing inflation in addition to increases caused by regulatory changes and citing FCC's budget increase of 21 percent to implement the 1996 Act); Virgin Islands July 10 reply at 8.

[238] Western Alliance petition at 10; Western Alliance petition to July 10 Order at 8; RTC petition to July 10 Order at 4, 8-9 (asserting that the Commission should presume all expenses are reasonable and should conduct an investigation to identify individual expenses that it believes to be unreasonable).

[239] ITC petition at 7-9.

[240] TCA reply at 5; *see also* RTC petition to July 10 Order at 6 (arguing that the formula is a proxy model and that this proxy does not meet the criteria the Commission has adopted for the forward-looking cost models for non-rural carriers).

[241] RTC petition to July 10 Order at 8, n.11 *citing* 5 U.S.C. § 603.

[242] RTC petition to July 10 Order at 6 (asserting that approximately 200 companies, or 35 percent of all cost companies, will receive less support under the July 10 formula).

88. In addition to challenging the decision to limit corporate operations expenses, several petitioners criticize specific portions of the method used to calculate the formula. For example, GVNW states that it is not clear whether the corporate operations expenses rule includes amounts from Accounts 6710 and 6720 or whether it includes "that portion assigned to loop cost in NECA's USF Algorithm (AL19)."[243] Western Alliance asserts that the *Order* contained no discussion or reasoned explanation of "(a) how or why the 115 percent ceiling was selected; (b) why a regression analysis using a spline function technique was accurate and appropriate; or (c) how or why the 1995 NECA data was representative."[244] Western Alliance also asserts that the data for LECs with more than 15,000 loops appear to fit the Commission's regression line relatively closely, but the data for LECs with fewer than 15,000 loops, and particularly for those with fewer than 5,000 loops, are widely scattered about the line.[245] Several petitioners suggest the Commission adopt a minimum cap of $300,000 to protect smaller carriers.[246] Some petitioners also favor such a minimum cap that does not vary by line count because they argue that it would more accurately reflect how corporate operations expenses are incurred.[247]

89. TCA and Virgin Islands Tel. Co. generally support the petitions for reconsideration.[248] Virgin Islands Tel. Co. asserts that the Commission's decision to adopt a nationwide cap violates the Act's requirement that the Commission ensure that rates in rural, insular, and high cost areas are comparable to those in urban areas.[249] Virgin Islands Tel. Co. asserts that the limitation on recovery of corporate operations expenses violates the Act's requirement that universal service support be "sufficient."[250] Virgin Islands Tel. Co. also asserts

[243] GVNW petition at 9.

[244] Western Alliance petition at 9.

[245] Western Alliance petition to July 10 Order at 8.

[246] GVNW petition at 9-10 (proposing a minimum allowance of $300,000); USTA petition at 10-11 (advocating a $300,000 minimum and a limit of two standard deviations); *contra* Virgin Islands Tel. Co. reply to July 10 Order at 11 (does not favor $300,000 minimum because it will not provide relief to mid-sized companies such as Virgin Islands Tel. Co.).

[247] RTC Petition of July 10 Order at 6 (stating that management salaries do not vary by size); Western Alliance petition to July 10 Order at 4 (arguing that the minimum monthly allowance of $9,505.90 is insufficient to retain employees such as telephone managers and accountants for rural LECs).

[248] TCA reply at 1-4; Virgin Islands Telephone Corporation reply at 7-12.

[249] Virgin Islands reply at 7, 8-9 *citing* 47 U.S.C. § 254(b)(3).

[250] Virgin Islands Tel. Co. reply at 10.

that the Commission's decision not to grant study area waivers for corporate operations expenses in excess of 115 percent of the national average absent "exceptional circumstances" based on its finding that such expenses are "not necessary for the provision of universal service" has effectively rendered relief through a study area waiver "unobtainable."[251] TCA and RTC argue that the Commission improperly invoked section 254(k) in support of its decision to limit corporate operations expenses.[252] TCA asserts that the Commission incorrectly relied on the comments of interexchange carriers suggesting that no common costs should be assigned to the loop to support the Commission's implied finding that carriers are subsidizing competitive services by recovering an excessive level of corporate operations expenses from high cost loop support mechanisms.[253]

90. Several petitioners challenge the procedural bases of both the *Order* and the *July 10 Order* under which the Commission's decided to limit corporate operations expenses. In particular, Western Alliance alleges that the Joint Board made no recommendation with respect to changing the recovery of corporate operations expenses.[254] Western Alliance also argues that this decision is a "vestige" of Docket No. 80-286, which Congress did not view as an appropriate foundation on which to base the proceedings for implementing the universal service provisions of the 1996 Act.[255] Western Alliance alleges that the Commission has not met the standard imposed by the Court of Appeals for the D.C. Circuit by supplying "reasoned analysis indicating that prior policies and standards are being deliberately changed, not casually ignored."[256] RTC contends that the Commission gave insufficient notice before adopting the limitation on corporate operations expense. Specifically, RTC contends that the Commission should have allowed all interested parties to comment on the formula, underlying data, assumptions, and

[251] Virgin Islands Tel. Co. July 10 reply at 12-13 (asserting that the heavier waiver burden is inconsistent with the 1996 Act); *accord* RTC petition to July 10 Order at 8. *See also Order*, 12 FCC Rcd at 8932.

[252] RTC petition at 20 (asserting that the Commission did not properly consider whether current levels of corporate operations expenditures are inconsistent with section 254(k)); TCA reply at 4 (asserting that section 254(k) has nothing to do with properly allocating part 32 expenses); *accord* RTC July 10 Petition at 4. Section 254(k) states, in part: "A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition."

[253] TCA reply at 4.

[254] Western Alliance petition at 9.

[255] Western Alliance petition to July 10 Order at 5-6.

[256] Western Alliance at 9 *quoting Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 852 (D.C. Cir. 1970); *accord* Virgin Islands Tel. Co. reply at 10-11 (arguing that the Commission provided insufficient reasoning to justify its decision to limit corporate operations expenses and the decision to limit expenses to those within 115 percent of the formula); Virgin Islands Tel. Co. July 10 reply at 12.

outputs, that there was no notice in Docket No. 96-45, and that the notice in Docket No. 80-286 consisted of only four sentences.[257] TCA asserts that, because 1996 expenses have already been incurred, rural LECs have no opportunity to reduce costs to levels that are consistent with the cap adopted by the Commission.[258]

91. AT&T, Comcast/Vanguard, GCI, and MCI oppose the petitioners' requests that the Commission reconsider limiting recovery of corporate operations expenses and urge the Commission to maintain the limitation.[259] AT&T agrees with the Commission that these expenses are not directly related to the provision of subscriber loops.[260] Comcast/Vanguard and GCI question whether rural LECs should receive universal service support -- which they note is funded by, among others, LEC competitors -- for expenses such as lobbying and the costs of moving into a competitive environment.[261] MCI states that none of the petitioners offered any evidence to rebut the Commission's findings that corporate operations expenses are discretionary and not inherent to the provision of universal service.[262]

3. Discussion

a. Imposition of a Limitation

92. In light of these challenges to the Commission's decision to limit recovery of corporate operations expenses, we take this opportunity to explain more fully the bases for this decision.[263] Expenditures for corporate operations in many instances may be discretionary, in contrast, for example, to expenditures to maintain existing plant and equipment.[264] Corporate

[257] RTC petition to July 10 Order at 5, 7.

[258] TCA reply at 5.

[259] AT&T opposition at 13; Comcast/Vanguard opposition at 9; General Communications opposition at 4-5; MCI opposition at 13. GCI also filed an opposition to the petitions to the July 10 Order. *See* GCI July 10 opposition.

[260] AT&T opposition at 13.

[261] Comcast/Vanguard opposition at 8-9; General Communications opposition at 4-5 (describing expenses such as advertising and improving customer service that are included in corporate operations expenses and will be incurred by incumbent LECs in a more competitive environment); *contra* RTC reply at 8-9 (arguing that limiting recovery of corporate operations expenses will hamper ability of small incumbent LECs to perform the planning necessary to facilitate competition).

[262] MCI opposition at 13.

[263] *See, e.g.*, Western Alliance at 9.

[264] NYDPS further comments at 6 n.1; *see also* AT&T further comments at 24, att. A (suggesting that recovery of all

operations expenses include, for example, travel, lodging and other expenses associated with attending industry conventions and corporate meetings. Although participation in such activities may be prudent, the levels of these expenditures are subject to managerial discretion. Carriers currently have little incentive to minimize these expenses because the current mechanism for providing support in high cost areas allows carriers to recover a large percentage of their corporate operations expenses. For companies with fewer than 200,000 lines, for example, the expenses attributed to the high cost expense adjustment are covered in full for companies with costs in excess of 150 percent of the national average.[265] Smaller carriers possess even fewer incentives to minimize corporate operations expenses because the Commission has a limited ability to ensure, through audits, that smaller companies properly assign corporate operations expenses to appropriate accounts and that these expenses do not exceed reasonable levels. The Commission, and frequently state commissions, cannot justify auditing smaller carriers because the Commission's audit staff is small, there are many hundreds of small telephone companies, and the costs of full-scale audits are in many instances likely to exceed any expenses found to be improper. We, therefore, conclude that imposing a cap that is relatively generous to small carriers, but still imposes a limitation, is a reasonable method of encouraging carriers to assign corporate operations expenses to the proper accounts and discouraging carriers from incurring excessive expenditures. Under this approach, we provide carriers with an incentive to control their corporate operations expenses without requiring carriers to incur the costs associated with a full Commission audit. As the Commission stated in its *Order* and as explained further below, carriers that contend that the limitation provides insufficient support may request a waiver from the Commission.[266] Therefore, only carriers whose expenses exceed the cap and who contend that the capped amount is insufficient will be required to provide additional justification for their expenditures. We, therefore, conclude that a cap on federal support for corporate operations expenses is a reasonable method of preventing the recovery of improperly assigned or excessive expenses from federal funds while minimizing the administrative burden on the Commission and on all carriers, including smaller carriers.

93. We disagree with petitioners who assert that, because some corporate operations expenses are not discretionary, we should not impose any limit on the recovery of corporate operations expenses.[267] We recognize that the expenses cited by petitioners and commenters

administrative expenses be excluded), NECA further comments at 19 (stating that, if the Commission is concerned about excessive levels of general and administrative expenses, it may wish to consider using statistical measures, such as the two standard deviation test proposed by NECA in the 80-286 proceeding).

[265] *See* 47 C.F.R. § 36.631(c).

[266] *Order*, 12 FCC Rcd at 8932.

[267] *Accord* Opposition by Comcast/Vanguard at 9; General Communications at 4-5; and MCI at 13; *contra, e.g.,* Rural Telephone Companies Reply at 1-2, 8-9.

may be necessary for the operation of a company, and that such expenditures are in some circumstances required by state or federal law or regulation.[268] Most companies, however, fulfill all such state and federal requirements while incurring corporate operations expenses that are well below the limitation imposed by the Commission.[269] No party has provided detailed data explaining the significant differences in corporate operations expenses for companies of similar sizes.[270] Further, we are not excluding recovery of corporate operations expenses from universal service support, but instead are imposing a reasonable limit. We reject ITC's request to exclude all federal regulatory expenses from the limitation because, although some expenditures may be necessary to participate in the federal regulatory process, we see no reason to permit the unlimited recovery of such expenses.[271] Moreover, individual companies that are required to incur unusually high corporate operations expenses, such as Alaskan or insular telephone companies, have the right to apply for a waiver with the Commission to demonstrate the necessity of these expenses for the provision of the supported services.[272]

b. Adjustments to Limitation Formula

94. In the *July 10 Order*, the Commission specified a minimum allowable corporate operations cost in order to ensure that carriers with small numbers of working loops would receive sufficient support to recover initial or fixed corporate operations expenses.[273] This monthly cost minimum was estimated from a regression of total corporate operations expenses

[268] *See, e.g.,* RTC petition to July 10 Order at 3-4 (stating that compliance with cost separation studies, revenue requirement and settlement calculations, special Commission data requests external audits, and service cost filings are not discretionary).

[269] The methodology used to calculate the cap ensures that more than a majority of carriers subject to this cap incur corporate operations expenses well below the cap, *see infra*, and we are not aware of any carrier that is currently unable to fulfill all of its state and federal requirements within current levels of expenditure.

[270] Although several Alaskan companies did provide more detailed breakdowns of their corporate operations expenses, these companies did not explain with specificity why their expenses differ from the expenses of similarly sized companies. *See* letter from Paula Eller, President, Yukon Telephone Company to William F. Caton, Acting Secretary, FCC (Sept. 17, 1997) (providing additional information for Yukon Telephone Company, Mukluk Telephone Company, Interior Telephone Company, Mantanuska Telephone Association, and Arctic Slope Telephone Association Cooperative).

[271] *See* ITC petition at 7-9.

[272] *See, e.g.,* Alaska Tel. Ass'n petition at 4; TCA petition at 1-5; Virgin Islands Tel. Co. petition at 8; RTC petitions to July 10 Order at 2-4.

[273] *See July 10 Order*, 12 FCC Rcd at 10104.

on the number of working loops.[274] After performing this analysis, the Commission adopted a minimum monthly recovery of $9,505, which results in a minimum recovery of $114,071 per year.[275] USTA and GVNW urge the Commission to increase this minimum recovery from $114,071 per year to $300,000 per year.[276] USTA additionally advocates adopting a limitation equal to the greater of either $300,000 per year or $34.82 per line per month.[277]

95. We reconsider, to a limited extent, the limitation on recovery of corporate operations expenses and adopt a new minimum cap of $300,000 per year as advocated by USTA and GVNW. Although we are fully confident in the formula that calculates the cap, we adopt a minimum cap of $300,000 out of an abundance of caution for the smallest carriers.[278] The increased minimum will reduce the need of the smallest carriers to seek a waiver of the cap. We intend to continue to monitor the effect of this limitation and the $300,000 minimum cap on smaller carriers. We note that, because the Commission has adopted an indexed cap for all high cost support, increases in the amount of support provided to some companies will reduce the amount of support provided to other companies. We find, however, that this change will result in a minimal increase in the total amount of universal service support provided to carriers.[279] We will continue to monitor this issue closely and will take steps to ensure that only necessary and prudent expenditures are supported. We do not adopt USTA's alternative proposal to increase recovery to $34.82 per line per month for all carriers because we believe the minimum cap of $300,000 provides adequate protection for the smallest carriers while imposing the smallest corresponding decrease in high cost loop support for carriers overall.[280]

96. Upon reconsideration, we make an additional change in the limitation formula to address a small discontinuity in the formula that causes the total allowable corporate operations expense to be slightly lower in the range from 17,988 and 17,997 lines than the amount

[274] *July 10 Order*, 12 FCC Rcd at 10102-03.

[275] 47 C.F.R. § 36.621.

[276] GVNW petition at 9-10; USTA petition at 10-11.

[277] USTA indicates that this figure is "two standard deviations from zero." USTA does not provide the calculations which produced this figure. Letter from Porter E. Childers, Executive Director, Legal and Regulatory Affairs, USTA to William F. Caton, Acting Secretary, FCC (Oct. 6, 1997) (*USTA Oct. 6 ex parte*).

[278] *See* 5 U.S.C. §§ 601-612 (Regulatory Flexibility Act).

[279] *See* GVNW petition at 12 (indicating that a $300,000 minimum cap will result in an increase equal to approximately 0.2 percent of all high cost support).

[280] As noted, because of the indexed cap, increases in high cost loop support for some carriers will decrease such support levels for the remaining carriers.

computed at 17,987 lines.[281] To eliminate the anomaly caused by this discontinuity, we alter the second threshold for access lines from 17,988 lines to 18,006 lines. Finally, to make our rules easier to apply, we standardized general mathematical conventions in the formulas.[282]

c. Methodology Used to Calculate the Limitation

97. Western Alliance questions the methodology the Commission used to create the formula for the corporate operations expense limitation. Western Alliance asserts that the *Order* contained no discussion or reasoned explanation of: "(a) why a regression analysis using a spline function technique was accurate and appropriate; (b) how or why the 115 percent ceiling was selected; or (c) how or why the 1995 NECA data were representative."[283] We address these arguments in turn. As detailed further in the *July 10 Order*, the Commission used a linear spline to estimate average corporate operations cost per loop, based on the number of loops served. To produce this formula, we used statistical regression techniques that focused on the relationship between expenses per loop, rather than total expense. We adopted this approach in order to establish a model under which the cap on corporate operations expense per line would decline as the number of loops increases for a range of smaller companies so that economies of scale, pursuant to which expenses per loop decline as carrier size increases, would be taken into account by the formula.[284] Of the models studied, the linear spline was found to have the highest R^2, a measure indicating that this model provides the best fit with the data.[285] The relationship between corporate operations expense and lines served may reasonably be expected to change as carriers' size increases. The linear spline method used allows a different slope to be fitted for smaller carriers than for larger carriers. The Commission adopted the "knot," or the point at which the two line segments of the linear spline model meet, at 10,000 loops because that point

[281] At 17,988 loops, total allowable corporate operations cost drops $79.30 from $147,365 to $147,285.70.

[282] For example, we distributed the 1.15 multiplier throughout the formulas and we no longer round 8.188 to 8.19 in section 36.631(a)(4)(ii)(C).

[283] Western Alliance petition at 9.

[284] *July 10 Order*, 12 FCC Rcd at 10115-18, App. B.

[285] The linear spline model, in this case, is two line segments joined together at a single point or knot. In general, the linear spline model allows the cap on corporate operations expense per line to decline as the number of loops increases for the smaller companies having fewer loops than the knot point. *See July 10 Order*, App. B. Regression analysis is a standard technique that quantifies relationships between input variables. In this case, the input variables are the number of lines a carrier serves and the levels of corporate operations expense per carrier. The R^2, a statistical measure for goodness of fit, for total operating costs using this model is 0.89. This implies that approximately 90% of the variation in total corporate operating costs is explained by the variations in the number of lines served. *See July 10 Order*, 12 FCC Rcd at 10115-18, App. B.

allowed the best-fitting overall spline.[286]

98. Regarding the remaining issues raised by Western Alliance, the 115 percent ceiling that limits recovery of corporate operations expenses is consistent with other Commission rules regarding universal service support under Part 36 of our rules.[287] The Commission has consistently considered carriers whose loop costs exceed the national average loop cost by more than 15 percent worthy of special treatment.[288] In the present context, out of an abundance of caution, we have concluded that companies will be allowed to recover costs up to 15 percent above average costs, rather than limiting recovery of such expenses to average costs.[289] We also find that, before receiving corporate operations expenses in excess of 115 percent of the average, companies should undergo additional scrutiny by submitting a waiver request to the Commission. Finally, the data used in the estimation are the actual corporate operations expenses that companies filed with NECA for the calculation of universal service support. We used the most current NECA data available at the time we performed these calculations.[290]

99. Western Alliance claims that the Commission's corporate operations expense formula affects smaller companies more significantly than larger companies.[291] It states that Figure 1 in the *July 10 Order* demonstrates that the data for LECs with more than 15,000 loops cluster more closely around the Commission's fitted line than the data for those LECs with fewer

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[286] *July 10 Order*, 12 FCC Rcd at 10115-18, App. B.

[287] *See* 47 C.F.R. § 36.631.

[288] Amendment of Part 67 of the Commission's Rules and Establishment of the Joint Board, CC Docket 80-286, *Decision and Order*, 96 FCC 2d 781 at para. 29 (1984) (adopting Joint Board's recommendation and analysis concluding that high cost support should be provided to companies whose costs are in excess of 115 percent of the national average); Amendment of Part 67 of the Commission's Rules and Establishment of the Joint Board, CC Docket 80-286, *Recommended Decision*, 48 Fed. Reg. 46,556, 46,567 (1983) (rejecting levels of both 110 percent and 120 percent, and concluding that the 115 percent level best balances the competing concerns of "insur[ing] universal availability of affordable telephone service and the need to limit the high cost amount to a level which can be recovered through a carrier's carrier access charges without resulting in economic inefficiency or uneconomic bypass.").

[289] When the Commission calculated the formula, it multiplied estimates of average costs by 1.15 to calculate the actual level of the cap. *July 10 Order*, 12 FCC Rcd at 10115-18, App. B. We note that this recovery is more generous than the Commission's initial proposal to eliminate recovery of all corporate operations expenses. *See infra* section IV.F.3.d.

[290] NECA files data each year on October 1. *See* NECA Universal Service Fund 1997 Submission of 1996 Study Results; 47 C.F.R. § 36.613.

[291] Western Alliance petition to July 10 Order at 8.

than 15,000 lines.[292] This observation, however, does not undermine the Commission's conclusion. Because corporate operations expense per line varies more for smaller companies than larger ones, any line that we might adopt would fit the data for larger companies more closely than it would fit the data for smaller ones. Moreover, as explained above, we have raised the minimum cap out of an abundance of caution to address concerns that, without modification, our formula may not afford sufficient recovery of corporate operations expenses for the smallest companies.

100. We reject GVNW's argument that it is not clear whether the corporate operations expense rule addresses amounts from Accounts 6710 and 6720 or whether it addresses "that portion assigned to loop cost in NECA's USF Algorithm (AL19)."[293] According to the *Order*, however, "[c]orporate operations expense are recorded in Account 6710 (Executive and planning) and Account 6720 (General and administrative)."[294] Hence, the limitation applies to accounts 6710 and 6720 and does not apply to NECA's USF algorithm.[295]

101. RTC asserts that the Commission's formula is a proxy model and therefore should be subject to the criteria the Commission adopted for forward-looking cost proxy models in the *Order*.[296] Although the formula we adopted to limit recovery of corporate operations expenses is a model, it is not a model intended to estimate forward-looking economic costs. Therefore, most of the criteria adopted by the Commission concerning forward-looking cost proxy models are inapplicable to the corporate operations expense formula.[297] Further, RTC is incorrect to the extent that it is arguing that the underlying data and assumptions for the formula are unavailable

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[292] *Id.*

[293] GVNW petition at 9.

[294] *See Order*, 12 FCC Rcd at 8930, n.735.

[295] "AL19" refers to line 19 of NECA's cost company loop cost algorithm. The portion of accounts 6710 and 6720 that are assigned to C&WF Category 1 and COE Category 4.13 are used as input values to line 19 of the algorithm. *See* NECA Universal Service Fund 1997 Submission of 1996 Study Results, section 3 at 3.

[296] *See* RTC Petition to July 10 Order at 5; *Order*, 12 FCC Rcd at 8912-16. These criteria, recommended by the Joint Board and adopted by the Commission, have been established to provide a guide in development and selection of proxy models, which are used to explain the behavior of forward-looking economic costs in capital investment. *Recommended Decision*, 12 FCC Rcd at 230-32; *Order*, 12 FCC Rcd at 8899 n. 573. "Forward-looking economic cost" is defined as the cost of producing services using the least cost, most efficient, and reasonable technology currently available for purchase with all inputs valued at current prices. *Id.*

[297] For example, criteria one requires the forward-looking economic cost models to assume the "least-cost, most-efficient, and reasonable technology for providing the supported services." *Order*, 12 FCC Rcd at 8913.

to the public.[298] The data used to create the line were filed publicly with the Commission by NECA for calendar year 1995. The assumptions and method we used to compute the formula can be found in greatest detail in the *July 10 Order*.[299] The Commission has not, as TCA alleges, contradicted its decision to base universal service support for rural telephone companies on embedded costs until January 1, 2001.[300] The formula we have adopted imposes a limit on the recovery of embedded costs and is not a proxy model designed to calculate forward-looking economic costs.

102. We find that our limitation on recovery of corporate operations expenses will not jeopardize the affordability of local services.[301] Because, as discussed above, such expenditures and the level of such expenditures are in many cases discretionary, we believe that imposing some limits on corporate operations expenses serves the public interest. Moreover, if carriers have prudent corporate operations expenses that exceed the cap, they may seek a waiver of that cap.[302]

103. Based on the changes described above, we modify the formula to limit the amount of corporation operations expenses per working loop that a carrier may recover as follows:

> for study areas with 6,000 or fewer working loops the amount per working loop shall be $31.188 - (.0023 x the number of working loops), or, ($25,000 ÷ the number of working loops), whichever is greater;
>
> for study areas with more than 6,000 but fewer than 18,006 working loops, the amount per working loop shall be $3.588 + (82,827.60 ÷ the number of working loops); and
>
> for study areas with 18,006 or more working loops, the amount per working loop shall be $8.188.

We conclude that this modified formula will better serve our goal of ensuring that carriers use universal service support only to offer the supported services to their customers through prudent

[298] *See* criteria 8 (requiring, *inter alia*, all underlying data, formulae, and computations to be available to interested parties). *Order*, 12 FCC Rcd at 8915.

[299] *July 10 Order*, 12 FCC Rcd at 10102-05; 10115-18, App. B.

[300] *See* TCA reply at 5.

[301] Fidelity petition at 4 (asserting that the limitation will cause increases in local rates).

[302] *See infra* section IV.F.3.d.

facility investment and maintenance consistent with their obligations under section 254(k).

d. Procedural Matters

104. We conclude that the limitation on corporate operations expenses was adopted in compliance with the Administrative Procedure Act (APA). The Commission gave the public ample notice regarding the possibility of limiting or excluding recovery of corporate operations expenses. In a Notice of Inquiry released in 1994, the Commission sought comment on whether we should exclude all recovery of corporate operations expenses. In a Notice of Proposed Rulemaking released in 1995, as the petitioners acknowledge, the Commission tentatively concluded that it should exclude recovery of all such expenses.[303] In the *Universal Service Notice*, the Commission specifically sought comment on whether any proposals in Docket No. 80-286 were worthy of consideration in Docket No. 96-45 and specifically incorporated the record of that proceeding into the 96-45 docket.[304] Moreover, in its Public Notice seeking further comment, the Common Carrier Bureau asked what modifications should be made to the high cost support mechanism if it were retained with respect to rural areas.[305] In response to this Public Notice, several parties recommended that the Commission limit or exclude recovery of corporate operations expenses as it had previously proposed.[306]

105. Not only did the Commission provide notice of a potential limit on or exclusion of the recovery of corporate operations expenses, the approach adopted by the Commission takes into consideration the comments filed in response to these notices.[307] The Commission initially

[303] *See* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, *Notice of Inquiry*, 9 FCC Rcd 7404 at 7416-17 (1994) (*1994 NOI*); Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket 80-286, *Notice of Proposed Rulemaking and Notice of Inquiry*, 10 FCC Rcd 12,309, 12,324 (*1995 Notice*).

[304] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Notice of Proposed Rulemaking and Order Establishing Joint Board*, 11 FCC Rcd 18092, 18112 (1996) (*Universal Service Notice*).

[305] Common Carrier Bureau Seeks Further Comment on Specific Questions in Universal Service Notice of Proposed Rulemaking, CC Docket 96-45, *Public Notice*, 11 FCC Rcd 7750, 7754 (Comm. Carr. Bur. 1996) (*Further Comment Public Notice*).

[306] *See, e.g.,* AT&T further comments at 24, att. A (suggesting that recovery of all administrative expenses be excluded), NECA further comments at 19 (stating that, if the Commission is concerned about excessive levels of general and administrative expenses, it may wish to consider using statistical measures, such as the two standard deviation test proposed by NECA in its comments to the *1995 Notice*, to limit the amount of expenses allocated to the USF); NYDPS further comments at 6, n.1.

[307] *Cf.* TCA reply at 4 (asserting that the Commission's decision was based on an insufficient record).

proposed disallowing all recovery for corporate operations expenses.[308] After considering the comments, however, the Commission concluded in the *Order* that it should limit such expenses to a reasonable level rather than excluding them altogether.[309] The approach taken is conceptually similar to the one NECA proposed in response to the *1995 Notice* and again in response to the Public Notice.[310] NECA proposed that high cost support recipients should recover only expenses that fall below a line that is two standard deviations above a regression line.[311] Our limitation is based on a regression line that takes into account the size of the company when calculating an acceptable range of recoverable corporate operations expenses and, rather than allowing all expenses within two standard deviations of the line as proposed by NECA,[312] allows recovery of expenses that are up to 115 percent of the typical costs of companies of similar size. Thus, because the corporate operations expense cap was within the scope of the proposal to eliminate recovery of all corporate operations expenses and was supported by record evidence, the requirements of the APA were met.[313]

106. We conclude that we are not barred from adopting this limitation because, although the Joint Board did not make a recommendation about limiting the recovery of corporate operations expenses,[314] the Commission properly referred to the CC Docket No. 96-45 Joint Board the question of whether proposals originating with the CC Docket No. 80-286 Joint Board should be adopted.[315] We also conclude that Western Alliance incorrectly implies that the legislative history to the 1996 Act prohibits the Commission from adopting any proposal that was

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[308] *1995 Notice*, 10 FCC Rcd at 12,324.

[309] *Order*, 12 FCC Rcd at 8931-32.

[310] *See* NECA further comments at 19 (stating that, if the Commission is concerned about excessive levels of general and administrative expenses, it may wish to consider using statistical measures, such as the two standard deviation test proposed by NECA in the 80-286 proceeding).

[311] NECA 1995 Notice comments, App. G1. NECA created three regression lines that regressed, respectively, administrative expenses per USF loop in accounts 6120, 6710, and 6720 against the natural logarithm of number of USF loops. *Id.* at 3.

[312] By adopting a two standard deviation approach, NECA's proposal reduced recovery of corporate operations expenses of approximately 5 percent of companies. NECA 1995 Notice comments, App. G1 at 4.

[313] *See Omnipoint Corp. v. FCC*, 78 F.2d 620, 632 (D.C. Cir. 1996) (citing *United Steelworkers of America, AFL-CIO-CIC v. Marshall*, 647 F.2d 1189 (D.C. Cir. 1981)); *see also, Small Refiner Lead Phase-Down Task Force v. EPA*, 705 F.2d 506, 547 (D.C. Cir. 1983).

[314] Western Alliance petition at 9.

[315] *Universal Service Notice*, 11 FCC Rcd at 18,112.

submitted in the record of the CC Docket No. 80-286 proceeding.[316] Although the Joint Explanatory Statement explained that Congress did not view the CC Docket No. 80-286 proceeding as an appropriate basis for implementing section 254(a),[317] nothing in the legislative history suggests that Congress, in enacting section 254, intended to preclude us from considering specific proposals from that docket in the separate proceeding undertaken to implement section 254. Indeed, the Commission, in the *Universal Service Notice*, sought comment on whether any proposals from the 80-286 docket were consistent with the 1996 Act so as to avoid duplication of previous Commission efforts.[318] As described above, several commenters proposed elimination or limitation of the recovery of corporate operations expenses in the 96-45 docket, and the Commission adopted this limitation as part of the 96-45 docket.

107. We also conclude that our adoption of a high standard for granting a waiver for corporate operations expense recovery is fully justified.[319] Because corporate operations expenses are in many cases completely within a company's discretion, they are more likely to be susceptible to abuse than other types of expenditures such as plant maintenance expenditures.[320] Accordingly, parties contending that they should recover unusually high amounts of such expenses should be required to meet a substantial burden. Additionally, because the limitation includes a buffer zone to accommodate companies that may have corporate operations expenses that are higher than average, but not extreme, we affirm our conclusion that the need for waivers should be limited to exceptional circumstances.

108. We also reject petitioners' suggestions that the limitation on recovery of corporate operations expenses should be phased in over a lengthy transition period.[321] Unlike other situations cited by the commenters, a transition period is not warranted in this instance. We conclude that we should not phase in a measure designed to prevent misallocation, manipulation, and abuse. Companies believing that they have reasonably incurred expenses in excess of the limitation may petition for a waiver from the Commission. We find that the availability of a waiver will sufficiently protect any company that legitimately incurred expenses in excess of the

[316] *See* Western Alliance petition to July 10 Order at 5-6.

[317] Joint Explanatory Statement at 131.

[318] *Universal Service Notice*, 11 FCC Rcd at 18112.

[319] *Order*, 12 FCC Rcd at 8932 (stating that the Commission will grant study area waivers only under "exceptional circumstances").

[320] *See supra* section IV.F.3.a and comments cited therein.

[321] *See, e.g.*, Fidelity petition at 3, 5.

limitation, whether caused by activity mandated by the 1996 Act or for any other reason.[322]

109. Contrary to the position of some commenters, the Commission is fully authorized to adopt rules to implement section 254(k) in addition to codifying the statutory provision as it has already done.[323] In fact, in the *Section 254(k) Order*, we concluded that we would "from time to time, re-evaluate our rules to determine whether additional rule changes are necessary to meet the requirements of section 254(k)."[324] The Commission concluded in the *Order* and the *July 10 Order* that some recipients of federal universal service support may be receiving funds beyond those necessary to provide the supported services.[325] Recovery of such expenditures may allow carriers to use these expenditures to subsidize competitive services in violation of section 254(k).[326] In addition to limiting support for corporate operations expense in order to control spending that may be in excess of that allowed by the Act,[327] the Commission correctly found that limiting corporate operations expenses would reduce the ability of incumbent LECs to subsidize competitive services with noncompetitive services by reducing the incumbent LECs' receipt of funds beyond those that may be necessary to provide the supported services. We therefore conclude that limiting recovery of corporate operations expenses is within the ambit of section 254(k).

V. SUPPORT FOR LOW-INCOME CONSUMERS

A. Obligation to Provide Toll-Limitation Services

[322] *See, e.g.*, Virgin Islands Tel. Co. July 10 reply at 8-9 (stating that corporate operations expenses in the Virgin Islands are higher than in other parts of the United States). We note, however, that staff analysis comparing 1995 data with 1996 data shows that corporate operations expenses for companies with more than 10,000 lines went down in 1996 and that such expenses increased by only 6 percent for companies with fewer than 10,000 lines. *Compare* NECA Universal Service Fund 1997 Submission of 1996 Study Results *with* NECA Universal Service Fund 1996 Submission of 1995 Study Results. *See also* NECA Universal Service Fund 1997 Submission of 1996 Study Results, section 10, nationwide totals (showing percent changes between 1995 and 1996).

[323] 47 U.S.C. § 254(k); Implementation of Section 254(k) of the Communications Act of 1934, as amended, *Order*, 12 FCC Rcd 6415 (May 8, 1997) (*Section 254(k) Order*).

[324] *Section 254(k) Order*, 12 FCC Rcd at 6415.

[325] *Order*, 12 FCC Rcd at 8930-32; *July 10 Order*, 12 FCC Rcd at 10102-05.

[326] Section 254(k) states, in part: "A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition." 47 U.S.C. § 254(k).

[327] *See* 47 U.S.C. § 254(e) (requiring carriers that receive universal service support to "use that support only for the provision, maintenance, and upgrading of facilities and services for which the support is intended").

1. Background

110. The Commission has defined toll-limitation services as toll blocking, which allows customers to block outgoing toll calls, and toll control, which allows customers to limit in advance their toll usage per month or billing cycle.[328] Toll-limitation services for qualifying low-income consumers are among the "core" or "designated" services that carriers must provide in order to be deemed "eligible telecommunications carriers."[329] In addition, once they are designated as eligible, all eligible telecommunications carriers must offer Lifeline and LinkUp services.[330] In the *Order*, the Commission agreed with the Joint Board's recommendation[331] that Lifeline customers should receive toll-limitation services at no charge, in addition to the other services that will be supported by federal universal service support mechanisms for rural, insular, and high cost areas.[332] In reaching this conclusion, the Commission found that, by limiting in advance customers' toll usage per month or billing cycle, toll-limitation services assist customers in avoiding involuntary termination of local telecommunications services for non-payment of long-distance charges.[333] The Commission authorized state commissions to grant carriers that are technically incapable of providing toll-limitation services a transitional period during which they may receive universal service support for serving Lifeline consumers while upgrading their switches to provide these services.[334]

2. Pleadings

111. Several petitioners seek clarification of certain Commission rules requiring carriers to offer toll-limitation services to all qualifying low-income consumers. Our rules define toll limitation as "toll blocking and toll control."[335] These parties object to having to offer both toll blocking and toll control, and argue that offering either one of these services should be

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[328] *Order*, 12 FCC Rcd at 8978-8979. *See also* 47 C.F.R. § 54.400(2).

[329] *Order*, 12 FCC Rcd at 8809.

[330] *See* 47 C.F.R. § 54.405.

[331] Federal-State Joint Board on Universal Service, CC Docket No. 96-45, *Recommended Decision*, 12 FCC Rcd 87, 285 (1996).

[332] *Order*, 12 FCC Rcd at 8980.

[333] *Order*, 12 FCC Rcd at 8980.

[334] *Order*, 12 FCC Rcd at 8982.

[335] USTA petition and Ameritech opposition *citing* 47 C.F.R. §§ 54.400(4) and 54.401(a)(3).

sufficient to qualify for universal service support.[336] RTC asserts that LECs generally do not have the "capability to determine, in real time, the accumulated toll billings of any subscriber" because, unlike IXCs, LECs cannot monitor toll usage as customers place toll calls.[337] Others parties contend that providing toll control, even if technically possible, would be difficult and expensive, and would not yield measurable benefits because parties could circumvent toll control protections simply by dialing around or using pre-paid calling cards.[338] Catholic Conference, in its opposition to USTA's and RTC's petitions, asserts that Lifeline consumers should have the choice of either toll blocking or toll control.[339]

112. The Florida Commission asks the Commission to clarify whether carriers offering Lifeline must offer Lifeline consumers toll-control services other than those identified in the *Order*.[340] The Florida Commission asks whether international toll-call-blocking and toll blocking that allows callers with a Personal Identification Number (PIN) to make toll calls, for example, must be provided free of charge to Lifeline consumers.[341] The Florida Commission points out that such toll-control services are not characterized by a pre-set spending limit, unlike the toll-blocking and toll-limitation services defined in the *Order*.[342] The Florida Commission seeks further clarification regarding whether toll control must limit incoming collect calls, noting that the Commission's rules require that toll blocking only block outgoing calls.[343] Finally, the Texas Commission requests clarification as to whether a carrier must provide Lifeline services in

[336] *See* USTA petition at 4-6; Ameritech opposition at 4-6; AT&T opposition at 24; Bell Atlantic opposition at 11-12; BellSouth opposition at 10; and GTE opposition at 15.

[337] RTC petition at 24. *See also* AT&T opposition at 24-25.

[338] *See* USTA petition at 5-6; Ameritech opposition at 5-6; AT&T opposition at 24-25; GTE opposition at 16.

[339] Catholic Conference opposition at 4-5.

[340] Florida Commission Oct. 9 petition at 5-6. On Oct. 9, 1997, Florida Commission filed a Petition for Declaratory Statement, Waiver, and Clarification and Request for Expedited Ruling. That portion of Florida Commission's petition that is styled as a petition for clarification was not timely filed within the period for filing petitions for reconsideration or clarification of the *Order*. *See* 47 U.S.C. § 405(a). *See also Virgin Islands Telephone Corp. v. FCC*, 989 F.2d 1231, 1237 (D.C. Cir. 1993); *Reuters Ltd. v. FCC*, 781 F.2d 946, 951-52 (D.C. Cir. 1986). Therefore, we consider that portion of its petition as informal comments.

[341] Florida Commission Oct. 9 petition at 5-6.

[342] The Commission defined "toll blocking" as a service that allows customers to block toll calls and "toll control" as a service that allows customers to limit in advance their toll usage per month or billing cycle. *Order*, 12 FCC Rcd at 8978-8979.

[343] Florida Commission Oct. 9 petition at 6.

order to be designated an eligible telecommunications carrier.[344]

113. In response to the Florida Commission's petition, USTA asks the Commission to reject any suggestion that international toll-call-blocking and toll blocking that allows callers with a Personal Identification Number (PIN) to make toll calls must be provided free-of-charge to Lifeline consumers.[345] According to USTA, most LECs offer only toll blocking services that block calls beginning with 1+, 0+, 0, and 10XXX. Thus, USTA does not support any requirement to provide toll-limitation services other than those that block calls beginning with these numerical codes. USTA further rejects the suggestion that international toll-call-blocking should be provided free-of-charge on grounds that most LECs, in providing toll-blocking service, are not able to differentiate between interstate, intrastate, or international calls.

3. Discussion

114. We believe that low-income consumers eventually should have the choice of selecting either toll blocking or toll control to restrict their toll usage. We conclude, however, that giving consumers such an option is not viable at this time. Based on the record before us, we find that an overwhelming number of carriers are technically incapable of providing both toll-limitation services, particularly toll-control services, at this time.[346] Under our current rules, carriers technically incapable of providing both types of toll-limitation services must seek from their state commissions a time-limited waiver of their obligation to provide both toll blocking and toll control.[347] Given that a large number of carriers are technically incapable of providing both toll blocking and toll control at this time, we believe that requiring carriers to provide both would result in an unnecessarily burdensome process for state commissions required to act on a large number of waiver proceedings.[348]

115. In light of these concerns, we believe that requiring carriers to provide at least one type of toll-limitation service is sufficient to provide low-income consumers a means by which to control their toll usage and thereby maintain their ability to stay connected to the public switched telephone network. Weighing the burdens on the states and the need to have carriers designated

[344] Texas Commission petition at 9-10.

[345] Letter from USTA to William F. Caton, FCC, dated November 5, 1997 (USTA November 5 ex parte) at 2.

[346] *See* RTC petition at 24; USTA petition at 5-6; Ameritech opposition at 5-6; AT&T opposition at 24-25; GTE opposition at 16.

[347] 47 C.F.R. § 54.101(c).

[348] Because state commissions are to designate eligible telecommunications carriers by January 1, 1998, these waiver proceedings would need to be completed prior to or on that date.

in a short time frame against the goal of giving low-income consumers a full range of options for controlling toll usage, we define toll-limitation services as either toll blocking or toll control and require telecommunications carriers to offer only one, and not necessarily both, of those services at this time in order to be designated as eligible telecommunications carriers. We note, however, that if, for technical reasons, a carrier cannot provide any toll-limitation service at this time, the carrier must seek a time-limited waiver of this requirement to be designated as eligible for support during the period it takes to make the network changes needed to provide one of those toll-limitation services. In addition, if a carrier is capable of providing both toll blocking and toll control, it must offer qualifying low-income consumers a choice between toll blocking and toll control. Because we agree with Catholic Conference that all qualifying low income consumers ideally should be offered their choice of toll blocking or toll control, we plan to monitor and revisit this issue if we determine that technological impediments to carriers' ability to offer toll limitation have been reduced or eliminated. We also encourage carriers to develop and investigate cost-effective ways to provide toll-control services.

116. We further conclude that carriers offering Lifeline service will not be required to provide toll-limitation services other than those specifically identified in the *Order*. The Commission defined toll blocking as a service that allows customers to block outgoing toll calls, and defined toll control as a service that allows customers to limit in advance their toll usage per month or billing cycle.[349] Therefore, carriers offering Lifeline service will not be required to offer, for example, international toll-call-blocking or toll blocking that allows callers with a Personal Identification Number (PIN) to make toll calls, as suggested by the Florida Commission. While we encourage carriers to offer Lifeline consumers, free of charge, toll-limitation services that include functions and capabilities beyond those described in the *Order*, we are persuaded by USTA that most carriers currently are technically incapable of providing these additional services. Furthermore, regarding the issue of whether toll control must limit collect calls, we conclude that, like toll blocking, toll control only must allow consumers to limit outgoing calls.

117. In response to the Texas Commission's request, we reiterate that toll-limitation services for qualifying low-income subscribers are included in the definition of the "core" or "designated" services that will receive universal service support. A carrier must provide these core services throughout its entire service area in order to be designated an eligible telecommunications carrier.[350] We further clarify that, compliance with the no disconnect rule[351]

[349] *Order*, 12 FCC Rcd at 8978-8979. *See also* 47 C.F.R. § 54.400(2).

[350] *See Order*, 12 FCC Rcd at 8821-8822.

[351] The no disconnect rule prohibits carriers from disconnecting customers who participate in the Lifeline program for nonpayment of toll charges. *See Order*, 12 FCC Rcd at 8983-8988.

and the prohibition on deposit rule[352] are not specific preconditions to being designated an eligible telecommunications carrier. Once designated as an eligible telecommunications carrier, however, that carrier must offer all Lifeline and LinkUp services to qualifying low-income subscribers.[353]

B. Recovery of PICC

1. Background

118. On May 7, 1997, the Commission adopted the *Access Charge Reform Order* that, among other things, created a new flat per-line charge assessed upon an end user's presubscribed interexchange carrier (IXC).[354] This flat, presubscribed interexchange carrier charge (PICC) will enable incumbent local exchange carriers to recover non-traffic sensitive common line costs not recovered through subscriber line charges (SLCs).[355] The PICC for primary residential lines will be capped at $0.53 per month for the first year, beginning January 1, 1998.[356] Beginning January 1, 1999, the ceiling on the monthly PICC on primary residential lines will be adjusted for inflation and will increase by $0.50 per year until the sum of the SLC plus the flat-rated PICC is equal to the price cap LEC's permitted common line revenues per line.[357] The sum of the single-line SLC and the PICC shall never exceed the sum of the maximum allowable multi-line SLC and multi-line PICC.[358] The Commission stated that incumbent LECs may collect directly from any customer who does not presubscribe to long distance service from an IXC the PICC that would otherwise be assessed against the presubscribed IXC at the beginning of each billing cycle.[359] The Commission instituted this policy to eliminate the incentive for customers to access long-distance services solely through "dial-around" carriers in order to avoid paying long-distance rates that reflect the PICC.[360]

[352] The prohibition on deposit rule provides that qualifying low-income consumers who elect toll blocking may not be required to pay service deposits. *See Order*, 12 FCC Rcd at 8988-8990.

[353] *See* 47 C.F.R. §§ 54.405, and 54.411.

[354] *Access Charge Reform Order* at paras. 91-105.

[355] *Access Charge Reform Order* at para. 91.

[356] *Access Charge Reform Order* at para. 94.

[357] *Access Charge Reform Order* at para. 94.

[358] *Access Charge Reform Order* at para. 94.

[359] *Access Charge Reform Order* at para. 92.

[360] *Access Charge Reform Order* at paras. 92-93.

119. Customers who elect toll blocking do not have a presubscribed IXC and, pursuant to our access rules, may be required to pay the $0.53 PICC directly to incumbent LECs.[361] On September 4, 1997, the Commission released a *Second Further Notice of Proposed Rulemaking* that proposed to waive the PICC charge for Lifeline customers who elect toll blocking and thus do not presubscribe to an IXC.[362] The Commission tentatively concluded that the costs of the PICC in such cases should be recovered from the low-income program of the new federal universal service support mechanisms and sought comment on this tentative conclusion.[363]

2. Pleadings

120. Several petitioners and commenters support the Commission's tentative conclusion to waive the PICC for Lifeline consumers who elect toll blocking, and to recover the waived PICCs from the low-income program of the federal universal service support mechanisms.[364] These parties generally take the position that toll blocking enables consumers to control their toll usage and that requiring Lifeline consumers to pay the PICC would undermine the Commission's intent to make toll blocking available free-of-charge. SBC argues that support for PICCs of low-income consumers who elect toll blocking should be provided in addition to the maximum $7.00 per Lifeline customer benefit established in the *Order*.[365] Sprint supports the Commission's proposal to waive the PICC for Lifeline customers, but asserts that the waived charges should be supported by the low-income program on a conditional basis for at least one year.[366] Sprint argues that, because it is difficult to predict the competitive effects of requiring competitors of incumbent LECs to contribute to the support of incumbent LECs, the Commission should monitor waived PICCs until it can be more "confident that the benefits of such increased

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[361] *Access Charge Reform Order* at para. 92.

[362] Federal-State Joint Board on Universal Service, Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge, CC Docket Nos. 96-45, 96-262, 94-1, 91-213, 95-72, *Second Further Notice of Proposed Rulemaking* (rel. Sept. 4, 1997) (*Second Further Notice*) at para. 5.

[363] *Second Further Notice* at para. 5.

[364] *See* Catholic Conference petition at 4-6; AT&T opposition at 25; BellSouth opposition at 10; Bell Atlantic comments to *Second Further Notice* at 1-2; MCI comments to *Second Further Notice* at 1-2; RTC comments to *Second Further Notice* at 3-4; SBC comments to *Second Further Notice* at 3; USTA comments to *Second Further Notice* at 2; US WEST comments to *Second Further Notice* at 2-3.

[365] SBC comments to *Second Further Notice* at 3-4.

[366] Sprint comments to *Second Further Notice* at 1-2.

burden outweigh the costs."[367] AT&T suggests that, to ensure competitive neutrality, the Commission should clarify that eligible competitive carriers that provide Lifeline service, as well as eligible incumbent LECs, may recover the waived PICC for consumers who elect toll blocking from the federal low-income program.[368] SBC opposes this proposal and contends that, because only price cap LECs are permitted to recover PICCs directly from end users who do not have presubscribed IXCs and are subject to regulation regarding the recovery of separated common line costs, only price cap LECs should be permitted to recover waived PICCs from the support mechanisms.[369] In the alternative, SBC proposes that the Commission limit support to eligible carriers that normally impose a charge on a presubscribed IXC and that collect such charges from end-user customers when those customers have toll blocking.[370] SBC further proposes to set support amounts as the lesser of such charge or the then-current PICC cap.[371]

121. AT&T argues that the federal low-income program should support all PICCs for low-income consumers who elect toll blocking, even if the consumers presubscribe to an IXC.[372] AT&T asserts that in rare instances a low-income consumer who has selected a presubscribed IXC and subsequently elects toll blocking may nevertheless continue to have a presubscribed IXC.[373] AT&T contends that, because the IXC will not receive revenue from a customer who elects toll blocking, the IXC should not be required to pay the PICC for that customer.[374] Instead, AT&T argues that the PICC for such a customer should be recovered from the federal low-income program.[375] Bell Atlantic counters that such action is not necessary to eliminate the financial barriers to a Lifeline consumer's selection of toll blocking, and, therefore, the IXC should remain responsible for those PICCs.[376] SBC contends that support should be provided to Lifeline customers who are placed on toll blocking as a result of failure to pay toll charges. SBC argues that requiring such Lifeline customers to pay the PICC would contradict the Commission's

[367] Sprint comments to *Second Further Notice* at 1-2.

[368] AT&T comments to *Second Further Notice* at 6.

[369] SBC comments to *Second Further Notice* at 5.

[370] SBC comments to *Second Further Notice* at 5-6.

[371] SBC comments to *Second Further Notice* at 5-6.

[372] AT&T comments to *Second Further Notice* at 5-6.

[373] AT&T comments to *Second Further Notice* at 5-6.

[374] AT&T comments to *Second Further Notice* at 5-6.

[375] AT&T comments to *Second Further Notice* at 5-6.

[376] Bell Atlantic comments to *Second Further Notice* at 1.

stated intention of ensuring that toll blocking be provided free-of-charge.[377] In addition, although the Florida Commission supports the Commission's tentative conclusion to waive the PICC for low-income consumers who elect toll blocking, it suggests that LECs recover all waived PICCs directly from IXCs.[378] The Florida Commission contends that the PICC is primarily intended to recover non-traffic sensitive (NTS) costs that currently are recovered from IXCs through the usage-sensitive carrier common line (CCL) charge.[379] Therefore, the Florida Commission argues that, because the PICC was intended to recover "IXC costs," IXCs should pay all PICCs.[380]

3. Discussion

122. Consistent with our efforts to make toll-blocking service easily affordable to low-income consumers, we adopt our tentative conclusion in the *Second Further Notice* to waive the PICC for Lifeline customers who elect toll blocking.[381] For the reasons discussed here and in succeeding paragraphs, we agree with SBC and AT&T and conclude that support for PICCs for Lifeline customers who have toll blocking, but nevertheless remain presubscribed to an IXC, will be provided by the universal service support mechanisms in addition to the support for Lifeline customers established in the *Order*. In the *Order*, the Commission noted that studies demonstrate that a primary reason subscribers terminate access to telecommunications services is failure to pay long-distance telephone bills.[382] The Commission concluded that, because voluntary toll blocking allows customers to block toll calls, and toll-control service allows customers to ensure that they will not spend more than a predetermined amount on toll calls, these services assist Lifeline customers in avoiding involuntary termination of their access to telecommunications services. The Commission concluded that, in order to increase the use of toll-blocking and toll-control services by low-income consumers, Lifeline customers should receive these services at no charge.[383] It would make little sense, and would undermine the very

[377] SBC comments to *Second Further Notice* at 8.

[378] Florida Commission comments to *Second Further Notice* at 2-3.

[379] Florida Commission comments to *Second Further Notice* at 3-4.

[380] Florida Commission comments to *Second Further Notice* at 3-4.

[381] The PICC is a charge through which incumbent LECs recover a portion of the costs of their local networks. Generally, incumbent LECs recover the PICC for each line from the IXC designated as the presubscribed interexchange carrier (PIC) for that line. Where the customer has not designated a PIC, we permit incumbent LECs to recover the PICC from the end user.

[382] *Order*, 12 FCC Rcd at 8980-8981 (*citing* Amendment of the Commission's Rules and Policies to Increase Subscribership and Usage of the Public Switched Network, *Notice of Proposed Rulemaking*, 10 FCC Rcd 13003, 13005-06 (1995)).

[383] *Order*, 12 FCC Rcd at 8980-8981. Although eligible telecommunications carriers will be prohibited from

basis for providing Lifeline customers free access to toll blocking, to assess the PICC on Lifeline customers who select toll blocking. In addition, in light of our decision herein to permit eligible carriers to offer either toll control or toll blocking, it would be particularly unfair to assess the PICC on Lifeline customers who do not have the option of selecting toll control, but that are limited to toll blocking. To do so would discriminate against Lifeline customers who may only select toll blocking, and thus would have no reason to presubscribe to an IXC. In contrast, a Lifeline subscriber who is able to select toll control likely will presubscribe to an IXC, because that subscriber's access to toll calling is limited, but not blocked entirely.

123. We thus conclude that, because toll blocking for low-income consumers is a supported service that carriers must provide to such customers and the PICC payment issue arises as a direct result of the toll blocking requirement, the PICC, in these instances, is sufficiently related to the provision of toll blocking that it should be supported for low-income consumers. Thus, such costs should be recovered in a competitively neutral manner that is consistent with section 254 of the Act. Therefore, all interstate telecommunications carriers, not just IXCs, should bear the costs of the waived PICCs.

124. Moreover, we agree with petitioners that the low-income program of the federal universal service support mechanisms should support PICCs attributable to all qualifying low-income consumers who have toll blocking. As stated above, we will support PICCs attributable to qualifying low-income consumers who have toll blocking but do not have a presubscribed IXC. We anticipate that most low-income consumers who receive toll blocking will do so voluntarily and that most will not have presubscribed IXCs. In the event, however, that a low-income consumer is required to elect toll blocking (*e.g.*, as a condition of receiving local service) or in the event that a low-income consumer remains presubscribed to an IXC even though the consumer receives toll blocking, the federal low-income program also will support the PICCs attributable to consumers in those circumstances. We disagree with Bell Atlantic that these revisions to our rules are unnecessary to protect the availability of toll blocking to low-income consumers. Low-income consumers who elect toll blocking, but who remain presubscribed to an IXC, would not receive toll blocking free-of-charge unless we waive the PICC for the consumers. If an IXC were required to pay the PICC attributable to a low-income consumer who elects toll blocking, that IXC would not be able to recover the PICC through per-minute charges associated with toll usage. Thus, absent changes to our rules, the IXC may seek to recover the PICC from the consumer in the form of a flat-rate charge. As we have noted above, toll blocking helps consumers to control their toll usage and should be available free-of-charge to qualifying low-income consumers. Therefore, to ensure the availability of toll blocking to all qualifying low-income consumers free-of-charge, we conclude that the low-income program of the federal

disconnecting Lifeline customers for failure to pay toll bills, this is not a substitute for access to toll-limitation services. The Commission sought to enable low-income consumers to take measures to ensure that they do not incur excessive toll charges in the first place.

universal service support mechanisms should support PICC charges attributable to all low-income consumers who have toll blocking.

125. We also agree with AT&T that all competitive eligible carriers that provide Lifeline service to customers who elect toll blocking should be able to recover an amount equal to the PICC that would be recovered by the incumbent LEC in that area from the low-income program of the federal universal service support mechanisms even though such carriers are not required to charge PICCs. Competitive eligible carriers should be able to receive support amounts equal to the PICCs because, like incumbent LECs, they will be unable to recover any portion of their costs associated with a toll-blocked customer from IXCs originating interexchange traffic on that customer's line. To avoid creating incentives for carriers to pass additional costs to low-income consumers through increased rates, we conclude that competitors should receive this additional support for Lifeline customers who elect to receive toll blocking. In addition, in order to ensure competitive neutrality, a competing local carrier serving a Lifeline customer should be able to receive the same amount of universal service support that an incumbent LEC would receive for serving the same customer. Because an incumbent LEC serving a low-income customer who elected toll blocking would receive support for the PICC associated with that customer, in order to ensure that competing local carriers are not operating at an unfair advantage, competing local carriers should be eligible to receive the same amount of support that the incumbent LEC would receive.

C. Florida Commission's Petition Pertaining to State Lifeline Participation

1. Background

126. The Commission's Lifeline program currently reduces end-user charges that low-income consumers in participating jurisdictions pay for some state-specified level of local service.[384] Support from the federal jurisdiction is provided in the form of a waiver of the federal SLC. To participate, states are required to generate a matching reduction in intrastate end-user charges. Participating states may generate their state support from any intrastate source.[385]

127. In the *Order*, the Commission concluded that a baseline amount of federal Lifeline support should be available in all states, irrespective of whether a state generates support from the intrastate jurisdiction.[386] With respect to states that generate intrastate Lifeline support,

[384] 47 C.F.R. § 69.104(j)-(l).

[385] *Order*, 12 FCC Rcd at 8967-8968.

[386] *Order*, 12 FCC Rcd at 8961.

the Commission did not prescribe a method by which states must generate such support.[387] In the *Order*, the Commission found "no reason at this time to intrude in the first instance on states' decisions about how to generate intrastate support for Lifeline."[388] Thus, the Commission did not require states to establish a state Lifeline fund, noting that many methods exist, including the competitively neutral surcharges on all carriers or the use of general revenues, that would not place the burden on any single group of carriers.

128. The Commission further determined in the *Order* that states that provide intrastate matching funds may set their own consumer qualification standards, but must base such standards on income or factors directly related to income.[389] With respect to states that do not participate in Lifeline by providing intrastate matching support, the Commission adopted a federal default Lifeline qualification standard. To qualify for Lifeline under the federal default standard, consumers must participate in Medicaid, food stamps, Supplementary Security Income (SSI), federal public housing assistance or Section 8, or Low-Income Home Energy Assistance Program.[390]

2. Pleadings

129. The Florida Commission seeks a declaratory ruling as to whether its state Lifeline program qualifies as a program that provides intrastate matching funds for purposes of determining whether its state-imposed consumer qualification standard or the federal default standard applies.[391] The Florida Commission explains that the state of Florida does not have Lifeline support mechanisms to which all carriers must contribute.[392] Rather, Florida state law provides that " . . . a telecommunications company serving as a carrier of last resort shall provide a Lifeline Assistance Plan to qualified residential subscribers, as defined in a commission-approved tariff . . . ."[393] Thus, as the Florida Commission explains, incumbent LECs provide a rate reduction of $3.50 per month to Lifeline consumers, but no state mechanism requires other

[387] *Order*, 12 FCC Rcd at 8967-8968.

[388] *Order*, 12 FCC Rcd at 8967-8968.

[389] *Order*, 12 FCC Rcd at 8973.

[390] *Order*, 12 FCC Rcd at 8973-8974.

[391] Florida Commission Petition for Declaratory Statement, Waiver, and Clarification and Request for Expedited Ruling, CC Docket No. 96-45 (Oct. 9, 1997) (Florida Commission Oct. 9 petition).

[392] Florida Commission Oct. 9 petition at 3-4.

[393] FLA. STAT. § 364.10(2).

carriers to contribute to state Lifeline support mechanisms.[394] The Florida Commission maintains that, "[w]hile the FCC has not mandated the creation of a state fund for carriers to obtain the $1.75 federal contribution above the baseline, it is not clear to [us] that our program will qualify as 2-for-1 matching for state participation in Lifeline."[395]

130. In response to the Florida Commission's petition, the Citizens of Florida, through the Office of Public Counsel (Citizens of Florida), asserts that Florida's Lifeline program qualifies as state participation and is thus eligible for federal matching funds in the amount of $.50 for every $1.00 provided by the state.[396] Citizens of Florida maintains that the *Order* "did not intend to disqualify existing state Lifeline programs from federal matching funding" and asserts that the Commission "went out of its way to state that it would not prescribe the methods states must use to generate intrastate Lifeline support."[397]

131. If we determine that Florida's state Lifeline program does not qualify as state participation, the Florida Commission seeks a waiver of the federal default consumer qualification standard to include the Temporary Assistance to Needy Families (TANF) program. The Florida Commission points out that the Commission did not include Aid to Families with Dependent Children (AFDC) in the federal default consumer qualification standard and that, although AFDC was significantly curtailed by the recently enacted welfare reform law, AFDC-successor programs funded under TANF should be included in the federal default standard.[398] Alternatively, the Florida Commission seeks a waiver to allow the Florida Commission to set eligibility requirements or implement a grandfather provision for certain Lifeline recipients.[399]

3. Discussion

132. Consistent with the Commission's earlier finding that we should not prescribe the methods that states use to generate intrastate Lifeline support in order to qualify for federal support, we conclude that, although all carriers are not required to contribute to Florida's Lifeline

[394] Florida Commission Oct. 9 petition at 3-4.

[395] Florida Commission Oct. 9 petition at 4.

[396] Comments by the Citizens of Florida on the Florida Public Service Commission's Petition for Declaratory Statement, Waiver, and Clarification, filed with William F. Caton, FCC, October 31, 1997 (Citizens of Florida *ex parte*), at 7-8.

[397] Citizens of Florida *ex parte* at 7.

[398] Florida Commission Oct. 9 petition at 2-3.

[399] Florida Commission Oct. 9 petition at 5.

support mechanisms, Florida's Lifeline program nevertheless qualifies as providing intrastate matching funds. We, however, encourage states to develop Lifeline matching programs that are competitively neutral and emphasize that, as noted in the *Order*, states must meet the requirements of section 254(e) in providing equitable and non-discriminatory support for state universal service support mechanisms.[400] Because we find that Florida's Lifeline program qualifies as state participation, we need not address the Florida Commission's request for a waiver of the federal default Lifeline qualification standard. For the same reason, we also decline to address the Florida Commission's request for a waiver allowing it to set eligibility requirements or implement a grandfather provision for certain Lifeline recipients.[401]

VI. SCHOOLS, LIBRARIES, AND RURAL HEALTH CARE PROVIDERS

A. Lowest Corresponding Price

1. Background

133. In the *Order*, the Commission concluded that, to ensure that inexperience does not prevent schools and libraries from receiving competitive prices, service providers must offer services to eligible schools and libraries at prices no higher than the lowest price the provider charges to similarly situated non-residential customers for similar services.[402] The Commission concluded that this requirement would not impose an unreasonable burden on service providers because all providers would be able to receive a remunerative price for their services. The *Order* stated that a provider need not offer the same lowest corresponding price to different schools and libraries in the same geographic service area if they are not similarly situated and do not subscribe to a similar set of services.[403] The Commission clarified that, for the purpose of determining the lowest corresponding price, similar services would include those provided under contract as well as those provided under tariff.[404] The Commission established a rebuttable presumption that rates offered within the previous three years are still compensatory.[405]

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[400] *Order*, 12 FCC Rcd at 8967-8968.

[401] We note that Florida's Lifeline consumer qualification standard must be based on income or factors directly related to income, pursuant to the *Order*. *See Order*, 12 FCC Rcd at 8973.

[402] *Order*, 12 FCC Rcd at 9031-9032.

[403] *Order*, 12 FCC Rcd at 9033-9034.

[404] *Order*, 12 FCC Rcd at 9032.

[405] *Order*, 12 FCC Rcd at 9034.

134. The Commission held that it would not require a service provider to match a price offered to a customer who is receiving a special regulatory subsidy or that was negotiated under very different conditions, if offering the service at such price would result in a rate below Total-Service Long-Run Incremental Cost (TSLRIC).[406]

135. The Commission also provided that, if schools, libraries, or providers believe that the lowest corresponding price is unfair, they may seek recourse from the Commission, regarding interstate rates, and from state commissions, regarding intrastate rates.[407] Eligible schools and libraries may request a lower rate if they believe the rate offered by the provider is not the lowest corresponding price. Providers "may request higher rates if they believe that the lowest corresponding price is not compensatory."[408] The Commission concluded that service providers will be permitted to charge schools and libraries prices higher than those charged to other similarly situated customers if the services sought by a school or library will generate significantly different traffic volumes or the provision of such services is significantly different from that of another customer with respect to any other factor that the state public service commission has recognized as being a significant cost factor.[409]

2. Pleadings

136. USTA seeks reconsideration of the Commission's decision to establish a rebuttable presumption that rates offered by a service provider within the previous three years are compensatory for purposes of calculating the lowest corresponding price that the provider must offer to an eligible school or library.[410] USTA contends that the three-year "look back" provision is unnecessarily burdensome, would impede the timeliness of the bidding process, and is not competitively neutral because it disadvantages larger providers with more potential contracts or prices to review.[411] USTA contends that each additional year that a provider must "look back" to determine the lowest corresponding price increases the number of customer contracts that a service provider must review.[412] GTE agrees with USTA and suggests that a one-year period

[406] *Order*, 12 FCC Rcd at 9034.

[407] *Order*, 12 FCC Rcd at 9034.

[408] *Order*, 12 FCC Rcd at 9034.

[409] *Order*, 12 FCC Rcd at 9034.

[410] USTA petition at 17.

[411] USTA petition at 17-18.

[412] USTA petition at 17.

would be more appropriate.[413]

137. USTA contends that the *Order* could be construed to require a carrier to provide service to a school or library at the same rate as another service provided under a special regulatory subsidy or negotiated under very different conditions.[414] USTA argues that

[413] GTE comments at 14.

[414] USTA petition at 18-19.

such a result is untenable.[415] In addition, USTA contends that many service providers must provide service rates at regulated tariffs, and that to require service providers to base their lowest corresponding price on historical or expired tariff rates would force the provider to offer a price that would be unlawful for that provider.[416] GTE contends that the Commission should clarify that promotional offerings are excluded from the comparable rates upon which the lowest corresponding price is determined.[417] Bell Atlantic contends that some states have established special rates for schools and libraries in anticipation of the *Order*, "under the assumption that the support in section 254(h)(1)(B) would apply to the difference between generally-available rates and the special school and library rate."[418] Bell Atlantic contends that there is no justification for classifying these special rates as the pre-discount price.[419]

138. USTA also requests that limits be placed upon the customer's ability to challenge the pre-discount price it has been offered.[420] USTA argues that, without such limits, customers could abuse the process by filing frivolous claims to obtain even more favorable rates.[421]

3. Discussion

139. Neither USTA nor any other party offers persuasive evidence that the three-year "look back" provision for determining the lowest corresponding price is either unnecessarily burdensome or will unfairly delay a service provider's participation in the bidding process.[422] Commenters do not assert that the relevant records are not maintained or are not accessible. We note that the universe of records that the provider must review to determine the lowest corresponding price is limited to charges involving similarly situated, non-residential customers for similar services.

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[415] USTA petition at 19.

[416] USTA petition at 18.

[417] GTE comments at 15.

[418] Bell Atlantic comments at 13.

[419] Bell Atlantic comments at 13.

[420] USTA petition at 19-20.

[421] USTA petition at 19-20.

[422] The "lowest corresponding price" is the lowest price that a service provider charges to non-residential customers who are similarly situated to a particular school, library, or library consortium for similar services. *See* 47 C.F.R. § 54.500.

140. We do not agree with USTA that the three-year "look back" provision violates the principle of competitive neutrality by disadvantaging larger providers. We note that this requirement applies equally to all providers and that, although larger providers may have a greater number of records to review for purposes of determining the lowest corresponding price, these providers also likely have greater resources and more sophisticated methods of recordkeeping.

141. We agree with USTA, however, that we should modify our earlier holding to clarify the application of our lowest corresponding price requirement.[423] We conclude that, for purposes of calculating the lowest corresponding price, a provider will not be required to match a price it offered to a customer under a special regulatory subsidy or that appeared in a contract negotiated under very different conditions. For example, we previously concluded that service providers will be permitted to charge schools and libraries prices higher than those charged to other similarly situated customers if the services sought by a school or library include significantly different traffic volumes or the provision of such services is significantly different from that of another customer with respect to any other factor that the state public service commission has recognized as being a significant cost factor.[424] Under our modified rules, a service provider will not be required to demonstrate further that matching such a price would force the provider to offer service at a rate below the compensatory rate for that service. The use of a rate below the compensatory rate would not be practical, given the limited resources of schools and libraries to participate in lengthy negotiations, arbitration, or litigation. Regarding Bell Atlantic's concern that special regulatory rates established by states for schools and libraries should not be treated as the pre-discount prices, we reiterate that special regulatory subsidies need not be considered in determining the lowest corresponding price. Consistent with our findings above, we conclude that each such situation should be examined on a case-by-case basis to determine whether the rate is a special regulatory subsidy or is generally available to the public. We also note that the universal service discount mechanism is not funding the difference between generally available rates and special school rates, as suggested by Bell Atlantic, but is applied to the price at which the service provider agrees to provide the service to eligible schools and libraries.

142. We disagree with USTA that earlier versions of tariffs that have been modified by regulators should be excluded from the comparable rates upon which the lowest corresponding price is determined. Unless a regulatory agency has found that the tariffed rate should be changed, and affirmatively ordered such change, or absent a showing that the rate is not compensatory, we find no reason to conclude that former tariffed rates do not represent a fair and reasonable basis for establishing the lowest comparable rate.

[423] USTA petition at 18-19.

[424] *Order*, 12 FCC Rcd at 9034.

143. We decline to adopt GTE's proposal to exclude all promotional offerings from the comparable rates upon which a provider must determine the lowest corresponding price. Instead, we conclude that only promotions offered for a period not exceeding 90 days may be excluded from the comparable rates upon which the lowest corresponding price must be determined. This conclusion is consistent with the decision of the U.S. Court of Appeals for the 8th Circuit upholding the portion of the Commission's interconnection decision finding that discounted and promotional offerings are telecommunications services that are subject to the resale requirement of section 251(c)(4), and that promotional prices lasting more than 90 days qualify as retail rates subject to wholesale discount.[425] Excluding shorter term promotional rates from consideration here balances the need to provide compensatory rates to providers while ensuring that eligible schools and libraries receive competitive, cost-based rates that are comparable to rates paid by similarly situated non-residential customers for similar services. Consistent with the Commission's rationale in the *Implementation of Section 254(g) Order*,[426] we agree that a 90-day period in which customers may receive discounted rates as part of a promotion is sufficient time for a targeted promotional offering to attract interest in new or revised services, but not so long as to undermine the requirement that the price offered to schools and libraries be no greater than the lowest corresponding price the carrier has charged in the last three years or is currently charging in the market.

144. As previously noted, providers and eligible schools and libraries will have the opportunity to seek recourse from the Commission, regarding interstate rates, and from state commissions, regarding intrastate rates if they believe that the lowest corresponding price is unreasonably low or unreasonably high.[427] We decline to adopt the suggestion of USTA that we impose limits on a customer's ability to challenge the pre-discount price it has been offered. We have no basis in this record for assuming that the possibility of such abuse by schools and libraries is greater than the potential for service providers to assert frivolously that the rates are too low. We will monitor parties' use of the dispute process and, if we find a pattern of frivolous challenges by schools, libraries, or service providers, we will take steps to remedy any such abuse at that time.

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[425] *Iowa Utilities Board v. FCC*, 120 F.3d 753, 818-820 (8th Cir. 1997) (holding that rule restricting ability of incumbent carriers to circumvent their resale obligations by offering services to subscribers at perpetual promotional rates was reasonable interpretation of statute).

[426] *See* Policy and Rules Concerning the Interstate, Interexchange Marketplace: Implementation of Section 254(g) of the Communications Act of 1996, *Report and Order*, CC Docket No. 96-61, FCC 96-331, 11 FCC Rcd 9564, 9578 (1996) (finding that a 90-day period in which customers may receive discounted rates as part of a promotion is sufficient time for a targeted promotional offering to attract interest in new or revised services, but not so long as to undermine the Commission's geographic rate averaging requirement) (*Implementation of Section 254(g) Order*).

[427] *Order*, 12 FCC Rcd at 9034.

B. Reporting Requirements for Schools and Libraries

1. Background

145. In the *Order*, the Commission determined that eligible schools and libraries seeking universal service discounts shall be required to: (1) conduct an internal assessment of the components necessary to use effectively the discounted services they order; (2) submit a complete description of services they seek so that it may be posted for competing providers to evaluate; and (3) certify to certain criteria under penalty of perjury.[428] The Commission required eligible schools and libraries to prepare and submit technology plans as part of their application for service. To ensure that technology plans are based on the reasonable needs and resources of the applicant and are consistent with the goals of the program, the Commission required approval of an applicant's technology plan, by the state or another entity.[429] The Commission noted that it would consult with the Department of Education in designing an application for this process.[430] Schools and libraries seeking universal service support must file FCC Form 470 and FCC Form 471.[431]

2. Pleadings

146. Global Village Schools Institute (Global) contends that section 254(h)(1)(B) requires only that eligible schools and libraries submit a bona fide request for services.[432] Global seeks reconsideration of the Commission's decision to require schools and libraries to prepare or include reports of technology inventories or assessments in their applications for telecommunications services. Global asks that the Commission not require specific local education technology planning activities, independent approval of local education technology plans, or submission of local educational technology plans as part of the application for

[428] *Order*, 12 FCC Rcd at 9076.

[429] *Order*, 12 FCC Rcd at 9078. The Commission also sought guidance from the Department of Education and the Institute for Museum and Library Services on alternative technology plan approval measures.

[430] *Order*, 12 FCC Rcd at 9076-9077.

[431] On December 8, 1997, the Commission's Common Carrier Bureau submitted to the Schools and Libraries Corporation the application forms to receive support under the federal universal service support mechanisms for schools and libraries. *See* Letter from A. Richard Metzger, Jr., FCC, to Ira Fishman, Schools and Libraries Corporation, dated December 8, 1997.

[432] Global petition at 3.

telecommunications services.[433] It argues that these application requirements are not essential elements of the purchasing process, that they usurp state and local authority for educational decision-making, and that they represent a reporting burden in excess of what is allowed under the Paperwork Reduction Act.[434]

147. Florida Department of Management Services, requests authorization for Florida to use that state's Advanced Telecommunications Service Request Form during the first year of the new universal service support mechanisms to apply for support.[435]

3. Discussion

148. We conclude that the reporting requirements established in the *Order* for eligible schools and libraries are not unreasonably burdensome, and that they represent a reasonable means of ensuring that schools and libraries are capable of utilizing the requested services effectively. Section 254(h)(1)(B) provides for discounts on services that are used for educational purposes and that are provided in response to a bona fide request.[436] In the *Order*, the Commission agreed with the Joint Board that Congress intended to require accountability on the part of schools and libraries and therefore, consistent with section 254(h)(1)(B), required eligible schools and libraries to conduct an internal assessment of the components necessary to use effectively the discounted services they order.[437] We note that the application requirements established in the *Order* were recommended by the Joint Board and supported by a majority of commenters on this issue.[438] We affirm our decision, because we find that it is in the public interest to ensure that funds are distributed only to support eligible services that serve the needs of the school or library requesting support. We find that the mere submission of a bona fide request is not an adequate substitute to ensure that these public interest goals are met.

149. The Commission determined in the *Order* that it would not be unduly burdensome to require eligible schools and libraries to conduct a technology assessment, prepare a plan for using these technologies, and receive independent approval of such plans.[439] Moreover, the

[433] Global petition at 8.

[434] Global petition at 8-9.

[435] Florida Department of Management Services petition at 2.

[436] 47 U.S.C. § 254(h)(1)(B).

[437] *Order*, 12 FCC Rcd at 9076. *See also* section VI.C, *infra*.

[438] *Order*, 12 FCC Rcd at 9076.

[439] *Order*, 12 FCC Rcd at 9077.

Commission took steps to eliminate unnecessary burdens, and prevent the need for duplicative review of technology plans. The Commission noted that many states have already undertaken state technology initiatives and that plans that have been approved for other purposes, e.g., for participation in federal or state programs, such as "Goals 2000," will be accepted without need for further independent approval.[440] We also note that the reporting requirements have been reviewed and approved by the Office of Management and Budget (OMB) pursuant to the Paperwork Reduction Act of 1995.[441] Because we conclude that the reporting requirements are not unduly burdensome, help ensure that funds are allocated in a manner that serves the policy goals set forth in section 254(b)(6) and section 254(h), and do not violate section 254(h)(1)(B), we deny Global's petition for reconsideration of those requirements.

150. We also deny Florida Department of Management Services' request to apply, during the first year of the federal support mechanisms, for universal service discounts using a form created by the state of Florida. We find that requiring all applicants to use the same forms serves several important purposes. First, the forms were designed to ensure accountability, and protect against fraud and abuse. For example, the forms require applicants to provide information designed to ensure that each school or library receives the discount to which it is entitled under the Commission's rules.[442] The forms also are designed to ensure that support is provided only with respect to eligible entities,[443] and only for services eligible for support,[444] and that applicants are otherwise in compliance with all applicable Commission requirements. Second, the forms were designed to facilitate the use of competitive bidding.[445] In addition, the forms were designed to be competitively neutral, so that no potential provider is precluded from offering service to a school or library.[446] Third, the use of a single set of forms will substantially ease burdens of administering the support mechanism, and thereby minimize the costs of administration. Moreover, if funds are allocated pursuant to a single set of forms, it may be

[440] *Order*, 12 FCC Rcd at 9078.

[441] 62 Fed. Reg. at 66,368 (1997).

[442] *See, e.g.,* FCC Form 470 Block 2; FCC Form 471 Blocks 5 and 6.

[443] *See e.g.*, FCC Form 470 Blocks 1 and 5; FCC Form 471 Block 1.

[444] *See, e.g.,* FCC Form 470 Block 3; FCC Form 471 Blocks 3 and 5.

[445] For example, FCC Form 470 Block 3, Item (11) asks whether the applicant has available a Request for Proposals (RFP), and if so, asks the applicant to provide the website address of such RFP, if there is one.

[446] For example, Block 3 of FCC Form 470, which asks the applicant for a summary description of needs or services requested, is phrased in a manner that ensures that both wireline and wireless carriers may bid to provide service.

easier to audit the administrative processes of the Schools and Libraries Corporation.[447] Fourth, the use of a single set of forms will facilitate tracking of the schools and libraries support mechanism over time. For example, it will make it easier to determine what types of services schools and libraries need, and how those needs change over time. Such information is useful for deciding what if any adjustments should be made with respect to the schools and libraries mechanism. Congress expressly provided for such adjustments.[448]

151. We note that the Commission invited, and received, substantial input on the application forms as they were developed. The Commission, in conjunction with the Schools and Libraries Corporation, held a public workshop, and draft application forms were posted on the Commission's website.[449] The application forms reflect comments and suggestions from schools and library representatives, service providers, the Department of Education and the Schools and Libraries Corporation. We anticipate that, as parties begin to use the application forms, they will discover ways to improve them, and we encourage suggestions for modifying and improving the application forms. For the reasons set forth above, however, we conclude that requiring all applicants to use the same application forms will serve the public interest. We find that it is particularly important, in the first year of implementation, to take all reasonable steps to make sure the Schools and Libraries Corporation is able to administer the support mechanism as efficiently and effectively as possible. We therefore deny Florida Department of Management Services' request to use its own application form.

C. Non-Public Schools and Libraries

1. Background

152. In the *Order*, the Commission determined that a school, whether public or private, is eligible for universal service discounts, if it falls within definitions contained in the Elementary and Secondary Education Act of 1965, does not operate as a for-profit business, and does not have an endowment exceeding $50 million.[450]

153. In order to fulfill the mandate of section 254(h)(1)(B) that only eligible entities

[447] *See* 47 C.F.R. § 69.621 (requiring an annual independent audit of the Schools and Libraries Corporation).

[448] 47 U.S.C. § 254(c). *See also* 47 U.S.C. § 254(b)(7).

[449] *See* Public Notice, October 10 Workshop Sponsored by the Common Carrier Bureau and the Schools and Libraries Corporation on Application Forms, DA Number 97-2152 (rel. Oct. 3, 1997).

[450] 47 C.F.R. § 54.501(b). The Elementary and Secondary Education Act of 1965 can be found at 20 U.S.C. § 8801(14) and (25); *Order*, 12 FCC Rcd at 9068.

receive discounted services, that such services be provided in response to a bona fide request, and that those services be used for educational purposes, the Commission determined that it was necessary to require eligible schools and libraries to conduct an internal assessment of the components necessary to use effectively the discounted services they order.[451] The Commission required all applications for universal service discounts from schools and libraries to include a technology inventory assessment of the telecommunications-related facilities the school or library already has in place or plans to acquire.[452] In addition, the Commission directed schools and libraries to prepare specific plans for using these technologies, both during the near term and in the future, and to describe how schools and libraries plan to integrate the use of these technologies in their curricula.[453] To ensure that these technology plans are based on the reasonable needs and resources of the applicant and are consistent with the goals of the program, the *Order* also required independent approval of an applicant's technology plan, "ideally by a state agency that regulates schools or libraries."[454] In the *NECA Report and Order*, the Commission concluded that the Schools and Libraries Corporation, the entity charged with administering significant aspects of the universal service support mechanisms for schools and libraries, may approve schools' and libraries' technology plans when a state agency has indicated that it will be unable to review such plans within a reasonable time.[455] In that *Order*, the Commission also stated that it anticipated that the Department of Education and the Institute for Museum and Library Services may recommend alternative review measures.[456] The Commission stated its intent to review any such proposals and determine whether to adopt additional review measures.[457]

2. Pleadings

154. The National Association of Independent Schools contends that institutions with technology plans approved under such programs as Goals 2000 or the Technology Literacy

[451] *Order*, 12 FCC Rcd at 9076.

[452] *Order*, 12 FCC Rcd at 9077.

[453] *Order*, 12 FCC Rcd at 9077.

[454] *Order*, 12 FCC Rcd at 9078.

[455] Changes to the Board of Directors of the National Exchange Carrier Association, Inc., Federal-State Joint Board on Universal Service, *Report and Order and Second Order on Reconsideration*, CC Docket No. 97-21, CC Docket No. 96-45, FCC 97-253 (rel. July 18, 1997) (*NECA Report and Order*) at para. 67.

[456] *NECA Report and Order* at para. 67.

[457] *NECA Report and Order* at para. 67.

Challenge will have an advantage over those institutions that require independent technology plan approval.[458] It also contends that non-public schools and libraries that do not have pre-approved technology plans or whose state agency refuses to review technology plans will be at a competitive disadvantage "as this highly time consuming application step will have been eliminated" for some schools and libraries.[459] Therefore, the National Association of Independent Schools suggests that technology plan approval should be waived for all schools and libraries for the first year, or at least six months, in order to provide sufficient time to develop alternative approval mechanisms.[460] In the event that such a waiver is not granted, the National Association of Independent Schools proposes that eligible schools and libraries should be permitted to check a box on the application form indicating that approval of a technology plan is pending and attach a copy of the technology plan to the application.[461] It argues that this approach would allow schools and libraries to initiate the application process in a timely manner. In addition, under the proposal of the National Association of Independent Schools, schools and libraries would indicate on FCC Form 471 that the technology plan had been approved during the four-week posting period or that it was still being reviewed. In the event of pending review, the allowable discount on the request for telecommunications services would be placed "in escrow" by the Schools and Libraries Corporation until such time as the technology plan is approved.[462] Thus, under this proposal, support would not be distributed unless and until the technology plan was approved.

155. The National Association of Independent Schools also recommends consideration of alternative approval mechanisms through either the state education agency or peer review panels.[463] It recommends that consideration be given to providing as many options as possible, including peer review panels comprised of representatives of the following groups:

1) local, state, or regional private school associations;
2) a technologically advanced model school, which would be appointed by a state or regional private school association;
3) a school consortium or central school authority, e.g., a diocese;

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[458] Letter from Jefferson Burnett, National Association of Independent Schools, to William Caton, FCC, dated October 2, 1997 (National Association of Independent Schools October 2 *ex parte*) at 1.

[459] National Association of Independent Schools October 2 *ex parte* at 1.

[460] National Association of Independent Schools October 2 *ex parte* at 1.

[461] National Association of Independent Schools October 2 *ex parte* at 1.

[462] National Association of Independent Schools October 2 *ex parte* at 1-2.

[463] National Association of Independent Schools October 2 *ex parte* at 2.

4) the U.S. Department of Education's Office of Nonpublic Education;
5) state Education and Library Network Coalition (EdLiNC); and
6) the Schools and Libraries Corporation.[464]

156. On July 31, 1997, the "E-Rate Implementation Working Group" (Working Group) filed a report with the Commission in response to the Commission's request to the U.S. Department of Education for guidance on certain issues regarding universal service support for schools and libraries.[465] The Working Group recommends that state agencies be allowed to delegate responsibility for approving technology plans to a peer review panel.[466] As an alternative mechanism for approving technology plans for schools and libraries that are not required by applicable state or local law to obtain state approval, the Working Group suggests that the Schools and Libraries Corporation should authorize "peer reviews" administered by independent entities, including existing peer reviews used by nonpublic schools for accreditation.[467]

3. Discussion

157. It is our expectation that states will approve technology plans in a reasonably timely manner. As noted above, however, the Schools and Libraries Corporation has authority to review and certify the technology plans of schools and libraries if the applicant provides evidence that a state agency is unwilling or unable to do so in a reasonably timely fashion.[468] We here conclude that a school or library may apply directly to the Schools and Libraries Corporation for technology plan approval if the school or library is not required by state or local law to obtain approval for technology plans and telecommunications expenditures. The Schools and Libraries Corporation has stated its intent to create a process for reviewing technology plans of private

[464] National Association of Independent Schools October 2 *ex parte* at 2.

[465] In the *Order*, the Commission sought guidance from the U.S. Department of Education on, for example, design of the schools and libraries applications and alternative technology plan approval measures. *Order*, 12 FCC Rcd at 9076-9078. The U.S. Department of Education formed a Working Group to assist in this process. The Working Group is comprised of the U.S. Department of Education, Institute of Museum and Library Services, National Telecommunications and Information Administration, Rural Utilities Service, and Education and Library Network Coalition. *See* U.S. Department of Education, Institute of Museum and Library Services, National Telecommunications and Information Administration, Rural Utilities Service, Education and Library Network Coalition, *Report by the E-Rate Implementation Working Group* (July 31, 1997) (Working Group Report).

[466] The Working Group also recommends that the state be required to notify the Schools and Libraries Corporation of any such delegation of authority to approve technology plans. Working Group Report at 19.

[467] Working Group Report at 19.

[468] *NECA Report and Order* at para. 67.

schools and other eligible entities whose states are unable to review their plans.[469] The Schools and Libraries Corporation may structure the review process in any manner it deems necessary to complete review in a timely fashion, consistent with the purposes of the review. We emphasize, however, that schools and libraries that are subject to a state review process by state or local law may not circumvent the state process by submitting plans directly to the Schools and Libraries Corporation for review. Eligible schools and libraries that are required by state or local law to obtain approval for technology plans and telecommunications expenditures will be allowed to submit technology plans to the Schools and Libraries Corporation for review only when the state is unwilling or unable to review such plans in a reasonably timely fashion. In addition, if a technology plan is rejected at the state level, a school or library may not then submit the plan to the Schools and Libraries Corporation in an attempt to circumvent the state review process.

158. In addition, FCC Forms 470 and 471 will allow applicants to indicate that their technology plans either have been approved or will be approved by a state, Schools and Libraries Corporation, or by another authorized body. This provision will allow schools and libraries that are required to obtain technology plan approval from an entity other than a state agency to submit both FCC Forms 470 and 471 without any delay due to a lack of technology plan approval. Schools and libraries will not be able to receive actual discounts, however, until their technology plans are approved.

159. Given the Schools and Libraries Corporation plan to institute an approval process that "will occur in sufficient time to meet the needs of those schools that choose to apply under the 75 day window,"[470] we see no need to adopt the suggestion of the National Association of Independent Schools that we waive the technology plan approval requirement for all schools and libraries for the first six to twelve months of the schools and libraries program in order to provide sufficient time to develop alternative approval mechanisms. We understand that the Schools and Libraries Corporation is moving forward with due diligence to ensure that their technology plan review process is put into place as quickly as possible. We reiterate that approval of an applicant's technology plan will assist in ensuring that technology plans are based on the reasonable needs and resources of the applicant and are consistent with the goals of the program.

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[469] Letter from Ira Fishman, Schools and Libraries Corporation, to Magalie Roman Salas, FCC, dated December 2, 1997 (SLC Dec. 2 *ex parte). See also* 47 C.F.R. § 69.619(c) (stating that "[t]he Schools and Libraries Corporation may review and certify schools' and libraries' technology plans when a state agency has indicated that it will be unable to review such plans within a reasonable time.").

[470] SLC Dec. 2 *ex parte*. *See also* Schools and Libraries Corporation and Rural Health Care Corporation Adopt Length of Filing Windows, *Public Notice*, CC Docket No. 96-45, DA 97-2349 (rel. Nov. 6, 1997) (noting that "all requests for support filed pursuant to a signed contract and received by the Schools and Libraries Corporation within 75 days of the day the Schools and Libraries Corporation begins to receive requests will be treated as if they were simultaneously received.")

D. Option to Post Requests for Proposals on Websites

1. Background

160. In the *Order*, the Commission required that schools, libraries, and rural health care providers, as a condition of their eligibility to receive universal service discounts, comply with a competitive bid requirement.[471] Pursuant to this requirement, schools, libraries, and rural health care providers must submit a request for services to the Administrator.[472] To allow schools, libraries, and rural health care providers to take advantage of the competitive marketplace, this request will be posted on either the school and library website or the rural health care provider website.[473] In the *Order*, the Commission stated, " . . . while schools and libraries may submit formal and detailed [requests for proposals] RFPs to be posted, . . . we will also permit them to submit less formal descriptions of services."[474] On July 18, 1997, the Commission released an order establishing the structure of the three corporations charged with administering the federal universal service support mechanisms.[475] On August 15, 1997, the Commission authorized NECA to perform certain functions on behalf of these corporations until the corporations are operational and can assume their respective duties.[476] Among other duties, the Commission authorized NECA to begin developmental work to create and design the websites that will be used to post competitive bids under the schools and libraries program and the rural health care program.[477]

2. Pleadings

[471] *Order*, 12 FCC Rcd at 9028-9029, 9078-9079, 9133-9134.

[472] *Order*, 12 FCC Rcd at 9028-9029, 9078-9079, 9133-9134.

[473] *Order*, 12 FCC Rcd at 9028-9029, 9078-9079, 9133-9134.

[474] *Order*, 12 FCC Rcd at 9078-9079; *see also Order*, 12 FCC Rcd at 9133-9134 (stating, that "[a]s with schools and libraries, the [rural health care provider's] request [for services] may be as formal and detailed as the health care provider desires . . . .").

[475] *NECA Report and Order* (directing the creation of USAC, the Schools and Libraries Corporation, and the Rural Health Care Corporation) at paras. 30, 57-60.

[476] Changes to the Board of Directors of the National Exchange Carriers Association, Inc., Federal-State Joint Board on Universal Service, *Order on Reconsideration, Second Report and Order, and Further Notice of Proposed Rulemaking*, CC Docket No. 97-21, CC Docket No. 96-45, FCC 97-292 (rel. Aug. 15, 1997) (*NECA Second Report and Order*) at paras. 8-12.

[477] *NECA Second Report and Order* at para. 11.

161. The Working Group recommends that, at least during the interim phase, the administrative corporations not post RFPs on the websites. It found, based on input from service providers, that "large quantities of information that has simply been digitized in textual form will be of limited usefulness."[478] The Working Group further recommends that RFPs should not be transmitted to the Schools and Libraries Corporation, but should instead be made available to potential bidders upon request.[479] On October 6, 1997, NECA submitted an *ex parte* letter to the Commission seeking clarification that the Commission's rules require posting of only a summary of the requested services sufficient for providers to draft bids and not the posting of full RFPs.[480] NECA contends that requiring applicants to post a summary request for services, rather than a full RFP, will help to ensure that systems for posting requests for services are operational by the commencement date of the universal service program.[481]

3. Discussion

162. In light of the concerns expressed by the Working Group and NECA, including significant costs and potential delays associated with requiring the administrative companies to post RFPs on the school and library and rural health care provider websites, we reconsider the Commission's requirement that the administrative companies post on the websites RFPs submitted by applicants. An RFP is a detailed request for the services and facilities that an entity is interested in procuring. RFPs may vary greatly in length, numbering over a hundred pages in some cases, including diagrams and specifications of the procurement of facilities. FCC Form 470,[482] submitted by school and library applicants, and FCC Form 465,[483] submitted by eligible health care applicants, will instruct applicants to describe the services they seek and to include information sufficient to enable service providers to identify potential customers.[484] We

[478] Working Group Report at 12. *See supra* section VI.C.2 for a discussion of the composition of the Working Group.

[479] Working Group Report at 12 (recommending in lieu of such transmissions, the use of standardized checklists, along with a short summary description of the applicant's objective in procuring the services).

[480] Letter from William Stern, NECA, to William Caton, FCC, dated October 6, 1997 (NECA October 6 *ex parte*).

[481] NECA October 6 *ex parte*.

[482] FCC Form 470 (Schools and Libraries Universal Service Program - Description of Services Requested and Certification Form).

[483] FCC Form 465 (Rural Health Care Providers Universal Service Program - Description of Services Requested and Certification Form).

[484] For example, FCC Form 465 requires rural health care providers to state whether a full RFP is available on the Internet or to provide a contact person that is able to provide a copy of the RFP. FCC Form 470 asks school and library

conclude that this information is adequate to serve the purposes underlying the website posting requirement by allowing schools and libraries to take advantage of the competitive marketplace. We conclude that any additional information contained in an RFP that is not submitted for posting on the website under FCC Forms 470 and 465 can be made available to interested service providers at the election of the school, library, or rural health care provider applicant. We encourage eligible school, library, and rural health care provider applicants to make RFPs available upon request to interested service providers. We do not, however, require the Schools and Libraries Corporation or the Rural Health Care Corporation to post RFPs on the websites, but instead require the administrative companies to post FCC Forms 470 and 465, respectively.

E. State Telecommunications Networks and Wide Area Networks

1. Background

163. Section 254(e) provides that only an "eligible telecommunications carrier" under section 214(e) may receive universal service support.[485] Section 254(h)(1)(B)(ii), however, states that any telecommunications carrier providing services to schools and libraries may receive reimbursement from universal service support mechanisms, notwithstanding the provisions of section 254(e).[486] Consequently, the Commission concluded in the *Order* that Congress intended that any telecommunications carrier, even one that did not qualify as an eligible telecommunications carrier, should be eligible for support for services provided to schools and libraries.[487] The Act defines "telecommunications carrier" as any provider of "telecommunications services. . . ."[488] The Act defines "telecommunications service" as "the offering of telecommunications for a fee directly to the public, or to such classes of users as to be effectively available directly to the public, regardless of the facilities used."[489]

164. In the *Order*, the Commission found that the definition of "telecommunications service," in which the phrase "directly to the public" appears, is intended to encompass only telecommunications provided on a common carrier basis.[490] The Commission further noted that

applicants to provide the website where their RFP is available if their RFP is posted on a website.

[485] 47 U.S.C. § 254(e).

[486] 47 U.S.C. § 254(h)(1)(B)(ii).

[487] *Order*, 12 FCC Rcd at 9015.

[488] 47 U.S.C. § 153(44).

[489] 47 U.S.C. § 153(46).

[490] *Order*, 12 FCC Rcd at 9177-78.

"precedent holds that a carrier may be a common carrier if it holds itself out 'to service indifferently all potential users'"[491] and that "a carrier will not be a common carrier 'where its practice is to make individualized decisions in particular cases whether and on what terms to serve.'"[492]

165. Section 254(h)(2)(A) directs the Commission to "establish competitively neutral rules to enhance, to the extent technically feasible and economically reasonable, access to advanced telecommunications and information services for all public and non-profit elementary and secondary school classrooms, health care providers, and libraries."[493] The Commission concluded that section 254(h)(2)(A), in conjunction with section 4(i),[494] authorizes the Commission to provide discounts and funding mechanisms for advanced services provided by non-telecommunications carriers.[495] The Commission reasoned that providing universal service support to non-telecommunications carriers "empower[s] schools and libraries to take the fullest advantage of competition to select the most cost-effective provider of Internet access and internal connections, in addition to telecommunications services, and allows us not to require schools and libraries to procure these supported services only as a bundled package with telecommunications services."[496]

166. The Commission set forth in the *Order* the criteria that schools and libraries must meet in order to be eligible for discounts on telecommunications and information services.[497] The Commission concluded that schools and libraries not eligible for discounts should not be

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[491] *Order*, 12 FCC Rcd at 9177-78, *citing National Association of Regulatory Utility Commissioners v. FCC*, 553 F.2d 601, 608 (D.C. Cir. 1976) (*NARUC II*).

[492] *Order*, 12 FCC Rcd at 9177-78, *citing NARUC II*, 553 F.2d at 608.

[493] 47 U.S.C. § 254(h)(2)(A).

[494] Section 4(i) provides that "[t]he Commission may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this Act, as may be necessary in the execution of its functions." 47 U.S.C. § 154(i).

[495] *Order*, 12 FCC Rcd at 9085.

[496] *Order*, 12 FCC Rcd 9086-87.

[497] The Commission concluded that a school must meet the statutory definition of an elementary or secondary school found in the Elementary and Secondary Education Act of 1965, must not operate as a for-profit business, and must not have an endowment exceeding $50 million. *See Order*, 12 FCC Rcd at 9068-69. Regarding libraries eligible for universal service support, the Commission adopted the Library Services and Technology Act's definition of library for purposes of section 254(h), but concluded that a library's eligibility for universal service funding will depend on its funding as an independent entity. *See Order*, 12 FCC Rcd at 9069-9072.

permitted to gain eligibility for discounts by participating in consortia with those that are eligible.[498] The Commission encouraged eligible entities, however, to participate in consortia with other eligible schools, libraries, and health care providers and public sector (governmental) entities,[499] because such participation should enable them to secure telecommunications and information services and facilities under more favorable terms and conditions than they could negotiate alone.[500] The Commission concluded that "[t]his approach also includes the large state networks upon which many schools and libraries rely for their telecommunications needs among the entities eligible to participate in consortia."[501] Furthermore, in the rules addressing consortia of schools and libraries, the Commission provided that, "state agencies may receive discounts on the purchase of telecommunications and information services that they make on behalf of and for the direct use of eligible schools and libraries, as through state networks."[502]

167. The Commission recognized, however, that its decision to permit purchasing consortia that include both eligible and ineligible entities creates some tension with section 254(h)(3)'s prohibition on resale.[503] Section 254(h)(3) bars entities that obtain discounts from reselling the discounted services.[504] The Commission interpreted section 254(h)(3) to restrict any resale whatsoever of services purchased pursuant to a section 254 discount to entities that are not eligible for support.[505] Thus, the Commission pointed out, it may be difficult to allow eligible institutions to aggregate their demand with ineligible entities while attempting to guard

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[498] *Order*, 12 FCC Rcd at 9072.

[499] Such governmental entities include, but are not limited to, state colleges and state universities, state educational broadcasters, counties, and municipalities. *See* 47 C.F.R. § 54.501(d).

[500] *Order*, 12 FCC Rcd at 9072-73. The Commission provided that, while consortium participants ineligible for support would pay the lower pre-discount prices negotiated by the consortium, only eligible schools and libraries would receive the added benefit of universal service discounts. *Order*, 12 FCC Rcd at 9073. The Commission concluded that those portions of the bill representing charges for services purchased by or on behalf of and used by an eligible entity would be reduced by the discount percentage to which the school or library using the services was entitled under section 254(h). *Order*, 12 FCC Rcd at 9073.

[501] *Order*, 12 FCC Rcd at 9028.

[502] 47 C.F.R. § 54.501(d)(3).

[503] *Order*, 12 FCC Rcd at 9075.

[504] Section 254(h)(3) states that "[t]elecommunications services and network capacity provided [to schools and libraries at a discount] may not be sold, resold, or otherwise transferred by such user in consideration for money or any other thing of value." 47 U.S.C. § 254(h)(3).

[505] *Order*, 12 FCC Rcd at 9074.

against the illegal resale of discounts to services used by ineligible entities.[506] The Commission noted, however, that "many schools and libraries rely primarily, if not solely, on access to the Internet through networks managed by their states," and that permitting schools and libraries to aggregate with such ineligible public sector institutions could enable the eligible entities to secure lower pre-discount prices.[507] The Commission therefore concluded that, despite the difficulties of allocating costs and preventing abuses, the benefits of permitting schools and libraries to join in consortia with other customers outweigh the danger that such aggregations will lead to significant abuse of the prohibition on resale.[508] The Commission reasoned that: (1) severely limiting consortia would not be in the public interest; (2) illegal resale, whereby eligible schools and libraries use their discounts to reduce the prices paid by ineligible entities, can be substantially deterred by a rule requiring providers to keep and retain careful records of how they have allocated the costs of shared facilities in order to charge eligible schools and libraries the appropriate amounts; and (3) the growing bandwidth requirements of schools and libraries will make it unlikely that other consortia members will be able to rely on using more than their paid share of the use of a facility.[509]

168. The Commission also concluded that schools and libraries should be able to enter into pre-paid, multi-year contracts for services eligible for universal service support.[510] Schools and libraries with multi-year contracts, however, may only apply for discounts on the portion of a long-term contract that is scheduled to be delivered or installed during the funding year for which the school or library is seeking discounts.[511] The Commission observed that "funding in advance for multiple years of recurring charges could enable a wealthy school to guarantee that its full needs over a multi-year period were met, even if other schools and libraries that could not afford to prepay multi-year contracts were faced with reduced percentage discounts if the administrator estimated that the funding cap would be exceeded in a subsequent year."[512]

2. Pleadings

[506] *Order*, 12 FCC Rcd at 9075.

[507] *Order*, 12 FCC Rcd at 9075.

[508] *Order*, 12 FCC Rcd at 9075-76.

[509] *Order*, 12 FCC Rcd at 9075-76.

[510] *Order*, 12 FCC Rcd at 9062.

[511] *Order*, 12 FCC Rcd at 9062.

[512] *Order*, 12 FCC Rcd at 9062.

169. According to the National Association of State Telecommunications Directors (NASTD),[513] most states, through their respective legislatures, have established state telecommunications networks that procure, oversee, and manage telecommunications resources.[514] As several petitioners explain, state telecommunications networks procure a variety of telecommunications services and hardware components from multiple service and equipment vendors and bundle such components into packages available to eligible entities such as schools, libraries, and health care providers.[515] NASTD maintains that state telecommunications networks procure such services pursuant to a system of competitive bidding mandated by state procurement laws.[516] In turn, eligible entities pay state telecommunications networks their proportionate share of costs based on the services each agency, school, or library uses.[517] Several petitioners assert that, by aggregating the demand for services by eligible entities throughout the state, state telecommunications networks can obtain significant volume discounts from the carriers and other vendors with which they contract.[518] Thus, NASTD states, "the volume purchasing power of aggregated government needs lowers the cost per unit of service for all

[513] According to NASTD's petition, NASTD is an organization comprised of state government telecommunications managers who administer the state organizations that provide state government communications facilities. Such organizations "function as aggregators of service volumes for all eligible users, obtaining term and volume discounts based on total requirements." In most cases, NASTD explains, volume discounted services are bundled and provided to customers as a complete turnkey service, and services are procured through the competitive bid process. NASTD petition at 1.

[514] Letter from NASTD to William F. Caton, FCC, dated September 26, 1997 (NASTD *ex parte*). As NASTD points out, although "most states" have telecommunications networks, each state implements its telecommunications network program differently. *See* NASTD *ex parte* at 2.

[515] *See, e.g.,* NASTD *ex parte* at 2-3; Georgia Department of Administrative Services - Information Technology (DOAS-IT) petition at 1, 3. DOAS-IT explains that it competitively procures, provides, and administers telecommunications and information system services (e.g., voice, data, video networks, wireline and wireless services and equipment, radio and microwave systems, and distance learning and telemedicine networks via landline and satellite) that serve a wide array of state and local entities throughout the state. DOAS-IT asserts that such services are provided and operated as "consolidated joint-use systems and a tightly integrated backbone telecommunications network". *Id*. *See also* Letter from Florida DMS to William F. Caton, FCC, dated September 22, 1997 at 1-2 (Florida DMS *ex parte*); Letter from the Commonwealth of Virginia, Office of the Governor (Commonwealth of Virginia), to William F. Caton, FCC, dated October 31, 1997 (Commonwealth of Virginia *ex parte*) at 1-2.

[516] NASTD lists the following services as among those procured by state telecommunications networks: local and long distance voice communications; video transmission; dedicated and shared data networks; Internet access; and premises wiring.

[517] NASTD *ex parte* at 5.

[518] *See, e.g.,* NASTD *ex parte* at 3; DOAS-IT petition at 3; Commonwealth of Virginia *ex parte* at 1-2.

government entities" on the state telecommunications network.[519]

170. The Iowa Communications Network (ICN) explains that it owns and operates, among other things, significant fiber capacity, switches, and high speed data hubs.[520] ICN further maintains that it integrates these facilities with services purchased from telecommunications carriers to provide DS-3 level connections to each school district.

171. DOAS-IT states that the network ultimately provides services to both public entities that are eligible and ineligible for universal service discounts.[521] DOAS-IT asserts, nevertheless, that it is impractical, and perhaps impossible, to separate the costs associated with providing services to entities eligible for universal service discounts from costs associated with providing services to entities that are ineligible for such discounts.[522]

172. The Florida Department of Management Services (DMS) states that, pursuant to state law, the Florida DMS must "develop and maintain the SUNCOM Network as the state communications system for providing local and long distance communications service to state agencies (including universities, community colleges, and libraries), political subdivisions of the state (including counties and school districts), and certain nonprofit corporations (including private universities and health care providers)."[523] According to Florida DMS, the SUNCOM Network transmits a variety of communications signals, including voice, data, video, image, and radio signals.[524] Florida DMS further explains that "ninety-nine percent of the services offered by the SUNCOM Network are leased from the telecommunications industry in Florida," including local and long-distance telephone service, Internet access, dedicated data service, and router transport service.[525] Furthermore, Florida DMS explains that state law requires Florida DMS to provide Florida's residents with better access to education and health services through advanced telecommunications services.

173. Regarding state telecommunications networks' costs associated with providing

[519] NASTD *ex parte* at 3.

[520] ICN petition at 4.

[521] DOAS-IT petition at 2.

[522] DOAS-IT petition at 2.

[523] Florida DMS petition at 1.

[524] Florida DMS petition at 1.

[525] Florida DMS *ex parte* at 1-2.

service to entities eligible for universal service discounts, NASTD maintains that: (1) the cost of services is passed on equitably to the eligible entities based on the cost of providing the services;[526] and (2) states predominantly operate the state telecommunications networks on a cost-recovery basis. In other words, because such networks typically do not receive direct state funding with which to acquire and maintain services, NASTD maintains that they allocate the costs of the aggregated services, along with "a small administrative charge to cover costs of the [state telecommunications networks'] employees, contract administration and other administrative expenses" among the entities eligible for support.[527] DOAS-IT asserts that no profit is included in the rates charged, and that such rates are regularly audited by both state and federal auditors.[528] ICN provides services at cost, and the state of Iowa provides a subsidy for certain of these services.[529] NASTD attributes much of the success of state telecommunications networks to "the centralization of service and billing."[530] The Kansas Department of Administration (DoA) explains that its Division of Information Systems and Communications (DISC) maintains detailed records for inventory and billing that are "sufficient to provide the necessary detail to identify the dollar amounts of individual [universal service] discounts for each eligible entity."[531] The Kansas DoA asks that any additional record keeping requirements imposed on state telecommunications networks remain simple and compatible with its current system.[532]

174. Several petitioners argue that state telecommunications networks should be eligible to receive direct reimbursement from the support mechanisms for services provided at a discount to eligible schools and libraries.[533] In its reply, NASTD states that, "[w]hile for the sake

[526] NASTD *ex parte* at 3. *See also* DOAS-IT petition at 2 (asserting that the cost of providing, operating, and managing the network is recovered fully from its users, as required by the state statutes that govern DOAS-IT and that the cost of service is billed to customers based on rates designed to recover the costs of the underlying carrier's services and other costs associated with providing the network).

[527] NASTD *ex parte* at 4. *See also* Florida DMS *ex parte* at 2 (providing that its rates "include those service and overhead costs incurred in providing services to comply with the statute that requires a system of equitable billing and charges.")

[528] DOAS-IT petition at 2.

[529] ICN petition at 6.

[530] NASTD *ex parte* at 4.

[531] Letter from Kansas DoA, DISC, to William F. Caton, FCC, dated October 14, 1997 (Kansas DoA *ex parte*) at 2.

[532] Kansas DoA *ex parte* at 2.

[533] *See, e.g.*, NASTD petition at 3; NASTD *ex parte* at 5; ICN reply at 2-3; Florida DMS petition at 2; Florida DMS *ex parte* at 4 (stating that "[a]s aggregator for the consortia of eligible facilities in Florida, DMS seeks recognition as

of administrative efficiency, NASTD believes that state networks should at least have the option of paying full price to service providers and being reimbursed directly from the universal service fund themselves, such an arrangement is for administrative convenience only, and does not place the state networks in the role of supported service providers."[534] In its *ex parte* letter, however, NASTD argues that, pursuant to the Commission's interpretation of section 254(h)(2), which permits non-telecommunications carriers to receive universal service support, state telecommunications networks, as providers of packages of service that include advanced telecommunications and information services, should be eligible to receive direct reimbursement from the support mechanisms. NASTD maintains that, based on the Commission's determination in the *Order* that section 254(h)(2) grants it broad authority "to enhance access to advanced telecommunications and information services, constrained only by the concepts of competitive neutrality, technical feasibility, and economic reasonableness,"[535] state telecommunications networks should be eligible for universal service support.[536] NASTD, therefore, asserts that the concepts of competitive neutrality, technical feasibility, and economic reasonableness are "inherent in the [state telecommunications network] structures."[537]

175. NASTD also argues that, based on the Commission's provision in the *Order* that, "to take advantage of the discounts provided by section 254(h)(1), non-telecommunications carriers can bid with telecommunications carriers through joint ventures, partnerships, or other business arrangements,"[538] state telecommunications networks that purchase services should be eligible to receive universal service support.[539] NASTD asserts that, "as representatives of their state governments tasked with the responsibility of aggregating services and equipment for schools, libraries and other state organizations, and because of the state-mandated procurement processes through which they must conduct business with the carriers, [state telecommunications networks] occupy a unique business relationship with such telecommunications providers."[540]

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agent to directly obtain discounts from the [universal service support mechanisms] based on DMS published prices"); Letter from STS of North Carolina to William F. Caton, FCC, dated September 29, 1997 (STS of North Carolina *ex parte*) at 4; Kansas DoA *ex parte* at 2; DOAS-IT petition at 3; Commonwealth of Virginia *ex parte* at 2.

[534] NASTD reply at 1 n.1.

[535] *Order*, 12 FCC Rcd at 9086-86.

[536] NASTD *ex parte* at 9-10.

[537] NASTD *ex parte* at 9-10.

[538] *Order*, 12 FCC Rcd at 9085.

[539] NASTD *ex parte* at 7-8.

[540] NASTD *ex parte* at 8.

176. STS of North Carolina argues that state telecommunications networks should be eligible to receive universal service support, provided such networks: (1) were created as part of a state agency or department pursuant to state statute; (2) are a "cost recovery operation" subject to rate review and oversight by a state authoritative body that is independent of the state telecommunications network; (3) are required by state procurement law to solicit competitive bids for services where competition exists; and (4) provide services only to those eligible entities that choose to receive services from state telecommunications networks (i.e., eligible entities should not be required to receive service from state telecommunications networks).[541]

177. ICN, unlike NASTD and DOAS-IT, argues that ICN is a telecommunications carrier and is therefore eligible for direct reimbursement from the support mechanisms.[542] ICN explains that it "provides services to a wide variety of users, not just schools and libraries" and owns and operates significant fiber capacity, switches, and high-speed data hubs."[543] DOAS-IT, on the other hand, asserts that it should be eligible to receive universal service support without being designated a telecommunications carrier.[544]

178. Several parties, on the other hand, contend that, under section 254(h)(1)(B), state telecommunications networks are ineligible to receive direct reimbursement from the support mechanisms.[545] USTA emphasizes that the Act defines "telecommunications carrier" as any provider of "telecommunications services" and further defines "telecommunications service" as "the offering of telecommunications for a fee directly to the public, or to such classes of users as to be effectively available directly to the public, regardless of the facilities used."[546] USTA and others argue that state telecommunications networks are ineligible for universal service support because they do not offer telecommunications "for a fee directly to the public . . . ."[547]

179. In response to the American Association of Educational Service Agencies' letter to

[541] STS of North Carolina *ex parte* at 6-7.

[542] ICN reply at 2.

[543] ICN reply at 2-3.

[544] DOAS-IT petition at 3.

[545] GTE opposition at 13-14; USTA opposition at 6; Letter from BellSouth, Bell Atlantic, and Ameritech to William F. Caton, FCC, dated October 7, 1997 (BellSouth, Bell Atlantic, Ameritech *ex parte*) at 2.

[546] 47 U.S.C. § 153(46).

[547] *See, e.g.,* USTA opposition at 6; BellSouth, Bell Atlantic, Ameritech *ex parte* at 2.

the Commission asking whether it could treat its member agencies as both schools and providers,[548] GTE argues that permitting state telecommunications networks to receive universal service support would violate the resale provisions of the Act, stating that section 254(h)(3) prohibits services provided at a discount to a user to be "sold, resold, or otherwise transferred by such user in consideration for money or any other thing of value."[549] GTE, therefore, asserts that state telecommunications networks should be ineligible for universal service support, although they could be eligible for discounts as a purchaser of eligible services.[550] Similarly, BellSouth, Bell Atlantic, and Ameritech contend that state telecommunications networks should be able to aggregate schools' and libraries' demand for services and obtain pro-rata discounts for such entities.[551] These parties argue that, operating in this capacity, state telecommunications networks should be considered consortia. BellSouth, Bell Atlantic, and Ameritech also assert that allowing state telecommunications networks to receive direct reimbursement from the support mechanisms "will tend to shield more information from scrutiny, risking the funding of an inappropriate portion of state-wide networks at the hands of the [schools and libraries] fund, jeopardizing the availability of the limited funding for intended purposes."[552]

180. Although it argues that ICN constitutes a telecommunications carrier, ICN contends that ICN and other entities "that exist solely to reduce the costs of telecommunications services to eligible entities such as schools and libraries" should not be required to contribute to the universal service support mechanisms pursuant to section 254(d).[553] ICN maintains that section 254(d) authorizes the Commission to adopt contribution mechanisms that are "'equitable,' a term that gives it considerable discretion to determine what entities are required to contribute to the fund and the nature of those contributions."[554] ICN further argues that the Commission should not require non-profit entities to contribute to the universal service support mechanisms.[555]

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[548] Letter from the American Association of Educational Service Agencies to Chairman Reed E. Hundt, FCC, dated July 16, 1997.

[549] GTE comments at 13.

[550] GTE comments at 13.

[551] BellSouth, Bell Atlantic, Ameritech *ex parte* at 2.

[552] BellSouth, Bell Atlantic, Ameritech *ex parte* at 2.

[553] ICN petition at 7-8. Section 254(d) provides that "[e]very telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis," to the universal service support mechanisms. 47 U.S.C. § 254(d).

[554] ICN petition at 7-8.

[555] ICN petition at 7.

181. In contrast to petitioners that argue that state telecommunications networks should receive direct reimbursement from the support mechanisms, Florida DOE seeks clarification with regard to whether state telecommunications networks will be eligible for discounts on supported services.[556] Florida DOE maintains that, while the Florida Information Resource Network (FIRN) does not meet the definition of "school" or "library," state telecommunications networks such as FIRN should be included in the category of recipients eligible for discounts.[557] Florida DOE explains that FIRN purchases network access and other telecommunications services in order to "provide access to schools and libraries across the state . . . [t]he services are not directly purchased on behalf of the libraries and schools, in the sense of aggregate purchases which are then conveyed to the libraries and schools. . . [h]owever, these services are purchased on behalf of the schools and libraries in the sense that FIRN purchases them and provides electronic access to them."[558] Florida DOE asks whether "services purchased must be conveyed directly to the schools and libraries, or whether the services can be purchased for the benefit of the eligible entities."[559]

3. Discussion

182. We conclude that state telecommunications networks that procure supported telecommunications and make them available to schools and libraries constitute consortia that will be permitted to secure discounts on such telecommunications on behalf of eligible schools and libraries. We further conclude that, with respect to Internet access and internal connections, state telecommunications networks may either secure discounts on such telecommunications on behalf of schools and libraries, or receive direct reimbursement from the universal service support mechanisms, pursuant to section 254(h)(2)(A), for providing such services. Finally, we conclude, on our own motion, that to the extent schools and libraries build and purchase wide area networks to provide telecommunications, such networks will not be eligible for universal service discounts.

a. State telecommunications networks

[556] Specifically, Florida DOE asks whether state telecommunications networks can receive discounts for providing "statewide access and technical support to eligible facilities." Florida DOE petition at 2.

[557] Florida DOE petition at 2-3, 4.

[558] Florida DOE petition at 3.

[559] Florida DOE petition at 3. According to Florida DOE, the Florida Information Resource Network (FIRN) electronically links all of Florida's public education entities to computing resources that serve public education and purchases services and provides an Internet Gateway for the direct use of those services by schools and libraries throughout the state.

1. Procuring telecommunications

183. We conclude that state telecommunications networks that procure supported telecommunications and make them available to eligible schools and libraries constitute consortia that will be permitted to secure discounts on such services on behalf of their eligible members.[560] We recognize the significant benefits that state telecommunications networks provide to schools and libraries in terms of, among other things, purchasing services in bulk and passing on volume discounts to schools and libraries. In order for eligible schools and libraries to receive discounts pursuant to the universal service support mechanisms for schools and libraries and to continue to receive the benefits currently provided by state telecommunications networks, such networks, consistent with the universal service rules,[561] may obtain discounts on telecommunications from the universal service support mechanisms on behalf of eligible schools and libraries and pass on such discounts to the eligible entities. We emphasize that, with respect to telecommunications, state telecommunications networks only will be permitted to pass on discounts for such services to eligible schools and libraries, but will not, as discussed below, be able to receive direct reimbursement from the universal service support mechanisms for providing such services. We conclude that a state telecommunications network itself will not qualify for discounts on telecommunications. Because it does not meet the definition of an eligible school or library as set forth in the *Order*,[562] a state telecommunications network only may secure such discounts on behalf of the schools and libraries it serves and pass through the discounts to those schools and libraries. Because schools and libraries will benefit from both the universal service discounts and the ability of state telecommunications networks to aggregate demand and secure prices based on volume discounts, the approach we adopt here will be advantageous to eligible schools and libraries. Furthermore, this approach will help maintain the

[560] In its discussion encouraging schools and libraries to participate in consortia, the Commission included the "large state networks upon which many schools and libraries rely for their telecommunications needs among the entities eligible to participate in consortia." *Order*, 12 FCC Rcd at 9028. Furthermore, in the rules addressing consortia of schools and libraries, the Commission provided that, "state agencies may receive discounts on the purchase of telecommunications and information services that they make on behalf of and for the direct use of eligible schools and libraries, as through state networks." 47 C.F.R. § 54.501(d)(3).

[561] 47 C.F.R. § 54.505(d).

[562] The Commission concluded that a school must meet the statutory definition of an elementary or secondary school found in the Elementary and Secondary Education Act of 1965, must not operate as a for-profit business, and must not have an endowment exceeding $50 million. *Order*, 12 FCC Rcd at 9068-69. Regarding libraries eligible for universal service support, the Commission adopted the Library Services and Technology Act's definition of library for purposes of section 254(h), but concluded that a library's eligibility for universal service funding will depend on its funding as an independent entity. *Order*, 12 FCC Rcd at 9061-72. Furthermore, the Commission concluded in the *Order* that schools and libraries not explicitly eligible for discounts should not be permitted to gain eligibility for discounts by participating in consortia with those that are eligible. *Order*, 12 FCC Rcd at 9072.

integrity of the universal service support mechanisms, because eligible schools and libraries will be able to secure pre-discount prices for telecommunications that are lower than the prices for such telecommunications if they had not been purchased in bulk.

184. In order to receive and pass through discounts on supported telecommunications for eligible schools and libraries, state telecommunications networks must make a good faith effort to ensure that each eligible school or library receives a proportionate share of shared services.[563] State telecommunications networks must take reasonable steps to ensure that service providers apply appropriate discount amounts on the portion of the supported telecommunications used by each eligible school or library. The service providers will submit to the state telecommunications network a bill that includes the appropriate discounts on eligible telecommunications rendered to eligible entities. The state telecommunications network then will direct the eligible consortium members to pay the discounted prices. Eligible consortium members may pay the discounted prices to their state telecommunications network, which will then remit the discounted amount to the service providers. Service providers will receive direct reimbursement from the support mechanisms in an amount equal to the difference between the pre-discount price of the eligible telecommunications and the discounted amount.[564] We emphasize that state telecommunications networks purchasing services on behalf of schools and libraries are required to comply with the applicable competitive bid requirements established in the *Order*.[565]

185. We note that, even where state telecommunications networks have procured telecommunications on behalf of schools and libraries through competitive bidding or are exempt from the competitive bid requirement, it may be advantageous for schools and libraries themselves to seek competitive bids on their requested services. In so doing, schools and libraries may be better able to ensure that they obtain the best price on the services that are most closely tailored to meet their needs. We have attempted to design the universal mechanisms so that schools, libraries, and rural health care providers utilize, and obtain the advantages of, competition, to the fullest extent possible. The competitive bidding process is a key component of the Commission's effort to ensure that universal service funds support services that satisfy the precise needs of an institution, and that the services are provided at the lowest possible rates. We

[563] We note that this requirement is consistent with our determination in section VI.G, *supra*, regarding services shared among consortium members.

[564] The pre-discount price is the total amount that carriers will receive for the services they sell to schools and libraries: the sum of the discounted price paid by a school or library and the discount amount that the carrier can recover from universal service support mechanisms for providing such services. *Order*, 12 FCC Rcd at 9026-27.

[565] *Order*, 12 FCC Rcd at 9029. We note that services provided pursuant to certain preexisting contracts are exempt from the competitive bid requirement, as set forth in section VI.I.

recognize that schools, libraries, and health care providers may need to transition to the new universal service mechanisms, and we have made reasonable accommodation for eligible entities that have preexisting contracts for telecommunications, internal connections, or access to the Internet.[566] We intend to continue to monitor our decision to exempt certain preexisting contracts from the competitive bidding requirement, to ensure that the exemption does not reduce the benefits that competitive bidding will provide. We thus encourage schools and libraries to seek competitive bids on their requests for services in order to obtain the best price for the desired services. We note that schools and libraries have an incentive to obtain the best price for services, because such schools and libraries will be responsible for paying a portion of the cost. We also note that, after seeking competitive bids, schools and libraries may nevertheless decide to obtain telecommunications that are procured by a state telecommunications network.

186. Because it appears that state telecommunications networks generally make telecommunications available to both eligible and ineligible entities, we emphasize that, pursuant to section 254(h)(4),[567] such networks may obtain and pass through universal service discounts only with respect to schools and libraries that are eligible to receive such discounts. In order to protect the integrity of the schools and libraries program, we direct state telecommunications networks to develop and retain records listing eligible schools and libraries and showing the basis on which the eligibility determinations were made. Such networks also must keep careful records demonstrating the discount amount to which each eligible entity is entitled and the basis on which such a determination was made. Additionally, consistent with the *Order*, service providers must develop and retain detailed records showing how they have allocated the costs of facilities shared by eligible and ineligible entities in order to charge such entities the correct amounts.[568]

187. We disagree with parties that argue that state telecommunications networks should be able to receive direct reimbursement from the support mechanisms for providing schools and libraries with services other than access to the Internet and internal connections.[569] Because they do not meet the definition of "telecommunications carrier," state telecommunications networks are not eligible to receive direct reimbursement from the support

[566] *See* Section VI.I., below.

[567] 47 U.S.C. § 254(h)(4).

[568] *Order*, 12 FCC Rcd at 9075-76.

[569] We clarify that connections between or among multiple instructional buildings that comprise a school campus or multiple non-administrative buildings that comprise a library branch are considered internal connections. For example, connections between three instructional buildings on a single school campus would qualify as internal connections eligible for support under the universal service discount program, whereas connections between instructional buildings located on different campuses would not qualify as internal connections eligible for such support.

mechanisms pursuant to section 254(h)(1)(B). Section 254(h)(1)(B) provides that only telecommunications carriers may receive support for providing schools and libraries with the telecommunications supported under section 254(h)(1)(B). Based on the record before us, we agree with USTA that, because they do not offer telecommunications "for a fee directly to the public, or to such classes of users as to be directly available to the public," state telecommunications networks do not meet the definition of "telecommunications carrier." As the Commission determined in the *Order*, the definition of "telecommunications service" is intended to encompass only telecommunications provided on a common carrier basis.[570] The Commission further noted that " . . . precedent holds that a carrier may be a common carrier if it holds itself out 'to service indifferently all potential users'"[571] and that "a carrier will not be a common carrier 'where its practice is to make individualized decisions in particular cases whether and on what terms to serve.'"[572]

188. We are not persuaded by the record before us that state telecommunications networks offer service "indifferently [to] all potential users." Rather, the evidence indicates that state telecommunications networks offer services to specified classes of entities. Because the record does not contain any credible evidence that a state telecommunications network offers or plans to offer service indifferently to any requesting party, we find that state telecommunications networks do not offer service "directly to the public or to such classes of users as to be directly available to the public" and thus will not be eligible for reimbursement from the support mechanisms pursuant to section 254(h)(1). We further find that prohibiting state telecommunications networks from receiving direct reimbursement from the support mechanisms pursuant to section 254(h)(1) is consistent with the Commission's determination in the *Order* that consortia of schools and libraries may receive discounts on eligible services,[573] but that such consortia will not be permitted to receive direct reimbursement from the support mechanisms.[574]

189. We recognize that it may be more administratively burdensome for state telecommunications networks to obtain and pass through discounts on behalf of schools and

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[570] *Order*, 12 FCC Rcd at 9177-78.

[571] *Order*, 12 FCC Rcd at 9177-78, *citing National Association of Regulatory Utility Commissioners v. FCC*, 553 F.2d 601, 608 (D.C. Cir. 1976) (*NARUC II*).

[572] *Order*, 12 FCC Rcd at 9177-78, *citing NARUC II*, 553 F.2d at 608.

[573] *Order*, 12 FCC Rcd at 9028, 9072.

[574] The *Order* provides that only telecommunications carriers, and non-telecommunications carriers that provide access to advanced services, may receive direct reimbursement from the support mechanisms. *Order*, 12 FCC Rcd at 9005-23, 9084-90; 47 C.F.R. §§ 54.501(a), 54.517.

libraries, rather than to receive direct reimbursement from the support mechanisms for procuring telecommunications and making such telecommunications available to schools and libraries.[575] As discussed above, however, state telecommunications networks do not meet the definition of "telecommunications carrier" and thus will not be permitted to receive direct reimbursement for the provision of telecommunications. Additionally, parties have not suggested any reason why state telecommunications networks should be treated differently from other consortia and thus be allowed to receive support directly from the universal service support mechanisms for providing telecommunications other than Internet access and internal connections. Furthermore, even if they were able to receive direct reimbursement from the support mechanisms for providing telecommunications, state telecommunications networks would still need to determine which entities are eligible for discounts and the discount rate to which each eligible entity is entitled. Therefore, any additional administrative burden created by requiring state telecommunications networks to pass through the discount amounts, rather than allowing them to receive direct reimbursement from the support mechanisms, may not be as significant as some parties suggest.

2. Internet access and internal connections

190. With respect to Internet access and internal connections, we conclude that state telecommunications networks may either secure discounts on the purchase of such telecommunications purchased from other providers on behalf of schools and libraries in the manner discussed above with regard to telecommunications, or receive direct reimbursement from the support mechanisms for providing Internet access and internal connections to schools and libraries, pursuant to section 254(h)(2)(A). As the Commission concluded in the *Order*, section 254(h)(2)(A), in conjunction with section 4(i),[576] authorizes the Commission to permit discounts and funding mechanisms to enhance access to advanced services provided by non-telecommunications carriers.[577] On this basis, the Commission stated that it would permit discounts for Internet access and internal connections provided by non-telecommunications carriers.[578] Thus, although we conclude that state telecommunications networks do not constitute telecommunications carriers that are eligible for reimbursement for making available telecommunications pursuant to section 254(h)(1)(B), we do find that networks that make Internet access and internal connections available to schools and libraries are eligible, under the

[575] For example, state telecommunications networks will be required to separate the costs associated with providing service to eligible and ineligible entities, pass through the discount to the eligible entities, and submit to USAC and the Schools and Libraries Corporation copies of a form designating the services made available to the eligible school or library and the support amount due to the service provider.

[576] 47 U.S.C. § 154(i).

[577] *Order*, 12 FCC Rcd at 9085.

[578] *Order*, 12 FCC Rcd at 9084-85.

Order and section 54.517 of our rules, as non-telecommunications carriers for direct reimbursement from the support mechanisms for providing these services.

191. NASTD suggests that the Commission's statement in the *Order* that it was "constrained only by the concepts of competitive neutrality, technical feasibility, and economic reasonableness" in implementing section 254(h)(2)(A) means that state telecommunications networks should be eligible for reimbursement from the support mechanisms for providing "bundled service packages" that include telecommunications and access to the Internet and internal connections. As explained above, however, the Act defines "telecommunications carrier" as any provider of "telecommunications service" and does not equate "telecommunications" (the term used in section 254(h)(2)(A)) with "telecommunications service." Therefore, because state telecommunications networks do not provide "telecommunications service," they do not meet the definition of "telecommunications carrier" and will not be permitted to receive direct reimbursement for the provision of services other than Internet access and internal connections. To the extent that they make available Internet access and internal connections, state telecommunications networks are non-telecommunications carriers. As non-telecommunications carriers, they are eligible, as we determined in the *Order*, pursuant to section 254(h)(2)(A), for direct reimbursement from the support mechanisms when they make available to eligible entities Internet access and internal connections.

192. Finally, we emphasize that, consistent with the *Order,* eligible schools and libraries will be required to seek competitive bids for all services eligible for section 254(h) discounts, including those services that state telecommunications networks provide using their own facilities.[579] Thus, schools and libraries in Iowa may not obtain support from the universal service support mechanisms if they select ICN as their provider of access to the Internet and internal connections without first seeking competitive bids. Schools and libraries are not required to select the lowest bids offered, although the Commission stated that price should be the "primary factor."[580] If eligible schools and libraries in Iowa choose ICN as their provider of access to the Internet and internal connections, we conclude that ICN may receive reimbursement from the support mechanisms for providing such services.

b. Wide area networks

[579] *Order*, 12 FCC Rcd at 9029.

[580] Schools and libraries are permitted to take into account service quality and the offering or offerings that meet their needs most effectively and efficiently. The Commission included the following factors as among those that schools and libraries may consider in selecting a service provider: prior experience, including past performance, personnel qualifications, including technical excellence, and management capability. *Order*, 12 FCC Rcd 9029-30. *See also* section VI.A. for a discussion of the lowest corresponding price that providers must offer to an eligible school or library.

193. On our own motion, we further conclude that, to the extent that states, schools, or libraries build and purchase wide area networks to provide telecommunications, the cost of purchasing such networks will not be eligible for universal service discounts. We reach this conclusion because, from a legal perspective, wide area networks purchased by schools and libraries and designed to provide telecommunications do not meet the definition of services eligible for support under the universal service discount program. First, the building and purchasing of a wide area network is not a telecommunications service because the building and purchasing of equipment and facilities do not meet the statutory definition of "telecommunications."[581] Moreover, as the Commission determined in the *Order*, the definition of "telecommunications service" is intended to encompass only telecommunications provided on a common carrier basis.[582] Second, wide area networks are not internal connections because they do not provide connections within a school or library.[583] We herein establish a rebuttable presumption that a connection does not constitute an internal connection if it crosses a public right-of-way.[584] Third, wide area networks built and purchased by schools and libraries do not appear to fall within the narrow provision that allows support for access to the Internet because wide area networks provide broad-based telecommunications.[585] For these reasons, therefore, we conclude that the purchase of wide area networks to provide telecommunications services will not be eligible for universal service discounts.

F. State Support

1. Background

194. In the *Order*, the Commission determined that eligible schools and libraries may receive discounts of between 20 percent and 90 percent on the cost of all telecommunications

[581] 47 U.S.C. § 151(43) ("the term `telecommunications' means the transmission, between or among points specified by the user, of information of the user's choosing, without change in the form or content of the information as sent and received").

[582] *Order*, 12 FCC Rcd at 9177-78.

[583] It should be noted, however, that connections between multiple instructional buildings that comprise a single school or library would not be considered part of a wide area network, but would instead be considered internal connections. For example, connections between multiple instructional buildings on a single school campus would constitute internal connections. Connections between multiple separate schools, however, would not constitute internal connections and would instead be considered part of a wide area network. *See infra* section VI.H for a further discussion of the definition of internal connections.

[584] *See, e.g.*, 47 C.F.R. § 68.3 (definition of demarcation point).

[585] This does not preclude schools and libraries from receiving universal service discounts on a wide area network run over leased telephone lines because such an arrangement constitutes a telecommunications service.

services, Internet access, and internal connections.[586] Service providers will receive universal service support based on the pre-discount price of the services they sell to schools and libraries. The Commission defined the pre-discount price as the price of services to schools and libraries prior to the application of a discount.[587] Certain states currently subsidize telecommunications services received by schools and libraries located within their jurisdiction. The *Order* did not address whether discounts under the federal universal service support mechanisms should be applied prior to the application of such state support or, alternatively, on the cost of service calculated after the application of any state support.

2. Pleadings

195. Iowa Telecommunications and Technology Commission asks the Commission to conclude that the provision of discounted telecommunications services to schools and libraries pursuant to a state subsidy program will not reduce the federal universal service support available to eligible entities.[588] Iowa Telecommunications and Technology Commission contends that federal support should be based upon the full cost of a service, rather than on the post-support cost calculated after the deduction of any state support.[589] It contends that, absent such confirmation by the Commission, states will be reluctant to adopt their own support programs that would further reduce costs to eligible entities.[590] Iowa Telecommunications and Technology Commission also contends that states that have existing subsidy programs may be able to redirect some of their funding to costs that the federal program does not support, such as computers, modems and software, if federal universal service discounts are applied before the deduction of any state subsidy.[591] In its opposition to the Iowa Telecommunications and Technology Commission petition, USTA contends that this request "would appear to suggest that all telecommunications providers subsidize Iowa's state-wide network."[592]

3. Discussion

[586] *Order*, 12 FCC Rcd at 9002.

[587] *Order*, 12 FCC Rcd at 9026-9027.

[588] Iowa Telecommunications and Technology Commission petition at 6.

[589] Iowa Telecommunications and Technology Commission petition at 6.

[590] Iowa Telecommunications and Technology Commission petition at 6.

[591] Iowa Telecommunications and Technology Commission petition at 6.

[592] USTA opposition at 6-7.

196. We conclude that, for services provided to eligible schools and libraries, federal universal service discounts should be based on the price of the service to regular commercial customers or, if lower than the price of the service to regular commercial customers, the competitively bid price offered by the service provider to the school or library that is purchasing eligible services, prior to the application of any state-provided support for schools or libraries. To find otherwise would penalize states that have implemented support programs for schools and libraries by reducing the level of federal support that those schools and libraries would receive. We anticipate that our conclusion will encourage states to implement or expand their own universal service support programs for schools and libraries.

197. Our determination to calculate discounts on the price of a service to eligible schools and libraries prior to the reduction of any state support will not require an adjustment in the $2.25 billion in annual support that the Commission estimated was necessary to fulfill the statutory obligation to create sufficient universal service support mechanisms for schools and libraries.[593] In estimating the level of universal service support needed to serve schools and libraries, the Commission purposefully did not take into consideration state universal service support to schools and libraries.[594] Thus, our determination to calculate federal universal service support levels on the price of service to schools and libraries prior to the application of any state-provided support should not threaten the sufficiency of the federal support mechanisms for schools and libraries.

198. Finally, we do not agree with USTA that allowing federal support levels to be based upon the price of service to schools and libraries prior to the application of any state-provided support for schools or libraries will force all telecommunications carriers to subsidize state-wide networks. Pursuant to section 254(h), universal service support for schools, libraries, and rural health care providers can be provided only to designated educational and health care providers.[595] Moreover, USTA has not explained why applying the federal discount rate before applying any state discounts would reduce the overall amount that a carrier will receive for providing a supported service.

G. Aggregate Discount Rates

1. Background

199. In the *Order*, the Commission adopted discounts from 20 percent to 90 percent for

[593] *Order*, 12 FCC Rcd at 9054.

[594] *Order*, 12 FCC Rcd at 9054-9056.

[595] 47 U.S.C. § 254(h).

all telecommunications services, Internet access, and internal connections, with the range of discounts correlated to indicators of economic disadvantage and high prices for schools and libraries.[596] The Commission also adopted a step function to define the level of discount available to schools and libraries based on the level of poverty in the areas they serve.[597]

200. The Commission encouraged schools and libraries to aggregate their demand with others to create a consortium with sufficient demand to attract competitors and thereby negotiate lower prices.[598] The Commission determined that schools and libraries should keep and retain careful records of how they have allocated costs of shared facilities in order to determine support to eligible schools and libraries in the appropriate amounts.[599] The Commission also determined that service providers shall keep and retain records of rates charged to and discounts allowed for eligible schools and libraries individually or as part of a consortium.[600] The Commission's rules provide that consortia applying for discounted services on behalf of their members shall calculate the portion of the total bill eligible for a discount using a weighted average based on the share of the pre-discount price for which each eligible school or library agrees to be financially liable.[601] Each eligible school, school district, library, or library consortia "will be credited with the discount to which it is entitled."[602] The Commission established that, for eligible schools ordering telecommunications and other supported services at the school district or state level, the individual schools with the highest percentages of economically disadvantaged students should continue to receive the higher discount for which they are eligible.[603] The Commission concluded that the school district or state may compute the discounts on an individual school basis or it may compute an average discount; in either case, "the state or the district shall strive to ensure that each school receives the full benefit of the discount to which it is entitled."[604] For

[596] *Order*, 12 FCC Rcd at 9035.

[597] *Order*, 12 FCC Rcd at 9049.

[598] *Order*, 12 FCC Rcd at 9027.

[599] *Order*, 12 FCC Rcd at 9076.

[600] 47 C.F.R. § 54.501(d)(4).

[601] 47 C.F.R. § 54.505(d).

[602] 47 C.F.R. § 54.505(d).

[603] *Order*, 12 FCC Rcd at 9051.

[604] *Order*, 12 FCC Rcd at 9051. For example, a school district would divide the total number of students in the district eligible for the national school lunch program by the total number of students in the district to compute the district-wide percentage of eligible students. Alternatively, the district could apply on behalf of individual schools and use the respective percentage discounts for which the individual schools are eligible. *See* 47 C.F.R. § 54.505(b)(1).

libraries ordering telecommunications and other supported services at the library system level, the Commission concluded that library systems should be able to compute discounts on either an individual branch basis or based on an average of all branches within the system.[605]

2. Pleadings

201. The Working Group recommends that the Commission clarify the methodology for determining the applicable discount rate for schools and libraries to ensure that the goal of targeting poor and rural schools for higher discounts is achieved in a minimally burdensome manner, and that the same methodology and process apply both to "higher-level governance units for schools and libraries and to consortia."[606] The Working Group contends that the choice of methodology to determine the discount rate for schools and libraries that participate in a consortium should depend on the extent to which usage of the services can be allocated to individual schools and libraries.[607] The Working Group asserts that, when a single application is filed for a contract covering multiple schools and libraries that will pay their own bills directly, there should be no need to calculate an aggregate discount rate. In this situation, the applicable individual discount rate should apply to each bill.[608] The Working Group further recommends that the appropriate methodology for the calculation of discount rates for contracts involving central billing for services provided to multiple schools or libraries is "to average the individual discount rates for those users weighted by the projected allocation of directly allocable services and the projected distribution of nonallocable common or shared services."[609] The Working Group recommends that the applicant rather than the Schools and Libraries Corporation be required to calculate the discount rate for the contract.[610] The Working Group also suggests that the Schools and Libraries Corporation create a list of individual discount rates for every school and library for which the necessary data are publicly available and post that list on the school and

[605] *Order*, 12 FCC Rcd at 9051-9052. Library systems applying for discounted services on behalf of their individual branches shall calculate the system-wide percentage of eligible families using an unweighted average based on the percentage of the student enrollment that is eligible for a free or reduced price lunch under the national school lunch program in the public school district in which they are located for each of their branches or facilities. *See* 47 C.F.R. § 54.505(b)(2).

[606] Working Group Report at 14. *See supra* section VI.C.2 for a discussion of the composition of the Working Group.

[607] Working Group Report at 14.

[608] Working Group Report at 14-15.

[609] Working Group Report at 15-16.

[610] Working Group Report at 18.

library website.[611]

202. The Working Group recommends that the Commission require applicants to adhere to the following principles in calculating weighted averages for applications involving multiple schools or libraries:

1) For those services that can be directly attributed to an individual school or library, the discount level for that school or library must be directly applied to that service.

2) For those services that are "shared" or "common" to multiple schools or libraries, the applicant will need to determine a rational cost-allocation method. In determining such a method, the applicant should have flexibility in determining the appropriate methodology for projecting allocation of eligible services that cannot be disaggregated and directly allocated. For example, such methods may include a calculation of the number of networked computers in each school or library divided by the total number of networked computers in the school district or library system.

3) The "work papers" that an applicant used to calculate a discount level should be maintained and available for auditing and inspection by the public. These records should contain not only the applicant's actual calculations, but also a short explanation of the rationale for calculating the aggregate discount rate, including how the applicant assures that each school or library receives the full benefit of the discount.

4) The applicant must certify that the discount rate has been calculated according to the principles outlined above.[612]

203. In response to a Public Notice seeking comment on this issue,[613] several commenters support the Working Group proposal as a viable method of ensuring that schools and libraries that participate in consortia receive the full benefit of the discounts to which they are entitled.[614] Others disagree with the Working Group's view of how school districts and

[611] Working Group Report at 18.

[612] Working Group Report at 16-17.

[613] Common Carrier Bureau Seeks Comment on Universal Service Support Distribution Options for Schools, Libraries, and Rural Health Care Providers, *Public Notice*, CC Docket No. 96-45, DA 97-1957 (rel. Sept. 10, 1997) (*Sept. 10 Public Notice*).

[614] *See, e.g.*, CNMI *Sept. 10 Public Notice* comments at 3; Florida DMS *Sept. 10 Public Notice* comments at 2-3;

library districts bill for and purchase telecommunications services. The Colorado DOE and NY Public Library contend that the assumption that each school or library is treated as an independent entity within the system is not always correct.[615] Mississippi Council for Education Technology argues that the Working Group proposal is too complicated to be practical.[616] It contends that, although some individual entities may not receive the higher discount rate to which they would be entitled if they filed individually, it is the entities' decision to file in an aggregate application.[617]

204. USTA observes that the Commission's rules do not address how discounts for rural schools will be treated if there is a mix of rural and urban schools in a consortium.[618] USTA also points out that there are no rules for multiple districts and for combining schools and libraries into a single consortium.[619] USTA contends that the Working Group proposal overly complicates the requirements of the Administrator and the billing requirements of the service provider.[620] USTA argues that the Working Group seems to confuse the rules for determining aggregated discount rates and the rules for allocating bills from its member participants.[621] USTA states that the Commission has determined that the rules for determining discounts will be based on two factors, poverty and geography, and that the Commission should not specifically define how schools' and libraries' governance authorities should allocate the bill among its member participants.[622] USTA contends that the Working Group proposal is dependent on data that are not commonly known by the Administrator and are subject to frequent changes.[623] EdLiNC contends that the Commission should not attempt to impose a required methodology for dividing costs among members of consortia.[624] EdLiNC argues that the imposition of a required

Great City Schools Council *Sept. 10 Public Notice* comments at 3.

[615] Colorado DOE *Sept. 10 Public Notice* comments at 5; NY Pub. Library *Sept. 10 Public Notice* comments at 1.

[616] Mississippi Council for Ed. Tech. *Sept. 10 Public Notice* comments at 5-6.

[617] Mississippi Council for Ed. Tech. *Sept. 10 Public Notice* comments at 6.

[618] USTA *Sept. 10 Public Notice* comments at 5.

[619] USTA *Sept. 10 Public Notice* comments at 5.

[620] USTA *Sept. 10 Public Notice* comments at 11.

[621] USTA *Sept. 10 Public Notice* comments at 7.

[622] USTA *Sept. 10 Public Notice* comments at 7.

[623] USTA *Sept. 10 Public Notice* comments at 12.

[624] EdLiNC *Sept. 10 Public Notice* comments at 4-5.

cost allocation methodology would encourage school districts and library systems to apply on an individual basis and increase the administrative burden.[625] It contends that, in many cases, consortia have already determined how they will divide the cost of service among their participants, and the participants have agreed that the method chosen is fair and equitable.[626]

3. Discussion

205. Our current rules require consortia to calculate the discount level by using a weighted average that is based on the share of the pre-discount price for which each school or library agrees to be "financially liable."[627] Our rules also provide that each "eligible school, *school district*, library, or *library consortium* will be credited with the discount to which it is entitled."[628] We hereby adopt a modified version of the Working Group's proposal regarding the application of discounts for schools and libraries that apply through consortia, including school districts, rather than on an individual basis. Because the discount is determined based on the weighted average of the amount for which each individual school or library agrees to be financially liable, we conclude that the amount of support likewise should be determined, where possible, on the discount rate to which each individual school or library is entitled. In other words, both the discount rate and the provision of support should be determined for each individual school or library if it is not unreasonably burdensome to do so. We therefore agree with the Working Group that, for services that will be used only by an individual institution, the applicable discount rate for the services should be determined based on the applicable discount rate for the individual school or library, not the consortium. Thus, for example, if a school applies for support as part of a consortium, but seeks support for internal connections that it alone will use, the amount of support for that internal connection should be calculated based on the specific discount rate applicable for that school. We find that this decision is consistent with our earlier decision that the level of support should be based on the economic level and geographic location of the institution seeking support.

206. We recognize, however, that we must balance the desire for equitable distribution of support against the need to keep the application process as simple and efficient as possible. Thus, while we require the state, school district, or library system to "strive to ensure" that each school and library in a consortium receives the full benefit of the discount on shared services to which it is entitled, we will not require school districts or library systems to compute their

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[625] EdLiNC *Sept. 10 Public Notice* comments at 4-5.

[626] EdLiNC *Sept. 10 Public Notice* comments at 4-5.

[627] *See* 47 C.F.R. § 54.505(d).

[628] 47 C.F.R. § 54.505(d) (emphasis added).

discount rate for shared services based on estimates of the actual usage that each of their schools or library branches will make and the respective discounts that these individual units are entitled to receive.[629] Shared services are those that cannot, without substantial difficulty, be identified with particular users or be allocated directly to particular entities. We conclude that the administrative burden of such a requirement would not be justified by the benefit in light of existing rules in this area. We recognize that states already prohibit unreasonable discrimination against disadvantaged schools in the state, and that the courts have upheld such rules of equity, even against the state itself.[630] Although we do not mandate consortia to adopt a particular methodology for distributing shared services, we seek to ensure that economically disadvantaged institutions receive the discounts to which they are entitled. Accordingly, we require that consortia certify that each individual institution listed as a member of a consortium and included in determining the discount rate will receive a proportionate share of the shared services within each year in which the institution is used to calculate the aggregate discount rate.[631] Consortia may, for example, satisfy this obligation by keeping track of the usage level of shared services with respect to each institution that was included in calculating the discount rate, or they may adopt other methods to ensure that each institution receives a proportionate share of shared services. This requirement is appropriate because the discount rate for calculating support for shared services will be based on all entities listed in the request for services. By the same token, this requirement is not unduly burdensome because it does not require applicants to develop complex weighting methodologies or to calculate different discount rates for different entities that use shared services. Our determination that the state or district must "strive to ensure" that each school or library receives the full benefit of the discount to which it is entitled will help ensure that this goal is met.[632] Moreover, the Schools and Libraries Corporation, pursuant to its obligation to review and approve schools' and libraries' applications and service providers' bills,[633] is developing cost allocation procedures to further ensure that schools and libraries

[629] *Order*, 12 FCC Rcd at 9051.

[630] *Abbott v. Burke*, 693 A.2d 471 (N.J. 1997) (holding that the state must provide money to low income districts allowing them to spend at the same level per pupil as higher income districts); *Edgewood Independent School District v. Kirby*, 777 S.W.2d 391 (Tex. 1989) (holding that the school financing system, based in part upon local property taxes, violated state constitutional provision requiring maintenance of an "efficient" system).

[631] FCC Form 471 (Schools and Libraries Universal Service - Services Ordered and Certification Form), one of the forms that schools and libraries must submit in order to receive universal service discounts, requires that applicants certify "that the discount level used for shared services is conditional, in future years, upon ensuring that the most disadvantaged schools and libraries that are treated as sharing in the service receive an appropriate share of benefits from those services." *See* FCC Form 471, Item 27.

[632] *Order*, 12 FCC Rcd at 9051-9052.

[633] *See NECA Report and Order* at para. 65; 47 C.F.R. § 69.619(a)(4).

receive the discounts to which they are entitled.[634]

207. Finally, we agree with the Working Group that an applicant that is comprised of multiple eligible schools and libraries must keep adequate records showing how the distribution of funds was made, and the basis for distribution. Our rules currently require such records.[635]

H. Limiting Internal Connections to Instructional Buildings

1. Background

208. In the *Order*, the Commission determined that eligible schools and libraries may, under sections 254(c)(3) and 254(h)(1), secure support for the installation and maintenance of internal connections.[636] Consistent with section 254(h)(1)(B)'s requirement that services requested by schools and libraries must be used for educational purposes, the Commission found that a given service is eligible for support as a component of the institution's internal connections only if it is necessary to "transport information all the way to individual classrooms."[637]

2. Discussion

209. We take this opportunity to make clear, on our own motion, that the *Order* limits support for internal connections to those essential to providing connections within instructional buildings. Thus, discounts are not available for internal connections in non-instructional buildings of a school district or administrative buildings of a library unless those internal connections are essential for the effective transport of information to an instructional building or library. Hence, discounts would be available for routers and hubs in a school district office if individual schools in the school district were connected to the Internet through the district office. The *Order* stated that "a given service is eligible for support as a component of the institution's internal connections only if it is necessary to transport information all the way to individual classrooms."[638] This focus on access to classrooms followed from the Commission's conclusion

[634] Letter from Debra M. Kriete, Schools and Libraries Corporation, to Magalie Roman Salas, FCC, dated December 22, 1997. In addition, billed entities completing FCC Form 471 (Schools and Libraries Universal Service - Services Ordered and Certification Form) are required to provide a list of each school and library for which universal service discounts are being sought and each entity's individual discount rate. *See* FCC Form 471, item 14.

[635] 47 C.F.R. § 54.516. *See also* 47 C.F.R. § 54.501(d)(4) (requiring service providers to maintain records of rates charged to and discounts allowed by consortia members).

[636] *Order*, 12 FCC Rcd at 9015-9016.

[637] *Order*, 12 FCC Rcd at 9021.

[638] *Order*, 12 FCC Rcd at 9021.

that "Congress intended that telecommunications and other services be provided directly to classrooms."[639] The Commission reached this conclusion based on its analysis of the statute (where classrooms are explicitly mentioned)[640] and of the legislative history (where Congress explicitly refers repeatedly to classrooms).[641] Similarly, to the extent that a library system has separate administrative buildings, support is not available for internal connections in those buildings. Sections 254(h)(1)(B) and (h)(2) provide for universal service support for "libraries."[642] Imposing this restriction on support to non-administrative library facilities is consistent with the approach to support for internal connections to instructional school buildings discussed above.

210. Consistent with this clarification, we modify our rules to reflect that support is not available for internal connections in non-instructional buildings used by a school district unless those internal connections are essential for the effective transport of information within instructional buildings or buildings used by a library for strictly administrative functions. Thus, discounts would be available for the internal connections installed in a school district office if that office were used as the hub of a local area network (LAN) and all schools in the district connect to the Internet through the internal connections in that office. We further hold that "internal connections" include connections between or among multiple instructional buildings that comprise a single school campus or multiple non-administrative buildings that comprise a single library branch, but do not include connections that extend beyond that single school campus or library branch. Thus, for example, connections between two instructional buildings on a single school campus would constitute internal connections eligible for universal service support, whereas connections between instructional buildings located on different campuses would not constitute internal connections eligible for such support.

I. Existing Contracts

1. Background

211. In the *Order*, the Commission concluded that eligible schools and libraries must solicit competitive bids for all services eligible for section 254(h) discounts.[643] The Commission

[639] *Order*, 12 FCC Rcd at 9015-9016.

[640] *Order*, 12 FCC Rcd at 9017, *citing* 47 U.S.C. § 254(h)(2)(A).

[641] *Order*, 12 FCC Rcd at 9018, *citing* Joint Explanatory Statement at 132-133.

[642] 47 U.S.C. §§ 254(h)(1)(B) and (h)(2).

[643] *Order*, 12 FCC Rcd at 9028-9029.

required a school or library to submit an application to the Administrator that includes a description of the services that a school or library seeks and also required the Administrator to post this information on a website.[644] These descriptions are to be available for all potential service providers to review, thus facilitating schools' and libraries' ability to benefit from the opportunity to seek competitive bids for the covered services.[645]

212. In the *Order*, the Commission held that schools and libraries could obtain section 254(h) discounts without complying with the competitive bid requirement if the school or library had signed a contract before November 8, 1996, the date of the Recommended Decision.[646] In so holding, the Commission adopted the Joint Board's recommendation that the Commission not require schools or libraries to renegotiate existing contracts in order to benefit from federal universal service support.[647] The Commission concluded that this exemption from the competitive bid requirement was necessary to ensure that eligible schools and libraries that signed contracts prior to November 8, 1996, could obtain affordable access to the services supported by federal universal service support mechanisms.[648] The Commission determined that it would not be in the public interest to penalize schools and libraries that had already entered into contracts for service by refusing to allow them to apply discounts to their existing contract rate.[649] The Commission concluded that schools and libraries had sufficient incentive to negotiate for low rates when they were paying the full undiscounted contract price.[650] The Commission did not, however, authorize schools and libraries to obtain discounts on contracts signed on or after November 8, 1996.

213. In the *July 10 Order*, the Commission concluded that it would provide a limited extension of the competitive bid exemption in order to accommodate schools and libraries that negotiate and sign contracts prior to the date that the competitive bid system becomes "fully

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644 *Order*, 12 FCC Rcd at 9078-9079. We note that, in the *NECA Report and Order* setting forth the structures of the three corporations that the Commission charged with administering the new universal service support mechanisms, the Commission assigned to the Schools and Libraries Corporation responsibility for posting to a website schools' and libraries' application information. *See NECA Report and Order* at para. 11.

645 *Order*, 12 FCC Rcd at 9028-9029, 9078-9080.

646 *Order*, 12 FCC Rcd at 9062-9063.

647 *Order*, 12 FCC Rcd at 9062-9063.

648 *Order*, 12 FCC Rcd at 9063.

649 *Order*, 12 FCC Rcd at 9064.

650 *Order*, 12 FCC Rcd at 9064.

operational."[651] The Commission defined the competitive bid system as fully operational when: 1) the Universal Service Administrator is ready to accept and post requests for service from schools and libraries on a website; and 2) that website may be used by potential service providers.[652] The Commission concluded that any contract signed on or after November 8, 1996 and prior to the date that the competitive bid system becomes operational will be considered an "existing contract" and, therefore, exempt from the competitive bid requirement if the contract terminates by December 31, 1998.[653] The Commission concluded that extending the exemption from the competitive bid requirement was necessary to avoid penalizing schools or libraries that elect or are compelled to negotiate contracts prior to the date that the universal service competitive bid system is operational.[654] The Commission also found that limiting the duration of this exemption would prevent schools, libraries, and service providers from avoiding the competitive bid requirement altogether by signing contracts for extended periods.[655] The Commission did not address issues pertaining to existing contracts for services furnished to rural health care providers in either the *Order* or the *July 10 Order*.

2. Pleadings

214. Several petitioners contend that the Commission should reconsider its decision to limit the exemption to the competitive bid requirement to contracts that terminate no later than December 31, 1998.[656] EdLiNC contends that the Commission's *July 10 Order* will disadvantage many schools and libraries by nullifying eligibility for discounts on services obtained through multi-year contracts signed on or after November 8, 1996.[657] It contends that many schools and libraries have exercised good faith business decisions since November 8, 1996 in procuring services for educational purposes and had no reason to believe from the Joint Board's recommendation that such business decisions would result in discount penalties.[658] EdLiNC also

[651] *July 10 Order*, 12 FCC Rcd at 10,097-10,098.

[652] *July 10 Order*, 12 FCC Rcd at 10,099.

[653] *July 10 Order*, 12 FCC Rcd at 10,098.

[654] *July 10 Order*, 12 FCC Rcd at 10,098.

[655] *July 10 Order*, 12 FCC Rcd at 10,098-10,099.

[656] *See, e.g.*, Bell Atlantic comments to *July 10 Order* at 1-2; Colorado DOE comments to *July 10 Order* at 1, 3; EdLiNC petition to *July 10 Order* at 1; USTA comments to *July 10 Order* at 1-2.

[657] EdLiNC petition to *July 10 Order* at 1.

[658] EdLiNC petition to *July 10 Order* at 2.

contends that the Joint Board's rationale that strong incentives exist for schools and libraries to obtain the lowest possible pre-discount price continued after November 8, 1996 and that most schools and libraries that entered into contracts after November 8, 1996 are unaware that they may not be eligible for discounts on services received after December 31, 1998.[659] EdLiNC recommends that discounts be available for all contracts that were entered into after November 8, 1996 but before the date on which the school and library website becomes fully operational, even if the termination dates of such contracts occur after December 31, 1998.[660]

215. Bell Atlantic contends that the Commission should encourage longer-term contracts in order to give schools and libraries greater savings and access to services that meet their particular needs.[661] It argues that carriers generally offer lower prices for longer-term service commitments. Bell Atlantic also asserts that carriers are willing to finance projects involving special construction and other customized activity over the term of a multi-year contract, "thus saving the schools and libraries from the need to fund the up-front costs."[662] Colorado DOE urges the Commission to adopt a five-year limit based on its view that a five-year extension "will accommodate the development plans of telecommunications vendors in reaching areas where competition is needed to reduce prices and increase access."[663] Colorado DOE also suggests that a five-year limitation represents the "maximum amount of time that is prudent for any technology-related contract, due to substantial and rapid changes in the marketplace."[664] Newport News requests that the existing contract rule be modified to permit universal service discounts for contracts that extend beyond December 31, 1998.[665] Newport News cites its intention to contract for services for a two year period to implement its "Techplan."[666] Newport News contends that it is not practical or financially advantageous to separate the work into phases to comply with the December 31, 1998 limitation.[667]

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[659] EdLiNC petition to *July 10 Order* at 4.

[660] EdLiNC petition to *July 10 Order* at 8-9.

[661] Bell Atlantic comments to *July 10 Order* at 2.

[662] Bell Atlantic comments to *July 10 Order* at 2.

[663] Colorado DOE comments to *July 10 Order* at 3.

[664] Colorado DOE comments to *July 10 Order* at 3.

[665] Newport News petition to *July 10 Order* at 1-2.

[666] Newport News petition to *July 10 Order* at 1-2.

[667] Newport News petition to *July 10 Order* at 2.

216. AHA, which represents 5,000 hospitals and health systems, states in an *ex parte* letter that many health care institutions have negotiated contracts for the provision of telecommunications services that will remain in effect upon commencement of the new universal service support mechanisms.[668] AHA argues that these institutions, many of which are small, rural hospitals with little administrative capability to renegotiate contracts, should be entitled to the same relief from the competitive bid requirements as the Commission granted to schools and libraries facing similar circumstances in the *July 10 Order*.[669] Similarly, the Telecare Network, an interactive telemedicine service offered by St. Alexius Medical Center in Bismarck, North Dakota, in cooperation with other health care providers in North and South Dakota, asks for relief from the competitive bid requirement with respect to contracts that will still be in effect on and after January 1, 1998. Specifically, Telecare Network asserts that requiring an eligible health care provider to comply with the competitive bid requirement for services received under an existing contract could require parties to "cancel existing contracts -- thereby adding significant penalty costs for terminating the contracts prior to the original terms."[670]

3. Discussion

217. We reconsider our earlier finding that contracts signed on or after November 8, 1996 are not eligible for universal service support after December 31, 1998. We conclude that a contract of any duration signed on or before July 10, 1997 will be considered an existing contract under our rules and therefore exempt from the competitive bid requirement for the life of the contract. Discounts will be provided for eligible services that are the subject of such contracts on a going-forward basis beginning on the first date that schools and libraries are eligible for discounts. We further conclude that contracts signed after July 10, 1997 and before the date on which the Schools and Libraries Corporation website is fully operational will be eligible for support and exempt from the competitive bid requirement for services provided through December 31, 1998. Contracts that are signed after July 10, 1997 are only eligible for support for services received between January 1 and December 31, 1998, regardless of the term or duration of the contract as a whole. In reconsidering our prior determination, we seek to avoid penalizing schools and libraries that were reasonably uncertain of their rights pursuant to the *Order* and to allow greater flexibility for schools and libraries to obtain the benefits of longer-term contracts,

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[668] *See* Letter from James Bentley, AHA, to Chmn. Reed Hundt, FCC, dated October 3, 1997 (AHA Oct. 3 *ex parte*) at 1; *see also*, Letter from Michael J. Mabin, St. Alexius, to Chmn. Reed Hundt, FCC, dated October 3, 1997 (St. Alexius Oct. 3 *ex parte*); Letter from Nancy R. Willis, North Dakota Healthcare Association, to Chmn. Reed Hundt, FCC, dated October 7, 1997 (NDHA Oct. 7 *ex parte*) at 1; Letter from Susan S. Gustke, MD, Eastern Area Health Education Center, to Chmn. Reed Hundt, FCC, dated October 3, 1997 (Eastern AHEC Oct. 3 *ex parte*).

[669] *See* AHA Oct. 3 *ex parte* at 1; Eastern AHEC Oct. 3 *ex parte*.

[670] St. Alexius Oct. 3 *ex parte*.

including potentially lower prices. The *Order* permitted schools and libraries to apply the relevant discounts to only those "contracts that they negotiated prior to the Joint Board's Recommended Decision [November 8, 1996] for services that will be delivered and used after the effective date of our rules."[671] We agree with commenters, however, that section 54.511(c) did not make clear that only contracts that were entered into prior to the date of the Joint Board's Recommended Decision would be eligible for discounts.[672] The *July 10 Order*, by contrast, clearly established that discounts would be provided only for those contracts that either complied with the competitive bid requirement or qualified as "existing" contracts under our rules.

218. We also clarify on our own motion that, if parties take service under or pursuant to a master contract, the date of execution of that master contract represents the applicable date for purposes of determining whether and to what extent the contract is exempt from the competitive bid requirement. For example, if a state signed a master contract for service prior to July 10, 1997, such contract would qualify as an existing contract. If an eligible school subsequently elects to obtain services pursuant to that contract, that school will be exempt from the competitive bid requirement because it is receiving service pursuant to an existing contract. This clarification is consistent with our rules regarding competitive bidding for master contracts set forth in section VI.J, *infra*. Nevertheless, as discussed in sections VI.E. and VI.J. herein, we believe that schools and libraries may benefit from soliciting competitive bids even in cases where they are exempt from such competitive bidding requirements.

219. We further conclude that we should extend our rules regarding support for existing contracts to eligible rural health care providers. Members of the health care community have expressed concern that they will face the same difficulties as those faced by members of the school and library communities, including negotiating lower prices through longer term contracts and avoiding penalties in terminating existing contracts.[673] For generally the same reasons noted above regarding schools and libraries, we also conclude that an eligible health care provider that entered into a contract prior to the date on which the websites are operational would be unfairly penalized by requiring that provider to comply with the competitive bid requirement. We thus extend the same treatment with regard to existing contracts to eligible rural health care providers as we have extended to eligible schools and libraries. An eligible rural health care provider will not be required to comply with the competitive bid requirement for any contract for eligible

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[671] *Order*, 12 FCC Rcd at 9062-9063.

[672] 47 C.F.R. § 54.511(c). Schools and libraries bound by existing contracts. Schools and libraries bound by existing contracts for services shall not be required to breach those contracts in order to qualify for discounts under this subpart during the period for which they are bound. This exemption from competitive bidding requirements, however, shall not apply to voluntary extension of existing contracts.

[673] *See* AHA Oct. 3 *ex parte* at 1; *see also* St. Alexius Oct. 3 *ex parte*.

telecommunications services that it signed on or before July 10, 1997, regardless of the duration of the agreement. In addition, such providers will be eligible to receive reduced rates for services provided through December 31, 1998 for any contract for telecommunications services signed after July 10, 1997 and before the website is operational. Although the *July 10 Order* addressed the issue of existing contracts for only schools and libraries, we believe that establishing July 10, 1997 as the date relevant to our existing contracts rule for rural health care providers is reasonable. We note that this determination is consistent with the request of rural health care providers to be treated in the same manner as schools and libraries.[674] In addition, we anticipate that adopting the same existing contract rules for schools, libraries, and rural health care providers should be administratively simpler and reduce potential confusion on the part of program participants and providers regarding the existing contracts eligible for universal service support. We note that no existing contract exception from the competitive bid requirement previously had been adopted for rural health care providers and that this modification will serve to benefit rural health care providers.

220. We reject the suggestion of EdLiNC that we eliminate any limitation on the duration of discounts for contracts executed before the website for schools and libraries is fully operational. Although we agree with EdLiNC that schools and libraries have a strong incentive to negotiate contracts at the lowest possible pre-discount price in an effort to reduce their costs, we affirm our initial finding that competitive bidding is the most efficient means for ensuring that eligible schools and libraries are informed about the choices available to them and receive the lowest prices.[675] Allowing eligible schools, libraries, and rural health care providers to receive discounts indefinitely on contracts entered into after July 10, 1997 without requiring participation in the competitive bid process would hinder the competitive provision of services for the reasons discussed above.

221. Schools, libraries, and rural health care providers that qualify for the "existing contract" exemption from the competitive bid process described herein will continue to be required to file applications each year with the Schools and Libraries Corporation and Rural Health Care Corporation, respectively, in order to receive universal service discounts. We note that approval of discounts in one year should not be construed as a guarantee of future coverage or assurance that the same level of support will be available in subsequent years.[676] We will continue to monitor the existing contract rule and will make further modifications if necessary.

J. Competitive Bid Requirements for Schools, Libraries, and Rural Health

[674] *See* AHA Oct. 3 *ex parte* at 1; *see also* St. Alexius Oct. 3 *ex parte*.

[675] *Order*, 12 FCC Rcd at 9029.

[676] *Order*, 12 FCC Rcd at 9058.

Care Providers

1. Background

222. Section 254(h)(1)(A) states that "[a] telecommunications carrier shall, upon receiving a bona fide request, provide telecommunications services that are necessary for the provision of health care services in a State . . . to any public or nonprofit health care provider that serves persons who reside in rural areas in that State at rates that are reasonably comparable to rates charged for similar services in urban areas in that State."[677] Section 254(h)(1)(B) states that "[a]ll telecommunications carriers serving a geographic area shall, upon a bona fide request for any of its services that are within the definition of universal service . . ., provide such services to elementary schools, secondary schools, and libraries"[678] at discounted rates. In the *Order*, the Commission concluded that any school, library, or rural health care provider that is eligible to receive supported services will be required to seek competitive bids for all services eligible for support pursuant to section 254(h) by submitting a bona fide request for services to the Administrator that includes a description of the services that the school, library, or health care provider seeks.[679] The Commission required the Administrator to post this information on a website for all potential providers to review.[680]

a. Minor Modifications to Contracts

1. Pleadings

223. USTA argues that there are circumstances in which requiring eligible schools, libraries, and rural health care providers to undertake a full competitive bid process is unduly burdensome.[681] For example, USTA states that "a school may need to add a few additional lines to an already existing contract and it would appear burdensome to require it to adhere to the entire bid process."[682] USTA suggests that the Commission develop a streamlined application process to address such situations.[683] No parties commented on USTA's petition with respect to

[677] 47 U.S.C. § 254(h)(1)(A).

[678] 47 U.S.C. § 254(h)(1)(B).

[679] *Order*, 12 FCC Rcd at 9029, 9133-9134.

[680] *Order*, 12 FCC Rcd at 9078, 9133-9134.

[681] USTA petition at 22.

[682] USTA petition at 22.

[683] USTA petition at 22.

this issue.

2. Discussion

224. We agree with USTA that requiring a competitive bid for every minor contract modification would place an undue burden upon eligible schools, libraries, and rural health care providers. Such eligible entities should not be required to undergo an additional competitive bid process for minor modifications such as adding a few additional lines to an existing contract. We, therefore, conclude that an eligible school, library, or rural health care provider will be entitled to make minor modifications to a contract that the Schools and Libraries Corporation or the Rural Health Care Corporation previously approved for funding without completing an additional competitive bid process. We note that any service provided pursuant to a minor contract modification also must be an eligible supported service as defined in the *Order* to receive support or discounts.[684]

225. In the *Order*, the Commission explained that the universal service competitive bid process is not intended to be a substitute for state, local, or other procurement processes.[685] Consistent with this observation, we conclude that eligible schools, libraries, and rural health care providers should look to state or local procurement laws to determine whether a proposed contract modification would be considered minor and therefore exempt from state or local competitive bid processes. If a proposed modification would be exempt from state or local competitive bid requirements, the applicant likewise would not be required to undertake an additional competitive bid process in connection with the applicant's request for discounted services under the federal universal service support mechanisms. Similarly, if a proposed modification would have to be rebid under state or local competitive bid requirements, then the applicant also would be required to comply with the Commission's universal service competitive bid requirements before entering into an agreement adopting the modification.

226. Where state and local procurement laws are silent or are otherwise inapplicable with respect to whether a proposed contract modification must be rebid under state or local competitive bid processes, we adopt the "cardinal change" doctrine as the standard for determining whether the contract modification requires rebidding. The cardinal change doctrine has been used by the Comptroller General and the Federal Circuit[686] in construing the

[684] *Order*, 12 FCC Rcd. at 9005-9023, 9098-9110.

[685] *Order*, 12 FCC Rcd at 9079, 9134.

[686] 31 U.S.C.A. § 3554(a)(4)(1996) gives the Comptroller General authority to determine whether solicitations of contracts by executive agencies, their proposed awards, or awards comply with statute and regulation. However, this jurisdiction is shared with the district courts of the United States and the Court of Federal Claims. 31 U.S.C.A. § 3556 (1996); 28 U.S.C.A § 1491(b)(1996); s*ee also* 41 U.S.C.A § 253(1996).

Competition in Contracting Act (CICA)[687] as implemented by the Federal Acquisition Regulations.[688] The CICA requires executive agencies procuring property or services to "obtain full and open competition through the use of competitive procedures."[689]

227. Because CICA does not contain a standard for determining whether a modification falls within the scope of the original contract, the Federal Circuit has drawn an analogy to the cardinal change doctrine.[690] The cardinal change doctrine is used in connection with contractors' claims that the Government has breached its contracts by ordering changes that were outside the scope of the changes clause.[691] The cardinal change doctrine looks at whether the modified work is essentially the same as that for which the parties contracted.[692] In determining whether the modified work is essentially the same as that called for under the original contract, factors considered are the extent of any changes in the type of work, performance period, and cost terms as a result of the modification.[693] Ordinarily a modification falls within the scope of the original contract if potential offerors reasonably could have anticipated it under the changes clause of the contract.[694]

228. The cardinal change doctrine recognizes that a modification that exceeds the scope of the original contract harms disappointed bidders because it prevents those bidders from competing for what is essentially a new contract. Because we believe this standard reasonably applies to contracts for supported services arrived at via competitive bidding, we adopt the cardinal change doctrine as the test for determining whether a proposed modification will require

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[687] 41 U.S.C. § 253(a)(1)(A) (1994).

[688] The FAR is issued as Chapter 1 of Title 48, CFR.

[689] The CICA is inapplicable here. We reference this statute and the decisions construing the open competition requirement under 41 U.S.C. § 253(a)(1)(A) only to inform our understanding as to when a contract modification may be deemed to fall within the scope of an original competition and when a contract, as modified, materially departs from the scope of the original competition.

[690] *GraphicData, LLC v. United States*, 37 Fed.Cl. 771, 781 (Fed. Cl. 1997) (citation omitted).

[691] *See* American Air Filter Co. - DLA Request for Reconsideration, 57 Comp. Gen. 567, 572 (1978), 78-1 CPD para. 443 at 9-10.

[692] *See Graphicdata, LLC supra; AT&T v. WILTEL*, 1 F.3d 1201, 1205 (Fed. Cir. 1993); *Cray Research v. Dept. of Navy*, 556 F. Supp. 201, 203 (D.D.C. 1982); *CAD Language Systems*, 68 Comp. Gen. 376 (1989), 89-1 CPD para. 364.

[693] *Information Ventures, Inc.*, B-240458, Nov. 21, 1990, 90-2 CPD para. 414.

[694] *Master Security, Inc.*, B-274990.2, Jan. 14, 1997, 97-1 CPD para. 21; *Air A-Plane Corporation v. United States*, 408 F.2d 1030 (Ct. Cl. 1968); *Hewlett Packard Co.*, B-245293, Dec. 23, 1991, 91-2 CPD para. 576.

rebidding of the contract, absent direction on this question from state or local procurement rules. If a proposed modification is not a cardinal change, there is no requirement to undertake the competitive bid process again.[695]

229. An eligible school, library, or rural health care provider seeking to modify a contract without undertaking a competitive bid process should file FCC Form 471 or 466, "Services Ordered and Certification," with the School and Libraries Corporation or the Rural Health Care Corporation, respectively, indicating the value of the proposed contract modification so that the administrative companies can track contract performance.[696] The school, library, or rural health care provider also must demonstrate on FCC Form 471 or 466 that the modification is within the original contract's change clause or is otherwise a minor modification that is exempt from the competitive bid process.[697] The school, library, or rural health care provider's justification for exemption from the competitive bid process will be subject to audit and will be used by the Schools and Libraries Corporation and Rural Health Care Corporation to determine whether the applicant's request is, in fact, a minor contract modification that is exempt from the competitive bid process.[698] We emphasize that, even though minor modifications will be exempt from the competitive bidding requirement, parties are not guaranteed support with respect to such modified services. A commitment of funds pursuant to an initial FCC Form 471 or Form 466 does not ensure that additional funds will be available to support the modified services. We conclude that this approach is reasonable and is consistent with our effort to adopt the least burdensome application process possible while maintaining the ability of the administrative companies and the Commission to perform appropriate oversight.

b. Master Contracts

1. Pleadings

230. USTA points out that schools, libraries, and rural health care providers in some states may be able to purchase services from a master contract at rates negotiated by a third party. USTA defines a "master contract" as a contract negotiated with a service provider by a third party, the terms and conditions of which are then made available to other entities that purchase

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[695] *See, e.g., MCI Telecommunications Corp.*, B-276659.2, Sept. 29, 1997, 1997 WL 602194 (C.G.) at 13;

[696] *See* USTA Oct. 3 *ex parte* at 2.

[697] *Graphicdata, LLC supra, citing AT&T Communications, Inc. v. WilTel*, 1 F.3d 1201, 1205 (Fed.Cir. 1993).

[698] *Graphicdata, LLC v. United States supra, citing Executive Bus. Media, Inc. v. United States, 3 F.3d at 763 n.3* (4th Cir. 1993).

directly from the provider.[699] According to USTA, "the decision to purchase from the master contract may be independent of the competitive bid process, although the rates offered via that contract may in fact be the most competitive, lowest rates available."[700] USTA notes that there is typically no contractual, financial, or management relationship between the third party that negotiates a master contract and the entity that purchases and receives the service under that master contract.[701] USTA asks the Commission to clarify: (1) that eligible entities that choose to obtain supported services by purchasing them from a master contract may do so without going through the competitive bid process; and (2) whether a third party that seeks to negotiate a master contract for services that eligible entities are expected to purchase would be required to adhere to the universal service competitive bid requirements, or in the case of existing contracts, be required to submit those contracts to the Administrator for registration.[702] USTA suggests that the Commission clarify that eligible entities purchasing from a master contract are required only to submit the paperwork necessary to notify the Administrator of the services it plans to order and to secure a commitment of funds from the Administrator.[703]

231. USTA also seeks clarification that a third party negotiating a master contract, or the lead member of another consortium or aggregated buying arrangement, is not itself required to be an entity eligible to receive universal service benefits and that non-eligible entities would be allowed to submit requests for proposals to the website on behalf of eligible entities.[704]

2. Discussion

232. We find that eligible schools, libraries, and rural health care providers seeking discounted services or reduced rates should be allowed to purchase services from a master contract negotiated by a third party.[705] In the *Order*, the Commission found that the competitive bid requirement would minimize the universal service support required by ensuring that schools,

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[699] *See* Letter from Hance Haney, USTA, to Chmn. Reed Hundt, FCC, dated October 3, 1997 (USTA Oct. 3 *ex parte*) at 1.

[700] USTA petition at 22-23.

[701] *See* USTA Oct. 3 *ex parte* at 1.

[702] *See* USTA Oct. 3 *ex parte* at 1-2.

[703] *See* USTA Oct. 3 *ex parte* at 2.

[704] *See* USTA Oct. 3 *ex parte* at 2.

[705] USTA petition at 22-23.

libraries, and rural health care providers are aware of cost-effective alternatives.[706] The Commission concluded that, like the language of section 254(h)(1) that targets support to public and nonprofit rural health care providers, this approach "ensures that the universal service fund is used wisely and efficiently."[707] Insofar as an independent third party negotiating a master contract may be able to secure lower rates than an eligible entity negotiating on its own behalf, we conclude that allowing schools, libraries, and rural health care providers to order eligible telecommunications services from a master contract negotiated by a third party is consistent with our goal of minimizing universal service costs and therefore is also consistent with section 254(h)(1).[708]

233. We wish to emphasize, however, that for eligible schools and libraries to receive discounted services, and for rural health care providers to receive reduced rates, the third party initiating a master contract either must have complied with the competitive bid requirement or qualify for the existing contract exemption before entering into a master contract.[709] An eligible school, library, or rural health care provider shall not be required to satisfy the competitive bid requirement if the eligible entity takes service from a master contract that has been competitively bid under the Commission's competitive bid requirement. If a third party has negotiated a master contract without complying with the competitive bid requirement, then an eligible entity must comply with the competitive bid requirement before it may receive discounts or reduced rates for services purchased from that master contract.

234. As noted above, the date of execution of a master contract represents the applicable date for purposes of determining whether and to what extent the contract is exempt from the competitive bid requirement under the existing contract exemption. For example, if a state signed a master contract for service prior to July 10, 1997 that qualifies as an existing contract under our rules, and a school elects to take service pursuant to that contract at a date after the website is operational, that school will be exempt from the competitive bid requirement because it is receiving service pursuant to an existing contract.[710] As we stated above, we strongly encourage schools and libraries to engage in competitive bidding even if they are exempt from such requirement pursuant to Commission rules. Schools and libraries may well be able to obtain more favorable terms if they issue new requests for bids designed to accommodate their

[706] *Order*, 12 FCC Rcd at 9029, 9134.

[707] *Order*, 12 FCC Rcd at 9134.

[708] *Order*, 12 FCC Rcd at 9134.

[709] Letter from Hance Haney, United States Telephone Association, to Kim Parker, FCC, Universal Service Branch, Dec. 4, 1997.

[710] *See* Section VI.I. *supra*.

specific needs, rather than obtain service under the terms of the master contract. For instance, a master contract that was put out for bid several years ago but has not yet expired might not reflect the cost reductions resulting from recent entry into the local exchange market, for example, by wireless carriers. Although we have provided for certain exemptions from competitive bidding requirements, to enable schools and libraries to transition to the Commission's procedures implementing the new universal service mechanisms, we believe that even institutions subject to the exemptions may obtain substantial benefit from soliciting competitive bids. Moreover, those institutions may ultimately obtain service pursuant to the master contract, if they determine that the service provider under the master contract is the most cost effective provider. We intend to monitor the impact of the competitive bid exemptions on an ongoing basis.

235. Furthermore, even if eligible schools, libraries, and health care providers are obligated by the school district or a consortium, for example, to purchase from a master contract, the third party nevertheless must have complied with the competitive bid process in order for an eligible entity to receive discounts or reduced rates on services ordered from the master contract. If the third party has not complied with the competitive bid requirement before entering into a master contract, then an eligible school, library, or rural health care provider itself must undertake the competitive bid process before it may receive discounts or reduced rates on services purchased from the master contract. These requirements will ensure that the eligible entity is receiving the most cost-effective service.

K. Reimbursement for Telecommunications Carriers

1. Background

236. Section 254(b)(5) establishes the principle that "[t]here should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service."[711] Furthermore, section 254(e) directs that any universal service support "should be explicit and sufficient to achieve the purposes of [section 254]."[712]

237. The Commission concluded that discounts for eligible schools and libraries shall be capped at $2.25 billion annually.[713] The Commission also concluded that discounts would be committed on a first-come-first-served basis. If and when total payments committed during a funding year have exhausted any funds carried over from previous years and there are only $250 million in funds available for the funding year, a system of priorities will govern the distribution

[711] 47 U.S.C. § 254(b)(5).

[712] 47 U.S.C. § 254(e).

[713] *Order*, 12 FCC Rcd at 9057.

of the remaining $250 million.[714] The Commission stated in the Order that some uncertainty may remain about whether an institution will receive the same level of discount from one year to the next because demand for funds may exceed the funds available.[715] The Commission stated further that it cannot guarantee discounts in the subsequent year in such a situation because doing so would place institutions that have not formulated their telecommunications plans in the previous year at a disadvantage, and possibly preclude such entities from receiving any universal service support.[716] The Commission directed Schools and Libraries Corporation to recommend to the Commission a reduction in the guaranteed percentage discounts as necessary to permit all expected requests in the next funding year to be fully funded, if it estimates that the $2.25 billion cap will be reached for the current funding year.[717] The Commission encouraged schools and libraries to make their agreements contingent on approval of universal service funding for the contracted services.[718]

238. In the *Order*, the Commission concluded that service providers, rather than schools and libraries, should seek compensation from the Administrator.[719] The Commission found, among other reasons, that permitting service providers to demand full payment from schools and libraries could create serious cash flow problems and would disproportionately affect the most disadvantaged schools and libraries.[720]

239. Similarly, in the health care section of the *Order*, the Commission adopted an annual cap of $400 million for universal service support for health care providers and concluded that support should be committed on a first-come-first-served-basis.[721] Health care providers will be permitted to submit funding requests once they have made agreements for specific eligible services, and the Administrator will commit funds based on those agreements until the total payments committed during a funding year reach the amount of the cap.[722] The

[714] *Order*, 12 FCC Rcd at 9057-9058.

[715] *Order*, 12 FCC Rcd at 9058.

[716] *Order*, 12 FCC Rcd at 9058.

[717] *Order*, 12 FCC Rcd at 9058.

[718] *Order*, 12 FCC Rcd at 9057 n. 1396.

[719] *Order*, 12 FCC Rcd at 9083.

[720] *Order*, 12 FCC Rcd at 9083.

[721] *Order*, 12 FCC Rcd at 9143.

[722] *Order*, 12 FCC Rcd at 9143.

Commission also encouraged health care providers to make their agreements contingent on approval of universal service funding for the contracted services.[723]

240. In the *October 14 Order*, the Commission adopted a filing window period and concluded that all applications for support from schools and libraries support mechanisms or the health care support mechanisms filed during the window will be treated as if received simultaneously.[724]

2. Pleadings

241. USTA asks the Commission to clarify that schools, libraries, and rural health care providers remain responsible for all charges incurred, "particularly if a provider is unable to receive full reimbursement from the universal service support mechanisms," as well as for the full payment of other charges that may arise, "such as state and federal taxes, termination liability or penalty surcharges, franchise fees, etc."[725]

242. USTA expresses the concern that a carrier may not receive reimbursement to which it is entitled from the universal service support mechanisms under certain circumstances. In such a case, USTA asks the Commission to clarify that the eligible entity receiving the benefit of discounts or lower urban rates should remain responsible for any payment due to the provider. We note that USTA does not specify the particular set of circumstances that may cause a service provider to recover less than the amount owed to it. No parties commented on USTA's petition with respect to this issue.

3. Discussion

243. We do not anticipate that the cost of funding eligible services will exceed the cap on universal service funding for schools, libraries, and rural health care providers[726] An applicant's "place in line," or seniority for the purposes of allocating funding will be determined by the date on which an applicant submits FCC Form 471 or 466 to the applicable administrative

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[723] *Order*, 12 FCC Rcd at 9143 n. 1850.

[724] Federal-State Joint Board on Universal Service, *Third Report and Order*, CC Docket No. 96-45, FCC 97-380 (rel. Oct. 14, 1997) *(October 14 Order*) at para. 2. The *Order* delegated to Schools and Libraries Corporation and Rural Health Care Corporation, respectively, authority to determine the duration of the window period. The administrative companies have since adopted a 75 day window.

[725] USTA petition at 23.

[726] *See Order*, 12 FCC Rcd at 9060, 9144.

corporation.[727] Because eligible entities will enter into contracts with service providers prior to the submission of requests for commitment of funds (FCC Form 466 or 471, "Services Ordered and Certification"), such a request could be denied in the unlikely event that funds prove to be insufficient. In light of this possibility, and because charges incurred for eligible telecommunications services remain the responsibility of the eligible entity, we agree with USTA and again urge schools, libraries, and rural health care providers to include clauses in their contracts that make implementation of the agreements contingent on the commitment of universal service funding.[728]

244. USTA asks for clarification regarding the types of charges associated with the purchase or termination of an eligible telecommunications service that will be covered by the federal support mechanisms. We conclude that the universal service support mechanisms will cover all reasonable charges, including federal and state taxes, that are incurred by obtaining an eligible telecommunications service. Charges for termination liability, penalty surcharges, and other charges not included in the cost of obtaining the eligible service will not be covered by the universal service support mechanisms. We do not include among the costs supported by the support mechanisms charges associated with terminating a service because we conclude that such charges are avoidable. The imposition of such charges typically results from a party's failure to discharge its duty of performance under a contract and supporting such charges does not advance program goals.

L. Universal Service Support for Intrastate Telecommunications Services Provided to Rural Health Care Providers

1. Background

245. Section 254(h)(1)(A) requires that eligible health care providers be permitted to purchase telecommunication services "necessary for the provision of health care services in a State, including instruction relating to such services . . . at rates that are reasonably comparable to rates charged for similar services in urban areas in that State."[729] In the schools and libraries section of the *Order*, the Commission determined that federal universal service support mechanisms will support discounts on both interstate and intrastate services.[730] The *Order* did

[727] *October 14 Order* at para. 3.

[728] *See Order*, 12 FCC Rcd at 9057 n. 1396 and 9080 n. 1496. Purchases of real estate are commonly contingent on approvals of mortgage applications.

[729] 47 U.S.C. § 254(h)(1)(A).

[730] *Order*, 12 FCC Rcd at 9064-9065. Consistent with section 254(h)(1)(B), which authorizes the states to determine the level of discount available to eligible schools and libraries with respect to intrastate services, the Commission

not address whether intrastate services provided to eligible rural health care providers will be supported by the federal universal service support mechanisms.

2. Pleadings

246. USTA seeks clarification that the federal universal service support mechanisms will support reduced rates on intrastate services provided to rural health care providers.[731] No parties commented on USTA's request for clarification with respect to this issue.

3. Discussion

247. The Commission clarifies that the federal universal service support mechanisms will support reduced rates on intrastate services provided to eligible rural health care providers.[732] As set forth in section 54.601(c)(1) of the Commission's rules, any telecommunications service of a bandwidth up to and including 1.544 Mbps that is the subject of a properly completed bona fide request by an eligible health care provider is eligible for universal service support, subject to distance limitations.[733] These eligible telecommunications services may be intrastate or interstate in nature. In addition, limited toll free access to an Internet service provider is eligible for universal service support under section 54.621 of the Commission's rules for health care providers that are unable to obtain such access.[734]

M. Support for Services Beyond the Maximum Supported Distance for Rural Health Care Providers

1. Background

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required states to establish intrastate discounts at least equal to the discounts available on interstate services as a condition of federal universal service support for schools and libraries in that state.

[731] USTA petition at 22.

[732] Unlike the Commission's decision, pursuant to section 254(h)(1)(B), to require states to establish intrastate discounts at least equal to the discounts available on interstate services as a condition of federal universal service support for schools and libraries in that state, the Commission did not impose such a requirement in the health care context. Section 254 contains no requirement authorizing or requiring the states to establish urban rates for intrastate services provided to rural health care providers.

[733] 47 C.F.R. § 54.601(c)(1). *See also* 47 C.F.R. § 54.613(b) (lesser bandwidth services may be selected as long as the total annual support amount for those services does not exceed the support amount for a telecommunications service with 1.544 Mbps capability).

[734] 47 C.F.R. § 54.621.

248. Section 254(h)(1)(A) states that "[a] telecommunications carrier shall . . . provide telecommunications services . . . to any public or non-profit health care provider . . . at rates that are reasonably comparable to rates charged for similar services in urban areas in that State."[735] In the *Order*, the Commission concluded that support for some distance-based charges is necessary to ensure that rates charged to rural health care providers are "reasonably comparable" to urban rates.[736] The Commission, therefore, determined that universal service support shall be provided for eligible telecommunications services carried over a distance not to exceed the distance between the health care provider and the farthest point on the jurisdictional boundary of the nearest large city to the health care provider's location (maximum supported distance).[737]

2. Pleadings

249. USTA asks the Commission to clarify that a rural health care provider may purchase a mileage-based service that is longer than the distance of the farthest point on the boundary of the nearest large city and pay the rural mileage price for the distance beyond the maximum supported distance.[738] No parties commented on USTA's request for clarification with respect to this issue.

3. Discussion

250. Although the Commission limited universal service support to an amount that would cover an eligible telecommunications service provided over a maximum allowable distance, nothing in the *Order* precludes a health care provider from purchasing an eligible telecommunications service carried over a distance that exceeds this limitation. We clarify that we do not intend to restrict a rural health care provider from purchasing an eligible telecommunications service that is provided over a distance that is longer than the maximum supported distance, that is, from the health care provider to the farthest point on the boundary of the nearest large city. Rural health care providers, however, must pay the applicable price for the distance that such service is carried beyond the maximum supported distance. This approach is consistent with Congress's intent to make rural and urban rates comparable while affording the eligible rural health care provider that chooses to connect to a city that is farther than the nearest large city in that state the flexibility to make such a decision without jeopardizing the provider's

[735] 47 U.S.C. § 254(h)(1)(A).

[736] *Order*, 12 FCC Rcd at 9127-9128.

[737] *Order*, 12 FCC Rcd at 9130.

[738] USTA petition at 22.

entitlement to receive a discount on services carried within the maximum supported distance.

N. Establishing the Standard Urban Distance and Maximum Supported Distance for Rural Health Care Providers

1. Background

251. In an effort to make urban and rural rates comparable, the Commission adopted the standard urban distance concept for determining the urban rate the rural health care provider should pay for a supported service.[739] Section 54.605(d) of the Commission's rules provides that '[t]he standard urban distance' for a state is the average of the longest diameters of all cities with a population of 50,000 or more within the state, *calculated by the Administrator*."[740]

2. Pleadings

252. USTA asks the Commission to clarify that the Administrator should be responsible for establishing the standard urban distance and the maximum supported distance applicable to rural health care providers and for posting this information on its website.[741] No parties commented on USTA's petition with respect to this issue.

3. Discussion

253. We amend section 54.605(d) of our rules to provide that the Rural Health Care Corporation will be responsible for calculating the standard urban distance (and, by definition, the maximum supported distance) applicable to eligible rural health care providers. Section 54.605(d) of the Commission's rules currently requires the "Administrator" to establish the standard urban distance.[742] Specifically, the *NECA Report and Order* [743] assigned to USAC and

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[739] *Order*, 12 FCC Rcd at 9131.

[740] 47 C.F.R. § 54.605(d) (emphasis added). In the *Order*, the Commission concluded that the longest diameters of all cities with a population of 50,000 or more within a state should be averaged to arrive at that state's standard urban distance. *Order*, 12 FCC Rcd at 9131 . If a rural health care provider requests that a service be provided over a distance that is less than or equal to the standard urban distance in a state, then the rate that would be paid by the rural health care provider for that service shall be the rate charged for a similar service provided over the same distance in the nearest large city. If a rural health care provider requests that a service be provided over a distance that is greater than the standard urban distance in a state, then the rate that would be paid by the rural health care provider for that service shall be the rate charged for a similar service provided over the standard urban distance in the nearest large city. *Order*, 12 FCC Rcd at 9131-9132.

[741] USTA petition at 24.

[742] 47 C.F.R. § 605(d). The term "Administrator" is defined in the Commission's Part 54 rules as:

to the entity ultimately selected to serve as the permanent Administrator, responsibility for performing the billing, collection and disbursement functions associated with all of the universal service support mechanisms, including the support mechanisms for rural health care providers.[744] The *NECA Report and Order* assigned to the Rural Health Care Corporation the remaining administrative functions associated with administering the rural health care program.[745] Consistent with this division of administrative responsibilities set forth in the *NECA Report and Order*, we conclude that the Rural Health Care Corporation rather than USAC or the permanent Administrator should perform the calculations necessary to establish the standard urban distance pursuant to section 54.605(d).

254. We also grant USTA's request that the calculation of the standard urban distance for each state be posted on a website. Accordingly, we direct the Rural Health Care Corporation to post such information to the Rural Health Care Corporation's website.

VII. ADMINISTRATION OF SUPPORT MECHANISMS

255. Universal service contribution requirements pursuant to section 254 of the Act will take effect on January 1, 1998. In the *Order*, the Commission found that requiring a broad range of providers to contribute to universal service was consistent with the statute.[746] Numerous parties have asked us to reconsider, prior to January 1, 1998, our decisions requiring certain providers to contribute to universal service pursuant to section 254. We herein reconsider those decisions. We note, however, that we will conduct a thorough reevaluation of who is required to

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> the National Exchange Carrier Association, Inc. until the date that an independent subsidiary of the National Exchange Carrier Association, Inc. is incorporated and has commenced the administration of the universal service support mechanisms. On that date and until the permanent Administrator has commenced the permanent administration of the universal service support mechanisms, the term "Administrator" shall refer to the independent subsidiary established by the National Exchange Carrier Association, Inc. for the purpose of temporarily administering the portions of the universal service support mechanisms described in section 69.616. On the date that the entity selected to permanently administer the universal service support mechanisms commences operations and thereafter, the term "Administrator" shall refer to such entity. 47 C.F.R. § 54.5.

[743] *NECA Report and Order* at paras. 30, 57-60 (directing NECA to establish USAC, the Schools and Libraries Corporation, and the Rural Health Care Corporation for purpose of administering the universal service support mechanisms).

[744] *NECA Report and Order* at para. 41.

[745] *NECA Report and Order* at paras. 65-66.

[746] *Order*, 12 FCC Rcd at 9173, 9177.

contribute to universal service, pursuant to Congress's direction to issue a report on this issue by April 10, 1998.[747] That report to Congress may serve as the basis for subsequent Commission action on this issue.

A. Paging Carriers

1. Background

256. Section 254(d) states that "[e]very telecommunications carrier that provides interstate telecommunications services shall contribute, on an equitable and nondiscriminatory basis" to universal service.[748] Based on this provision, the Commission concluded that all telecommunications carriers, including paging carriers, that provide interstate telecommunications services must contribute to universal service.[749] In arriving at this conclusion, the Commission rejected suggestions that contributions to universal service should only be assessed against telecommunications carriers that are eligible to receive high cost support or that carriers that are ineligible to receive such support should be permitted to make reduced contributions.[750] The Commission reasoned that the statute requires all telecommunications carriers to contribute to universal service support mechanisms, but provides that only "eligible" carriers should receive support, and therefore affords the Commission no discretion to establish preferential treatment for carriers that are ineligible for support.[751]

2. Pleadings

257. Several petitioners challenge the requirement that paging carriers contribute to universal service.[752] These petitioners argue that their contributions to universal service are tantamount to an unconstitutional tax, because paging carriers will derive no benefit from the tax.[753] For example, ProNet asserts that, because its customers are businesses and high-income

[747] Pub. L. 105-119, 111 Stat. 2440 (approved November 26, 1997) ("Report to Congress"). *See* Section VII.D., below.

[748] 47 U.S.C. § 254(d).

[749] *Order*, 12 FCC Rcd at 9206.

[750] *Order*, 12 FCC Rcd at 9188.

[751] *Order*, 12 FCC Rcd at 9188.

[752] *See, e.g.*, Ozark petition at 4; PCIA petition at 3-7; ProNet petition at 7-9; Teletouch petition at 3-5.

[753] ProNet petition at 7-9; Teletouch petition at 3-5. Specifically ProNet argues that the universal service goals of upgrading the nation's school and library facilities are characteristic of general welfare goals, and thus render

individuals, it will receive no benefit from universal service.[754] ProNet adds that, even if contributions were considered "user fees" rather than a tax, the assessment of such contributions would still be unconstitutional because, according to ProNet, user fees must be reasonably related to the benefits conferred.[755] Teletouch argues that universal service contributions are tantamount to a tax because carriers must submit payments that will be distributed to non-contributing beneficiaries. ProNet also asserts that paging carriers receive no benefits from universal service and thus contributions represent an unconstitutional taking of property without just compensation under the Fifth Amendment. By contrast, Ozark contends that requiring paging carriers to contribute to universal service violates the universal service goal of providing affordable service to low-income consumers.[756] It asserts that most of its customers are low-income consumers or unemployed individuals and that, if it raises its rates to recover its contribution, those customers may not be able to afford its paging service.[757]

258. Several paging carriers also contend that their obligation to contribute to universal service on the same basis as eligible telecommunications carriers is inequitable and discriminatory.[758] PCIA asserts that the contribution requirements are not equitable because paging carriers that are ineligible to receive high cost support would contribute equal percentages as entities that are eligible to receive high cost support.[759] PCIA further states that requiring paging carriers to make the same contributions as other carriers is discriminatory because paging carriers will be forced to compete with telecommunications carriers that are eligible to receive universal service support.[760] Specifically, PCIA claims that eligible telecommunications carriers that also provide paging services will have an unfair advantage over paging companies.[761] Teletouch asserts that the paging market is more competitive than other sectors of the telecommunications industry.[762] Therefore, Teletouch argues that the contribution requirements

contributions a tax.

[754] ProNet petition at 7-8.

[755] ProNet opposition at 5-6.

[756] Ozark petition at 6-8.

[757] Ozark petition at 6-8.

[758] *See* Ozark petition at 4; PCIA petition at 3-7.

[759] PCIA petition at 5-6.

[760] PCIA petition at 6-7. *See also* Ozark petition at 4; ProNet petition at 3-4.

[761] PCIA petition at 6-7.

[762] Teletouch petition at 6-7.

are not equitable because paging carriers, unlike other contributors, will be unable to raise consumer prices to recover universal service contributions.[763] ProNet further argues that "on a 'net' basis" the Commission's contribution requirements will discriminate in favor of eligible telecommunications carriers that receive support because that support will allow eligible telecommunications carriers to offset the cost of making contributions.[764] Paging carriers, however, according to ProNet, will make contributions based on total end-user telecommunications revenues, as opposed to "net revenues" as described above, and will have no opportunity to offset their contributions.[765]

259. To remedy what it describes as an inequitable tax on paging carriers, Teletouch proposes that paging carriers be exempt from universal service contribution requirements.[766] Alternatively, to take into account the highly competitive paging industry, Teletouch asserts that the Commission should assess paging carriers' contributions on the basis of net profits.[767] PCIA proposes a different remedy, and recommends that paging carriers be required to make contributions that are 50 percent less than those made by eligible telecommunications carriers.[768] ProNet argues that the Commission has treated paging carriers differently than other CMRS providers in the context of regulatory fees, and states that there is no reason why the Commission must treat all carriers equally for universal service contribution purposes.[769]

260. In response to these arguments, RTC counters that other universal service contributors are not eligible to receive universal service support, such as IXCs,[770] payphone service providers, and private service providers, and the Commission should not exempt special categories of contributors.[771] AT&T and Bell Atlantic also contend that paging carriers should

[763] Teletouch petition at 6-7. *See also* ProNet petition at 5.

[764] ProNet petition at 4.

[765] ProNet petition at 4.

[766] Teletouch petition at 7.

[767] Teletouch petition at 7.

[768] PCIA petition at 8.

[769] ProNet petition at 5-6. Specifically, in FY 1996, CMRS one-way paging licensees paid regulatory fees of $0.02 per unit, while cellular carriers paid fees of $0.17 per unit. *See* Assessment and Collection of Regulatory Fees for Fiscal Year 1996, *Report and Order*, 11 FCC Rcd 18774 (1996).

[770] We note that many IXCs will be ineligible to receive high cost support. IXCs that provide all of the core services, however, may be eligible to receive high cost support.

[771] RTC opposition at 6-8. *See also* AT&T opposition at 21; Bell Atlantic opposition at 8-9.

not be afforded special reduced contribution obligations or other special treatment.[772] ProNet responds that, unlike paging carriers, other "ineligible" carriers, such as IXCs, immediately benefit from an expanded local network.[773]

261. Finally, Teletouch challenges its obligation to contribute to universal service by asserting that, pursuant to section 2(b) of the Act, the Commission does not have jurisdiction over paging carriers, whose only interstate service is the provision of access to the interexchange network.[774]

3. Discussion

262. We affirm our conclusion in the *Order* that all telecommunications carriers, including paging carriers, are required by section 254(d) to contribute to universal service. Petitioners offer no compelling arguments to alter the Commission's earlier decision. We find that universal service contributions do not constitute a tax. As noted in the *Order*, the U.S. Court of Appeals for the D.C. Circuit has held that "a regulation is a tax only when its primary purpose judged in legal context is raising revenue."[775] The fact that section 254 permits discounts to be provided to schools and libraries for certain services provided by non-telecommunications carriers also does not convert universal service contributions into a revenue-raising "tax" because the primary purpose of the contributions is not to raise general revenues.[776] Rather, the primary purpose of the universal service contribution requirements is the preservation and advancement of universal service in furtherance of the principles set forth in section 254(b). Universal service contributions are not commingled with government revenues raised through taxes. Furthermore, contrary to ProNet's assertions, requiring contributions to universal service confers a benefit on paging carriers because such contributions help preserve the universal availability of service over the public switched telephone network. Without the public switched telephone network, subscribers of paging carriers would not be able to receive pages, retrieve pages, or respond to

[772] AT&T opposition at 21; Bell Atlantic opposition at 8-9.

[773] ProNet opposition at 5.

[774] Teletouch supplement to petition at 2-4. Teletouch filed this supplement on September 9, 1997. The filing deadline for petitions for reconsideration in a notice and comment rulemaking proceeding are prescribed in section 405 of the Act. *See* 47 U.S.C. § 405(a). The Commission lacks discretion to waive this statutory requirement. *See Virgin Islands Telephone Corp. v. FCC*, 989 F.2d 1231, 1237 (D.C. Cir. 1993); *Reuters Ltd. v. FCC*, 781 F.2d 946, 951-52 (D.C. Cir. 1986). The filing deadline for petitions for reconsideration of the *Order* was July 17, 1997. We will consider the supplement as an informal comment. 47 U.S.C. § 154(j).

[775] *Order*, 12 FCC Rcd at 9088, *citing Brock v. Washington Metropolitan Area Transit Authority*, 796 F.2d 481, 488 (D.C. Cir. 1986).

[776] *See Order*, 12 FCC Rcd at 9088.

messages. We find that the benefits of universal service accrue to all paging carriers, regardless of whether they serve high-income or low-income customers.[777]

263. Section 254(d) requires "[e]very telecommunications carrier" to contribute to universal service. It does not limit contributions to carriers eligible for universal service support.[778] In fact, as RTC notes, IXCs, payphone service providers, private service providers, and CMRS providers are required to contribute to universal service, even though they might not receive support from the high cost mechanisms. The petitioning paging companies have not advanced any credible evidence that would justify exempting them from the Congressional requirement that we create a broad base of support for universal service programs. The fact that the Commission may treat paging carriers differently than other CMRS providers in the context of regulatory fees is not relevant to the treatment of paging carriers under section 254(d).

264. We disagree with PCIA that requiring paging carriers to contribute to universal service is discriminatory or not competitively neutral. Although some two-way carriers that compete with paging carriers may be eligible to receive universal service support, such telecommunications carriers will receive support only for those services included within the core definition of universal service (*e.g.*, voice-grade access, single-party service, and access to emergency services).[779] Eligible telecommunications carriers that provide paging services will not receive support for their paging services. Thus, eligible telecommunications carriers that provide paging services will not have an unfair advantage over paging carriers.

265. We also disagree with ProNet's argument that requiring contributions from paging companies, that are not eligible for support, violates competitive neutrality unless eligible telecommunications carriers are required to include amounts they receive from the universal service support mechanisms in calculating their total end-user telecommunications revenues. To the contrary, as we found in the *Order*, basing contributions from all telecommunications carriers on their gross end-user telecommunications revenues best satisfies our goals of competitive neutrality and ease of administration, as well as the statutory requirement that support be explicit.[780] Payments received from the universal service support mechanisms are not counted as end-user telecommunications revenues in the assessment base, because such funds are derived

[777] We note that paging carriers may receive universal service support for providing discounted paging services to eligible schools and libraries, provided those telecommunications services are used for educational purposes only. *See* 47 U.S.C. § 254(h)(1)(B); *Order*, 12 FCC Rcd at 9006 n.1117.

[778] *See also supra* section V.B.

[779] *Order*, 12 FCC Rcd at 8807, 8899-8900.

[780] *Order*, 12 FCC Rcd at 9211.

from the federal support mechanisms, not end users of telecommunications.[781] Furthermore, high-cost support does not "offset" eligible telecommunications carriers' contributions. Support is provided to offset in part the cost of serving high cost areas. Moreover, it would be counter-productive to universal service goals to require carriers eligible for support to make a contribution based on support amounts. That approach would increase the level of contributions needed to provide adequate support to carriers that serve high cost areas.

266. Finally, we reject Teletouch's argument that the Commission lacks jurisdiction over paging carriers whose only interstate service is the provision of access to the interexchange network. It is well established that access to the interstate interexchange network is an interstate service that brings paging carriers within the coverage of section 254(c).[782] An interstate telecommunication is defined as a communication or transmission that originates in one state and terminates in another.[783] A page that originates in one state and terminates in another meets the statutory definition of "interstate telecommunication." Therefore, even if a paging carrier's service area does not cross state boundaries, if a paging carrier enables paging customers to receive out-of-state pages, i.e., be paged by someone located in another state, then that paging carrier provides an interstate service and must contribute to universal service.[784]

B. Other Providers of Interstate Telecommunications

1. Background

267. Section 254(d) provides that "[e]very telecommunications carrier that provides interstate telecommunications services" must contribute to universal service.[785] Section 254(d) also states that "[a]ny other provider of interstate telecommunications may be required to contribute if the public interest so requires."[786] Under the Act, "telecommunications" are defined as the transmission, between or among points specified by the user, of information of the user's choosing without change in the form or content of the information as sent and received."[787] An

[781] *Order*, 12 FCC Rcd at 9212.

[782] *See National Ass'n of Regulatory Utility Com'rs v. F.C.C.*, 746 F.2d 1492, 1498 (D.C. Cir. 1984).

[783] 47 U.S.C. § 153(22).

[784] *See* 47 U.S.C. § 153(22).

[785] 47 U.S.C. § 254(d).

[786] 47 U.S.C. § 254(d).

[787] 47 U.S.C. § 153(43).

"interstate" transmission generally is defined as a transmission that originates in one state, territory, or possession and terminates in another state, territory, or possession.[788] In the *Order*, the Commission found that the phrase "other providers of interstate telecommunications" refers to entities that provide interstate telecommunications on a non-common carrier basis.[789] "Other providers of interstate telecommunications" compete with telecommunications carriers, and the Commission did not want contribution obligations to influence a business's decision to sell telecommunications to others on a common carrier or private contractual basis. The Commission, therefore, found that the public interest requires private service providers that provide interstate telecommunications to others for a fee on a non-common carrier basis to contribute to universal service.[790] The Commission found, however, that entities providing direct broadcast satellite (DBS) services, open video services (OVS), and cable leased access would not be required to contribute on the basis of revenues derived from those services.[791]

2. Pleadings

268. Several petitioners contend that non-common carriers should not be required to contribute to universal service.[792]

269. *Systems Integrators*. Several systems integrators[793] assert that the public interest would not be served by requiring them to contribute to universal service because the costs associated with requiring these entities to contribute outweigh any benefits.[794] Ad Hoc asserts that the administrative costs incurred by systems integrators to develop accounting systems to comply with universal service reporting requirements will exceed the amount that systems integrators will contribute to universal service. In view of these costs, Ad Hoc maintains that the

[788] 47 U.S.C. § 153(22).

[789] *Order*, 12 FCC Rcd at 9182.

[790] *Order*, 12 FCC Rcd at 9182.

[791] *Order*, 12 FCC Rcd at 9176.

[792] *See, e.g.*, Ad Hoc petition at 12-13; ITAA petition at 5-7; EDS reply at 8; IBM reply at 3-4; AAPTS informal comments.

[793] Systems integrators provide integrated packages of services and products that may include the provision of computer capabilities, interstate telecommunications services, remote data processing services, back-office data processing, management of customer relationships with underlying carriers and vendors, provision of telecommunications and computer equipment, equipment maintenance, help desk functions, and other services and products. Ad Hoc petition at 11-12. Systems integrators are non-facilities-based, non-common carriers.

[794] *See* Ad Hoc petition at 12-13; ITAA petition at 5-7; EDS reply at 8; IBM reply at 3-4.

public interest will not be served by requiring systems integrators to contribute.[795] Ad Hoc also argues that systems integrators do not provide interstate telecommunications on a stand-alone basis and, instead, charge a single monthly fee for a package of services.[796] IBM contends that total end-user telecommunications revenues of all systems integrators will not significantly expand the total funding base and, thus, the inclusion of systems integrators in the pool of contributors will not add significant additional revenues to the funding base.[797]

270. IBM asserts that it would be consistent with the Commission's goal of competitive neutrality to exempt systems integrators from contribution requirements because such firms do not compete with common carriers or other carriers for the same customers. IBM claims that systems integrators provide service to a different market in which telecommunications are not the primary focus.[798] Consequently, IBM states that the Commission's rationale for requiring non-common carriers to contribute does not apply to systems integrators.[799] Ad Hoc contends that, contrary to the Commission's stated intention, contribution requirements will influence business decisions and may prompt systems integrators to discontinue the provision of interstate telecommunications.[800]

271. Systems integrators also contend that the contribution assessment mechanism is not competitively neutral as applied to systems integrators. Ad Hoc alleges that the assessment mechanism is not competitively neutral because systems integrators face a double-counting problem. Ad Hoc states that, because systems integrators cannot determine the precise amount of service that they utilize internally and the amount of service that they resell, underlying carriers will charge these companies "end-user" rates for services that are actually resold.[801] Ad Hoc claims that, for those resold services that are mistakenly billed as end-user services, systems integrators will pay universal service contributions twice; once through their own direct contributions and once through rates that include the underlying carriers' universal service contribution. ITAA adds that many wholesale carriers may not know that private service providers contribute to the support mechanisms and thus may charge them "end-user" rather than

[795] Ad Hoc petition at 12.

[796] Ad Hoc petition at 12.

[797] IBM opposition at 12-13.

[798] IBM comments at 3-4.

[799] IBM comments at 3-4.

[800] Ad Hoc petition at 14-15. *See also* IBM comments at 14-15.

[801] Ad Hoc petition at 15-16. *See also* IBM comments at 6; EDS reply at 8.

"reseller" rates for all of their services.[802] Furthermore, IBM notes that, prior to the adoption of the *Order*, many systems integrators entered into multi-year contracts with common carriers and that the carriers' universal service costs are reflected in the terms of those contracts. IBM maintains that, unless common carriers reduce their rates to take into account systems integrators' contributions to universal service, the assessment mechanism is not competitively neutral because systems integrators will contribute twice to universal service.[803] IBM avers that parties may not be able to renegotiate their contracts for several years, thus perpetuating the double payment problem.[804] For these reasons, systems integrators claim that they should not be required to contribute to universal service.[805]

272. Ad Hoc contends that Congress did not intend non-common carriers, including systems integrators, to contribute to universal service unless private telecommunications services become a significant means of bypassing the public switched telephone network.[806] Ad Hoc further contends that the Commission made no finding that private networks are a significant means of bypassing the public switched telephone network and therefore erred in finding that the public interest requires private service providers that serve others for a fee to contribute to universal service.[807]

273. In addition, ITAA contends that systems integrators should not be required to contribute to universal service because they are information service providers.[808] ITAA states that, pursuant to long-standing Commission precedent, if a service provider offers an enhanced service "in conjunction with" a basic service, the entire service offering is deemed to be an enhanced service. Thus, ITAA concludes that a systems integrator would only be required to contribute to universal service if it provides a free-standing telecommunications service.

274. In response to these arguments, Bell Atlantic asserts that systems integrators do

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[802] ITAA petition at 8.

[803] IBM comments at 4-5. *See also* EDS reply 6-7.

[804] IBM comments at 8-9.

[805] *See* Ad Hoc petition at 12-13; ITAA petition at 5-7; IBM reply at 3-4.

[806] Ad Hoc petition at 17-18, citing Report of the Senate Committee on Commerce, Science, and Transportation on the *Telecommunications Competition and Deregulation Act of 1995*, S.Rep.No. 104-23, 104th Cong., 1st Sess. (March 30, 1995) at 28.

[807] Ad Hoc petition at 17-18.

[808] ITAA petition at 5 n. 9.

compete with common carriers and cautions that exempting them would skew the competitive marketplace.[809]

275. *Broadcasters*. On September 2, 1997, the Association of America's Public Television Stations and the Public Broadcasting Service (AAPTS)[810] asked the Commission to clarify the contribution obligations of broadcasters, including Instructional Television Fixed Service (ITFS) licensees. AAPTS urges the Commission to clarify that broadcasters that lease excess capacity to others for a fee are not "providers of interstate telecommunications" that are required to contribute to universal service. Alternatively, AAPTS contends that public broadcasters and ITFS licensees should be exempt from or receive a waiver of the contribution requirement. AAPTS states that educational, non-profit broadcasters sometimes lease excess transmission capacity to third parties to transmit educational programming, radio reading services for the visually impaired, and informational programming guides for television viewers.[811] AAPTS asserts that public broadcasters and ITFS licensees are engaged primarily in educational activities, rather than in providing telecommunications services, and should not be required to contribute to universal service. AAPTS also contends that such a requirement would undermine non-profit broadcasters' ability to fulfill their primary educational purposes.[812] No parties responded to AAPTS's petition.

3. Discussion

276. We affirm our decision that private service providers that provide interstate telecommunications on a non-common carrier basis must contribute to universal service, pursuant to our permissive authority over "providers of interstate telecommunications." In the *Order*, we found that the public interest requires private service providers that furnish interstate telecommunications to others for a fee to contribute to universal service on the same basis as common carriers. We concluded that this approach (1) was consistent with the principle of competitive neutrality because it will reduce the possibility that carriers with universal service obligations will be placed at an unfair competitive disadvantage in relation to carriers that do not have such obligations; (2) will avoid creating a disincentive for carriers to offer services on a common carrier basis; and (3) will broaden the funding base, thereby lessening contribution

[809] Bell Atlantic comments at 8-9. *See also* AT&T comments at 22.

[810] America's Public Television Stations and the Public Broadcasting Service Petition for Clarification and Exception or Waiver, filed Sept. 2, 1997 (AAPTS informal comments).

[811] AAPTS informal comments at 3.

[812] AAPTS informal comments at 7-12.

requirements of any particular class of telecommunications providers.[813] We affirm each of these findings.

277. Contrary to petitioners' arguments, we conclude that the Commission was not required to find that private networks constitute a significant means of bypassing the public switched telephone network before exercising our permissive authority to apply the universal service contribution requirements to non-common carriers.[814] Section 254(d) grants the Commission explicit and unambiguous authority to require "other providers of interstate telecommunications" to contribute to universal service if the public interest so requires. On this issue, the Joint Explanatory Statement merely states that this section "preserves the Commission's authority to require all providers of interstate telecommunications to contribute, if the public interest requires it to preserve and advance universal service."[815] There is no mention of a network bypass requirement in either the Act or the Joint Explanatory Statement. Thus, we find that the plain language of section 254(d) allows the Commission to require non-common carriers to contribute if the Commission concludes that doing so serves the public interest and furthers the goals of universal service. We conclude, however, for the reasons discussed below that we should not exercise our permissive authority to require systems integrators, broadcasters, and non-profit schools, universities, libraries, and rural health care providers to contribute to universal service.

278. *Systems Integrators.* We are persuaded by systems integrators' arguments that the public interest would not be served if we were to exercise our permissive authority to require entities that do not provide services over their own facilities[816] and are non-common carriers that obtain a *de minimis* amount of their revenues from the resale of telecommunications to contribute to universal service. Systems integrators provide integrated packages of services and products that may include, for example, the provision of computer capabilities, data processing, and telecommunications.[817] Systems integrators purchase telecommunications from telecommunications carriers and resell those services to their customers. They do not purchase unbundled network elements from telecommunications carriers and do not own any physical components of the telecommunications networks that are used to transmit systems integration

[813] *Order*, 12 FCC Rcd at 9183-9184.

[814] *See* Ad Hoc petition at 17-18.

[815] Joint Explanatory Statement at 131.

[816] We interpret the phrase "own facilities" to mean exclusive use of any physical components of the telecommunications network that are used to transmit systems integration customers' information for a period of time. *See Order*, 12 FCC Rcd at 8861-8866.

[817] *See* Ad Hoc petition at 11-12.

customers' information. In other words, systems integrators provide telecommunications solely through reselling another carrier's service. We conclude that systems integrators that satisfy these criteria, as discussed below, should not be required to contribute to the federal universal service support mechanisms.

279. In our view, systems integrators that obtain a *de minimis* amount of their revenues from the resale of telecommunications do not significantly compete with common carriers that are required to contribute to universal service. Systems integrators are in the business of integrating customers' computer and other informational systems, not providing telecommunications. Occasionally, systems integrators may provide interstate telecommunications along with their traditional integration services, but the provision of telecommunications is incidental to their core business. Systems integration customers who receive telecommunications from systems integrators choose systems integrators for their systems integration expertise, not for their competitive provision of telecommunications.

280. In determining what constitutes a *de minimis* amount of revenues, we could compare the amount of revenues derived from telecommunications to overall business revenues,[818] revenues derived from systems integration,[819] or revenues derived from systems integration contracts that also contain telecommunications.[820] We conclude that the second approach, telecommunications revenues relative to systems integration revenues, is the best method to determine whether systems integrators derive a *de minimis* amount of revenues from telecommunications. Overall business revenues are irrelevant to the determination of whether telecommunications revenues constitute a small part of the systems integration business. Similarly, evaluating only systems integration contracts that contain telecommunications will not provide an accurate account of the systems integration business as a whole. IBM and EDS suggest that *de minimis* should be defined as revenues that are less than five percent of systems integration revenues.[821] Based on this record, we conclude that systems integrators' telecommunications revenues will be considered *de minimis* if they constitute less than five percent of revenues derived from providing systems integration services. A systems integrator

[818] *See* Letter from Randolph J. May, EDS, to Magalie Roman Salas, FCC, dated December 18, 1997; Letter from Steven W. Stewart, IBM, to Magalie Roman Salas, FCC dated December 18, 1997.

[819] IBM states that telecommunications revenues represent less than five percent of its systems integration revenues. Letter from Steven W. Stewart, IBM, to Magalie Roman Salas, FCC dated December 18, 1997. EDS states that telecommunications revenues represent less than five percent of its systems integration revenues. Letter from Randolph J. May, EDS, to Magalie Roman Salas, FCC, dated December 18, 1997.

[820] Letter from Randolph J. May, EDS, to Magalie Roman Salas, FCC, dated December 18, 1997.

[821] *See* Letter from Steven W. Stewart, IBM, to Magalie Roman Salas, FCC dated December 18, 1997. Letter from Randolph J. May, EDS, to Magalie Roman Salas, FCC, dated December 18, 1997.

would not be required to file a Universal Service Worksheet if, over the requisite reporting period, its total revenues derived from telecommunications represent less than five percent of its total revenues derived from systems integration. Systems integrators that derive more than a *de minimis* amount of revenues from telecommunications will be required to contribute to the federal universal service support mechanisms and comply with universal service reporting requirements. We conclude that the limited nature of this exclusion from the obligation to contribute will ensure that systems integrators that are significantly engaged in the provision of telecommunications do not receive an unfair competitive advantage over common carriers or other carriers that are required to contribute to universal service.

281. To maintain the sufficiency of the support mechanisms, we find that systems integrators that are excluded from contribution requirements constitute end users for universal service contribution purposes.[822] In addition, systems integrators that obtain a *de minimis* amount of their revenues from the resale of telecommunications must notify the underlying facilities-based carriers from which they purchase telecommunications that they are excluded from the universal service contribution requirements. We conclude that excluding systems integrators that obtain a *de minimis* amount of their revenues from the resale of telecommunications from the obligation to contribute will not significantly reduce the universal service contribution base because revenues received by common carriers for minimal amounts of telecommunications provided to systems integrators will be included in the contribution bases of underlying common carriers. We anticipate that, by providing this exclusion from the obligation to contribute, the total contribution base will be reduced only by systems integrators' mark-up on telecommunications.

282. We disagree with ITAA's contention that, because systems integrators provide both basic telecommunications services as well as enhanced services for a single price, systems integrators are engaged exclusively in the provision of enhanced or information services.[823] Traditionally, the Commission has not regulated value-added networks (VANs)[824] because VANs

[822] Where systems integrators are treated as end users, those systems integrators will not be required to contribute to universal service based on revenues derived from the provision of interstate telecommunications to others. Revenues derived from the provision of telecommunications to systems integrators should be included in lines 34-47, where appropriate, of the Universal Service Worksheet by carriers providing telecommunications to systems integrators.

[823] Enhanced services are "services offered over common carrier transmission facilities used in interstate communications, which employ computer processing applications that act on the format, content, code, protocol or similar aspects of the subscriber's transmitted information; provide the subscriber additional, different, or restructured information; or involve subscriber interaction with stored information." 47 C.F.R. § 64.702(a).

[824] VANs provide services that combine protocol processing with basic transmission services. Basic services are regulated by the Commission and can be characterized as "a pure transmission capability over a communications path that is virtually transparent in terms of its interaction with customer supplied information." *See* Amendment to Sections 64.702 of the Commission's Rules and Regulations, *Report and Order*, 2 FCC Rcd 3072, 3074 (1987).

provide enhanced services. VAN offerings are treated as enhanced services because the enhanced component of the offering, i.e., the protocol conversions, "contaminates" the basic component of the offering, thus rendering the entire offering enhanced.[825] Citing the Commission's position that all enhanced services are information services,[826] ITAA argues that, because systems integrators offer information and telecommunications services for a single price, the information services "taint" the telecommunications services, thereby rendering the entire package an information service for purposes of applying the universal service contribution requirements. The Commission's treatment of VANs, however, does not imply that combining an enhanced service with a basic service for a single price constitutes a single enhanced offering.[827] The issue is whether, functionally, the consumer is receiving two separate and distinct services. A contrary interpretation would create incentives for carriers to offer telecommunications and non-telecommunications for a single price solely for the purpose of avoiding universal service contributions. Thus, a private service provider that provides information services along with a basic interstate voice-grade telecommunications service is not relieved of its statutory obligation to contribute to universal service. To the extent that a provider is offering basic voice-grade interstate telephone service and is not otherwise exempt, it is required to contribute to universal service.[828]

283. *Broadcasters.* The deadline for filing petitions for reconsideration in a notice and comment rulemaking proceeding are prescribed in section 405 of the Communications Act of 1934, as amended.[829] The Commission lacks discretion to waive this statutory requirement.[830] The filing deadline for petitions for reconsideration of the *Order* was July 17, 1997. Therefore, to the extent that AAPTS' petition, filed September 2, 1997, seeks reconsideration of the *Order*,

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[825] *See* Amendment to Sections 64.702 of the Commission's Rules and Regulations, *Report and Order*, 2 FCC Rcd 3072, 3075 (1987).

[826] *See* Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, *First Report and Order & Further Notice*, 11 FCC Rcd 21905 (1996).

[827] For example, if a reseller offers basic voice-grade telephone service with Internet service for one flat monthly fee, the fact that the reseller provides an enhanced service with a basic service for a single price does not render the basic voice service an enhanced service. In that instance, the enhanced service is not combined with the basic service into a single enhanced offering because, functionally, the consumer is receiving two separate and distinct services, voice-grade telephone service and Internet service.

[828] *See Recommended Decision* at para. 790. We base this decision pursuant to conclusions set forth in the May 8 *Order*. We will be reexamining those underlying conclusions pursuant to our Report to Congress.

[829] *See* 47 U.S.C. § 405(a).

[830] *See Virgin Islands Telephone Corp. v. FCC*, 989 F.2d 1231, 1237 (D.C. Cir. 1993); *Reuters Ltd. v. FCC*, 781 F.2d 946, 951-52 (D.C. Cir. 1986).

we will treat it as an informal comment.[831] We agree with AAPTS and reconsider, on our own motion, our determination that all providers of interstate telecommunications must contribute to universal service.[832] For the reasons described below, we find that the public interest would not be served if we were to exercise our permissive authority to require broadcasters, including ITFS licensees, that engage in non-common carrier interstate telecommunications to contribute to universal service.[833] In the *Order*, we found that, in order to ensure that our contribution rules do not confer a competitive advantage to non-common carriers, non-common carriers should contribute to universal service pursuant to our permissive authority over "other providers of interstate telecommunications." On further reconsideration, however, we agree with AAPTS that broadcasters do not compete to any meaningful degree with common carriers that are required to contribute to universal service because broadcasters primarily transmit video programming, a service that is not generally provided by common carriers. Moreover, we conclude that broadcasters' primary competitors for programming distribution are cable, OVS, and DBS providers. Because cable, OVS, and DBS providers are not required to contribute to universal service,[834] the exclusion from the obligation to contribute for broadcasters will ensure that broadcasters are not competitively disadvantaged in the video distribution industry by our contribution requirements. As broadcasters begin to offer digital television, however, they may choose to provide interstate telecommunications that are not used to distribute video programming. We will, therefore, monitor broadcasters' provision of interstate telecommunications on a non-common carrier basis. If we determine that broadcasters compete with common carriers that are required to contribute to universal service, we will revisit our exclusion of broadcasters from the contribution requirements.

284. *Non-profit Schools, Colleges,Universities, Libraries, and Health Care Providers.* We also find, on our own motion, that non-profit schools, colleges, universities, libraries, and health care providers should not be made subject to universal service contribution requirements. To the extent these non-profit entities provide interstate telecommunications on a non-common carrier basis, our rules require them to contribute to universal service, pursuant to our permissive

[831] 47 U.S.C. § 154(j).

[832] In light of pending petitions for reconsideration in this proceeding, the Commission retains jurisdiction to reconsider its own rules on its own motion. *See* 47 U.S.C. § 405, 47 C.F.R. § 1.108, and *Central Florida Enterprises, Inc. v. FCC*, 598 F.2d 37, 48, note 51 (D.C. Cir. 1978), *cert. dismissed*, 441 U.S. 957 (1979).

[833] Broadcasters that provide interstate telecommunications to others will be treated as end users and will not be required to contribute to universal service based on those revenues. Revenues derived from the provision of telecommunications to broadcasters should be included in lines 34-47, where appropriate, of the Universal Service Worksheet by carriers providing telecommunications to broadcasters.

[834] 47 C.F.R. § 54.703.

authority over "other providers of interstate telecommunications."[835] We conclude, however, that the public interest would not be served if we were to exercise our permissive authority to require these entities to contribute to universal service. Many of these entities will be eligible to receive support pursuant to sections 54.501(b), (c), and (d) and 54.601(a) and (b). We conclude that it would be counter-productive to the goals of universal service to require non-common carrier program recipients of support to contribute to universal service support because such action effectively would reduce the amount of universal service support they receive. In addition, we find that it would be inconsistent with the educational goals of the universal service support mechanisms to require colleges and universities to contribute to universal service. To maintain the sufficiency of the federal support mechanisms, we have determined to treat non-profit schools, colleges, universities, libraries, and health care providers as telecommunications end users for universal service contribution purposes.[836]

C. Providers of Bare Transponder Capacity

1. Background

285. Section 254(d) allows the Commission to require "other providers of interstate telecommunications" to contribute to universal service if the public interest so requires.[837] In the *Order*, the Commission found that the public interest requires "other providers of interstate telecommunications," which include entities that provide interstate telecommunications on a non-common carrier basis, to contribute to universal service because "other providers of interstate telecommunications" compete with telecommunications carriers that must contribute to universal service.[838]

2. Pleadings

286. Several commenters request that the Commission clarify that satellite providers are not required to contribute to universal service on the basis of revenues derived from the lease of bare transponder capacity.[839] AT&T, however, asserts that, because satellite providers can

[835] *Order*, 12 FCC Rcd at 9183-9184.

[836] Where such non-profit entities are treated as end users, those entities will not be required to contribute to universal service based on revenues derived from the provision of interstate telecommunications to others. Revenues derived from the provision of telecommunications to such entities should be included in lines 34-47, where appropriate, of the Universal Service Worksheet by carriers providing telecommunications to such entities.

[837] 47 U.S.C. § 254(d).

[838] *Order*, 12 FCC Rcd at 9183.

[839] *See, e.g.*, Columbia petition at 5-6; GE Americom petition at 3, 9-12; Loral comments at 2-3, 9; PanAmSat

offer bare transponder capacity pursuant to tariffs, leasing bare transponder capacity constitutes the provision of telecommunications. AT&T, therefore, argues that leasing bare transponder capacity should be subject to the universal service contribution requirements.[840]

287. GE Americom urges the Commission to find that satellite providers must contribute to universal service only to the extent that they provide interstate telecommunications on a common carrier basis.[841] To support its assertion, GE Americom points out that the Commission stated in the *Order* that ". . . satellite and video service providers must contribute to universal service only to the extent that they are providing interstate telecommunications services."[842] Several commenters argue that a contrary finding would be inequitable because leasing bare transponder capacity does not directly involve the public switched telephone network.[843] PanAmSat contends that requiring contribution by bare transponder providers is inequitable because such providers would be ineligible to receive universal service support.[844]

3. Discussion

288. We affirm the Commission's finding that satellite providers that provide interstate telecommunications services or interstate telecommunications to others for a fee must contribute to universal service. We conclude that GE Americom's assertion that the Commission found that satellite and video service providers need only contribute to universal service if they are operating as common carriers misconstrues that passage of the *Order*. As discussed in the *Order*, the sentence in section 254(d) that requires all telecommunications carriers to contribute to universal service applies only to common carriers. Thus, the Commission concluded that only common carriers fall within the category of mandatory contributors. Accordingly, satellite operators that provide transmission services on a common carrier basis are mandatory contributors to the universal service support mechanisms. Pursuant to section 254(d), the Commission also exercised its permissive authority to impose contribution obligations on other providers of interstate telecommunications. The Commission's statement that satellite providers must contribute to universal service only to the extent that they are providing interstate telecommunications services described satellite providers' mandatory contribution obligation as

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comments at 3-4; Vyvx reply at 3-4.

[840] AT&T comments at 23. *See also* Bell Atlantic comments at 8-9.

[841] GE Americom petition at 6-7. *See also* Vyvx reply at 3-4.

[842] *Order*, 12 FCC Rcd at 9176.

[843] Columbia petition at 5-6; GE Americom petition at 6; Loral comments at 4-5; PanAmSat comments at 2.

[844] PanAmSat comments at 3.

set forth in section 254(d).[845] The Commission further concluded that satellite providers that provide interstate telecommunications on a non-common carrier basis must contribute to universal service as "other providers of interstate telecommunications" under section 254(d). The obligation of satellite providers to contribute to universal service as mandatory contributors does not relieve them of their obligation to contribute as other providers of interstate telecommunications. Therefore, if a satellite provider offers interstate telecommunications on a common carrier or non-common carrier basis, it must contribute to universal service, unless otherwise excluded.

289. We are not persuaded by petitioners' assertions that satellite providers that are ineligible to receive universal service support should not be required to contribute to universal service. As discussed in the *Order*, section 254 does not limit contributions to eligible telecommunications carriers.[846] Section 254(b)(4) provides that the Commission should be guided by the principle that "all providers of telecommunications services" should contribute to universal service. Because not all providers of telecommunications services may be eligible to receive universal service support, we believe that the plain text of the statute contemplates that the universe of contributors will not necessarily be identical to the universe of potential recipients.

290. Several parties ask us to clarify that satellite providers do not transmit information to the extent that they merely lease bare transponder capacity to others. According to PanAmSat,

> [w]hen a satellite operator enters into a bare transponder agreement with a customer, the satellite operator is merely providing its customer with the exclusive right to transmit to a *specified piece of hardware on the satellite*. That, essentially, is the extent of the operator's obligation.[847]

Based on the descriptions by PanAmSat and other commenters of the very limited activity that satellite providers engage in when they lease bare transponder capacity, it appears that, for

[845] *See Order*, 12 FCC Rcd at 9176.

[846] *Order*, 12 FCC Rcd at 9188.

[847] PanAmSat comments at 4. PanAmSat further notes that the party leasing bare transponder capacity (or its customer) is required by Commission rules to obtain a separate earth station license to transmit to the satellite. *Id*. *See also* GE Americom petition at 10 ("satellite companies [that lease bare transponder capacity] . . . make available and maintain the network component consisting of a repeater at the spacecraft. . . . The space segment user must configure and manage the transmission path for itself"); Loral comments at 6; Columbia reply at 1-2; Vyvx reply at 2 ("Vyvx or its affiliates engage in various non-telecommunications activity, including the provision of customer premises equipment, switches, and most relevant here, bare satellite space segment or earth stations. In each case, the customer uses these network elements, generally along with others obtained elsewhere, to design and operate a transmission path").

purposes of the contribution requirements under section 254 of the Act, satellite providers do not transmit information when they lease bare transponder capacity. Satellite providers, therefore, are not required to contribute to universal service on the basis of revenues derived from the lease of bare transponder capacity. We emphasize that this conclusion is premised on the accuracy of the uncontested representations by satellite providers of what is involved in the lease of bare transponder capacity. We might reconsider our determination if presented with different factual evidence. Satellite providers must, however, contribute to universal service to the extent they provide interstate telecommunications services and interstate telecommunications.

291. We are not persuaded by AT&T's assertion that, because the lease of bare transponder capacity may be provided pursuant to tariff, it necessarily constitutes the provision of telecommunications. Because the definition of "telecommunications" was added to the Act in 1996, the fact that bare transponder capacity may be provided or was provided pursuant to tariff is not dispositive.

D. Universal Service Report to Congress

292. Congress has instructed the Commission to review our decisions regarding who is required to contribute to the federal universal service support mechanisms and to submit our findings to Congress.[848] Consistent with the statutory deadline, the Commission will submit such a report to Congress by April 10, 1998.

E. *De Minimis* Exemption

1. Background

293. Section 254(d) states that the "Commission may exempt a carrier or class of carriers from this [contribution] requirement if the carrier's telecommunications activities are limited to such an extent that the level of such carrier's contribution ... would be *de minimis*."[849] Based on language in the Joint Explanatory Statement, the Commission found that the *de minimis* exemption should only exempt contributors whose contributions are less than the Administrator's administrative costs of collection.[850] The Commission found that, if a

[848] Pub. L. 105-119, 111 Stat. 2440 (approved November 26, 1997).

[849] 47 U.S.C. § 254(d).

[850] *Order*, 12 FCC Rcd at 9187. Specifically, the Joint Explanatory Statement provides that "this [*de minimis*] authority would only be used in cases where the administrative cost of collecting contributions from a carrier or carriers would exceed the contribution that carrier would otherwise have to make under the formula for contributions selected by the Commission." Joint Explanatory Statement at 131 (1996).

contributor's annual contribution would be less than $100.00, it is not required to contribute to universal service or comply with Commission Worksheet filing requirements.[851] Contributors that do not qualify for the *de minimis* exemption must file a semi-annual Universal Service Worksheet.[852]

2. Pleadings

294. Several petitioners seek reconsideration of the Commission's interpretation of the *de minimis* exemption. Ad Hoc petitions the Commission to include a contributor's costs of complying with contribution reporting requirements when setting the *de minimis* threshold.[853] Ad Hoc asserts that, because some contributors do not provide interstate telecommunications on a stand-alone basis and charge a single monthly fee for a package of services, it can be costly and administratively difficult to separate interstate and intrastate end-user telecommunications revenues by the category breakdowns that are required by the Worksheet.[854] Ad Hoc states that the *de minimis* exemption should encompass a contributor whose contribution would be less than the combined administrative expenses of the Administrator and the contributor, including costs of separating and identifying revenues in accordance with the Worksheet. ITAA adds that the Administrator's administrative costs of collecting contributions should be higher than $100.00 because the Administrator will have to expend significant funds to identify private service providers.[855] Ozark contends that all carriers that are not "eligible telecommunications carriers" should be eligible for the *de minimis* exemption.[856]

3. Discussion

295. Based on petitioners' arguments, we reconsider our previous determination and conclude that the *de minimis* exemption should be based on the Administrator's costs of collecting contributions and contributors' costs of complying with the reporting requirements. In reaching its finding that the *de minimis* exemption should only exempt contributors whose

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[851] *Order*, 12 FCC Rcd at 9187.

[852] 47 C.F.R. § 54.711.

[853] Ad Hoc petition at 13-14. *See also* ITAA petition at 6-7. ITAA alleges that all private service providers will incur significant costs to create new accounting systems to comply with reporting requirements.

[854] Ad Hoc petition at 12.

[855] ITAA petition at 7.

[856] Ozark petition at 5.

contributions would be less than the Administrator's administrative costs of collection,[857] the Commission looked to the Joint Explanatory Statement for guidance. Specifically, the Joint Explanatory Statement observes that "this [*de minimis*] authority would only be used in cases where the administrative cost of *collecting* contributions from a carrier or carriers would exceed the contribution that carrier would otherwise have to make under the formula for contributions selected by the Commission."[858] In the *Order*, the Commission found that this statement indicated that the Commission should look only to the Administrator's costs of *collecting* contributions and not the carrier's cost of determining contribution obligations. We find, however, that "the administrative cost of collecting contributions" can include both the Administrator's as well as contributors' administrative costs. We agree with Ad Hoc that the public interest would not be served if compliance costs associated with contributing to universal service were to exceed actual contribution amounts. We decline to exclude from the contribution requirement all entities that claim compliance costs in excess of their contribution amounts, however, based on our concern that such a rule may encourage contributors to report artificially high administrative compliance costs in order to avoid their contribution obligation. Rather, we adopt a substantially increased *de minimis* threshold that takes into account contributors' compliance costs in addition to the Administrators' administrative costs of collection based on our view that this increased threshold will accommodate a reasonable level of reporting compliance costs for all contributors.

296. We also agree with ITAA that the contribution collection costs incurred by the Administrator in many cases will exceed $100 per contributor. We find that in determining the Administrator's administrative costs, we should include the costs associated with identifying contributors, processing and collecting contributions, and providing guidance on how to complete the Universal Service Worksheet.

297. Therefore, we conclude that the *de minimis* contribution threshold should be raised to $10,000. If a contributor's annual contribution would be less than $10,000, it will not be required to contribute to universal service. We find that this exclusion will reduce significantly the Administrator's collection costs. Based on Universal Service Worksheets, we estimate that approximately 1,600 entities will qualify for the *de minimis* exemption. Therefore, the Administrator will have to collect and process 1,600 fewer Worksheets and will have to identify and collect contributions from 1,600 fewer entities. Additionally, by exempting entities whose annual contributions would be less than $10,000 from contribution and Worksheet reporting requirements, we anticipate that we will reduce reporting burdens on many small entities.

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[857] *Order*, 12 FCC Rcd at 9187.

[858] *Order*, 12 FCC Rcd at 9187, *quoting* Joint Explanatory Statement at 131 (1996) (emphasis added).

298. To maintain the sufficiency of the universal service support mechanisms, we conclude that entities that qualify for the *de minimis* exemption should be considered end users for Universal Service Worksheet reporting purposes. Entities that resell telecommunications and qualify for the *de minimis* exemption must notify the underlying facilities-based carriers from which they purchase telecommunications that they are exempt from contribution requirements and must be considered end users for universal service contribution purposes. Thus, underlying carriers should include revenues derived from providing telecommunications to entities qualifying for the *de minimis* exemption in lines 34-47, where appropriate, of their Universal Service Worksheets.

F. Requirement that CMRS Providers Contribute to State Universal Service Support Mechanisms

1. Background

299. In 1993, Congress amended the Communications Act to include section 332. Section 332(c)(3)(A) of the Act provides that:

> . . . no State or local government shall have any authority to regulate the entry of or the rates charged by any commercial mobile service or private mobile service, except that this paragraph shall not prohibit a State from regulating the other terms and conditions of commercial mobile services. Nothing in this paragraph shall exempt providers of commercial mobile services (where such services are a substitute for land line telephone exchange service for a substantial portion of the communications within such State) from requirements imposed by a State commission on all providers of telecommunications services necessary to ensure the universal availability of telecommunications services at affordable rates.[859]

Subsequently, in 1996, Congress enacted a new section 254. Section 254(f) of the Act provides that "[e]very telecommunications carrier that provides intrastate telecommunications services shall contribute, on an equitable and nondiscriminatory basis, in a manner determined by the State to the preservation and advancement of universal service in that State."[860] In earlier stages of this proceeding, several commenters argued that the second sentence of section 332(c)(3)(A) prohibits states from requiring CMRS providers operating within a state to contribute to state universal service support programs unless the CMRS provider's service is a substitute for land line service in a substantial portion of the state.[861] In the *Order*, the Commission agreed with the

[859] 47 U.S.C. § 332(c)(3)(A).

[860] 47 U.S.C. § 254(f).

[861] *See Order*, 12 FCC Rcd at 9590.

Joint Board that section 332(c)(3)(A) "does not preclude states from requiring CMRS providers to contribute to state support mechanisms."[862] The Commission also noted that, although the California PUC has required CMRS providers to contribute to the California state universal service mechanisms, a Connecticut state court ruled that section 332(c)(3) prohibits Connecticut from assessing contributions against CMRS providers for Connecticut's universal service programs.[863] The Commission rejected the argument that interpreting section 332(c)(3)(A) and section 254(f) violates the notice and comment requirements of the Administrative Procedure Act (APA), noting that an exception to the notice requirement exists for interpretive rules and general statements of policy.[864]

2. Pleadings

300. Several CMRS providers have requested that the Commission reconsider its conclusion that section 332(c)(3)(A) does not preclude states from requiring CMRS providers to contribute to state universal service support mechanisms. They argue that, except when a CMRS provider's service is a substitute for land line service in a substantial portion of the state, section 332(c)(3)(A) prohibits states from requiring providers of commercial mobile services to contribute to state support mechanisms.[865] These petitioners also argue that the *Order* conflicts with Congress's express purpose in adopting the 1993 amendments to section 332, which was to provide that CMRS offerings are to be considered exclusively interstate for purposes of government regulation.[866] According to AirTouch, section 254(f)'s command that "every telecommunications provider that provides intrastate telecommunications services . . . contribute" to state universal service mechanisms should not apply to CMRS providers.[867] Commenters also assert that the specific provisions of section 332(c)(3)(A) cannot be superseded by section 254(f)'s general grant of authority to the states.[868] ProNet argues that paging carriers should be

[862] *Order*, 12 FCC Rcd at 9181.

[863] *Id.*, *comparing* California PUC, Decision 94-09-065, 56 CPUC2d 290 *with Metro Mobile CTS v. Connecticut Dept. of Public Utility Control*, No. CV-95-05512758 (Conn. Super. Ct., Judicial Dist. of Hartford-New Britain, Dec. 9, 1996).

[864] *Order*, 12 FCC Rcd at 9182, *citing* 5 U.S.C. § 553(b)(3)(A).

[865] *See* AirTouch petition at 13; CTIA petition at 9; Comcast Cellular/Vanguard Cellular joint petition at 2-9; Nextel petition at 5-12; ProNet petition at 9-13. *See also* 360° Communications comments at 2-7; PCIA comments at 3-10; AMSC comments at 3-4.

[866] *See, e.g.*, AirTouch petition at 15; Nextel petition at 9; ProNet petition at 11.

[867] *See* AirTouch petition at 15.

[868] *See, e.g.*, AirTouch petition at 15-16; Comcast Cellular/Vanguard Cellular petition at 10-12.

exempt from state universal service fund contributions because paging services are not substitutes for land line exchange services. ProNet also argues that, because there was no notice that issues regarding state universal service funds would be considered in this proceeding, the Commission's decision on this issue violated the notice and comment requirements of the APA.[869] Some petitioners further request that, if the Commission affirms its decision, it ensure that state universal service requirements are consistent with federal policy, *i.e.*, that they do not amount to rate regulation or become effective barriers to entry, and that the Commission establish a framework that would prevent duplicative contributions.[870]

3. Discussion

301. The Commission recently addressed, in *Pittencrieff Communications, Inc.*,[871] the issue of whether section 332(c)(3)(A) limits the ability of states to require CMRS providers to contribute to state universal service support mechanisms. The issues raised on reconsideration in this proceeding were resolved in *Pittencrieff*. In *Pittencrieff*, the Commission explicitly affirmed the finding made in the *Order* that section 332(c)(3)(A) does not preclude states from requiring CMRS providers to contribute to state support mechanisms.[872] The Commission concluded that a state's requirement that CMRS providers contribute on an equitable and nondiscriminatory basis to its universal service support mechanisms is neither rate nor entry regulation but instead is a permissible regulation on "other terms and conditions" under section 332(c)(3)(A).[873] The Commission also stated:

> We believe [the second sentence of section 332(c)(3)(A)] applies only to a state's authority to impose requirements that would otherwise constitute regulation of rates or entry. In that situation, a state would have to comply with section 332(c)(3) by showing that CMRS is 'a substitute for land line telephone exchange service for a substantial portion of the communications within such State.' The state is not required to

[869] ProNet petition at 12-13.

[870] *See, e.g.*, Nextel petition at 18-20; CTIA petition at 6-10; Comcast Cellular/Vanguard Cellular joint petition at 19-20. *See also* CTIA opposition at 9-12; AMSC comments at 4; GTE comments at 20.

[871] Pittencrieff Communications, Inc., *Memorandum Opinion and Order*, File No. WTB/POL 96-2, FCC 97-343 (rel. October 2, 1997) (*recon. pending*) (*Pittencrieff*). In addition, three parties, Airtouch, CTIA, and Sprint Spectrum, have filed Petitions for Review of *Pittencrieff* with the U.S. Court of Appeals, D.C. Circuit.

[872] *See also Mountain Solutions, Inc. v. State Corporation Commission of the State of Kansas*, 966 F.Supp. 1043 (D. Kan. 1997) (refuting Connecticut state court decision in the *Metro Mobile* decision) (*Mountain Solutions*). This case is on appeal in the Tenth Circuit.

[873] *Pittencrieff* at paras. 15-22.

> demonstrate that CMRS is a substitute for land line service, however, when it requires a CMRS provider to contribute to the state's universal service mechanisms on an equitable and nondiscriminatory basis, in compliance with section 254(f).[874]

Finally, the Commission noted that, if section 332(c)(3) were interpreted to conflict with section 254(f), section 254(f) would take precedence over section 332(c)(3).[875] Section 254(f), which requires all telecommunications carriers that provide intrastate telecommunications services, including CMRS providers, to contribute to state universal service programs, was enacted later in time and speaks directly to the contribution issue.[876] Reconsideration petitions to this proceeding do not raise issues that were not addressed in *Pittencrieff*. We find that our order in *Pittencrieff* resolves the issues that have been raised by the reconsideration petitions in this proceeding and we find no basis in this record for reaching a different determination.

302. We do not anticipate that state contribution requirements will violate section 253. Section 253(a) prohibits state and local governments from enacting any statute, regulation or legal requirement that prohibits or has the effect of prohibiting the ability of any entity to provide any interstate or intrastate telecommunications service.[877] Section 253(b), among other things, protects state authority to impose universal service requirements, as long as they are done "on a competitively neutral basis and consistent with section 254 . . . ."[878] Section 254(f) of the Act allows states to adopt universal service regulations "not inconsistent with the Commission's rules . . . ."[879] To demonstrate that state universal service contribution requirements for CMRS providers violate section 253, there must be a showing that the state universal service programs act as a barrier to entry for CMRS providers and are not competitively neutral.

303. We reject the argument that state universal service mechanisms should not apply to CMRS providers because CMRS services should be considered jurisdictionally "interstate." Data submitted to the Commission by CMRS carriers in connection with their TRS reporting for the year 1995 reveal that interstate revenues amounted to only 5.6 percent of total revenues for cellular and personal communications service carriers, and 24 percent of total revenues for

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[874] *Pittencrieff* at para. 5. *See also Mountain Solutions*, 966 F.Supp. at 1049.

[875] *Pittencrieff* at para. 26.

[876] *Pittencrieff* at para. 26.

[877] 47 U.S.C. § 253(a).

[878] 47 U.S.C. § 253(b).

[879] 47 U.S.C. § 254(f).

paging and other mobile service carriers.[880] Thus, we find that it would be inappropriate to classify all CMRS services as "interstate." CMRS providers that offer intrastate CMRS services cannot shield themselves from state universal service contributions.

304. We also reject ProNet's argument that the Commission's consideration of this issue in the *Order* violates the notice provisions of the APA. The general requirement of notice contained in section 553(b) of the APA does not apply "to interpretive rules, general statements of policy, or rules of agency organization, procedure or practice . . . ."[881] Although the courts have recognized that the distinction between those agency rules that are subject to the notice requirement and those that are exempt is not always easy to discern,[882] the relevant law here is clear. As the U.S. Court of Appeals for the D.C. Circuit stated:

> Ultimately, an interpretive statement simply indicates an agency's reading of a statute or a rule. It does not intend to create new rights or duties, but only "'reminds' affected parties of existing duties." A statement seeking to interpret a statutory or regulatory term is, therefore, the quintessential example of an interpretive rule.[883]

At issue here is the correct interpretation of the second sentence of section 332(c)(3)(A) of the Act. The Commission's statement on this issue, as expressed in the *Order*, created neither new rights or new obligations that did not exist before. Therefore, the Commission did not violate the notice provisions of the APA by addressing this issue.

305. ProNet argues that, because the Commission's interpretation of the statute "has immediate, direct impact on universal service contributions at the state level," it cannot be exempt from the APA's notice requirement, and that notice was required because "the Commission's interpretation of Sections 332(c)(3) and 254(f) of the Act operates as an instruction to the states regarding their ability to fund universal services, and creates immediate

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[880] *See Telecommunications Industry Revenue: TRS Fund Worksheet Data*, Industry Analysis Division, Common Carrier Bureau, December 1996.

[881] 5 U.S.C. § 553(b)(A).

[882] *See, e.g., American Hospital Association v. Bowen*, 834 F.2d 1037, 1045 (D.C. Cir. 1987) ("[T]he spectrum between a clearly interpretive rule and a clearly substantive one is a hazy continuum"); *General Motors Corp. v. Ruckelshaus*, 742 F.2d 1561, 1565 (D.C. Cir. 1984) (distinction is "enshrouded in considerable smog").

[883] *Orengo Caraballo v. Reich*, 11 F.3d 186, 195 (D.C. Cir. 1993), *quoting General Motors Corp. v. Ruckelshaus*, 742 F.2d at 1565. *Accord, National Medical Enterprises, Inc. v. Shalala*, 43 F.3d 691, 697 (D.C. Cir. 1995) ("[I]nterpretive rules are those that merely clarify or explain existing laws or regulations").

burdens on CMRS carriers . . . ."[884] We disagree. No burdens on CMRS carriers are created as a result of the Commission's statement on this issue in the *Order*. Individual states must determine whether to exercise their authority under section 254(f) to require universal service contributions from CMRS carriers. Even if our interpretation had a substantial impact, the mere fact that a rule may have a substantial impact, however, "does not transform it into a legislative rule."[885] If not, the exemption for interpretative rules from the APA's notice requirement would have little practical application. We therefore reaffirm our conclusion that the Commission's interpretation of sections 332(c)(3)(A) and 254(f) in the *Order* is exempt from the notice requirement of the APA.

G. Recovery of Universal Service Contributions by CMRS Providers

1. Background

306. In the *Order*, the Commission determined to continue its historical practice of permitting carriers to recover the amount of their contributions to the federal universal service support mechanisms through rates for interstate services only.[886] This determination was based on a desire to ensure the continued affordability of residential dialtone service, to promote comity between the federal and state governments in light of the fact that the Joint Board had not reached a recommendation as to whether to include intrastate revenues in the base for the high cost and low income mechanisms, and to "maintain the traditional federal-state partnership."[887] The Commission also noted that limiting the recovery of contributions to revenues from interstate services would "avoid any of the asserted difficulties raised by commenters such as NYNEX that oppose assessing contributions from interstate and intrastate revenues because some carriers may face difficulty recovering contributions based on intrastate revenues."[888]

2. Pleadings

307. In its petition for reconsideration and clarification, CTIA requests that the Commission make clear that CMRS providers will be permitted to recover their universal service

[884] ProNet petition at 13 n. 27.

[885] *American Postal Workers Union v. United States Postal Service*, 707 F.2d 548, 560 (D.C. Cir. 1983), *cert. denied*, 465 U.S. 1100, 104 S.Ct. 1594, 80 L.Ed.2d 126 (1984).

[886] *Order*, 12 FCC Rcd at 9198-9199.

[887] *Order*, 12 FCC Rcd at 9198-9199.

[888] *Order*, 12 FCC Rcd at 9199.

contributions through rates on all their services.[889] In a similar vein, Comcast Cellular and Vanguard Cellular jointly argue that, because wide area wireless traffic cannot be easily classified as intrastate or interstate, the Commission should recognize CMRS as a wholly interstate service and treat CMRS revenues and traffic accordingly.[890] CTIA asserts that, because of the mobile nature of most CMRS communications and the technical configuration of many CMRS systems, it is difficult to determine exactly when users are using the systems for interstate telecommunications or intrastate telecommunications.[891] In particular, CTIA argues that CMRS service areas do not correspond with state boundaries, and that conventional assumptions about telecommunications traffic are not applicable to CMRS because CMRS antennas often cover territory in more than one state.[892] CTIA also claims that to the extent that the Commission's decision was based on a desire to avoid the legal and political issues involved in requiring carriers to ask states to alter intrastate rates, this problem does not exist for CMRS providers because states are precluded by section 332(c)(3) from engaging in rate regulation over CMRS services.[893]

308. Arch, a paging carrier, argues that the two reasons given for the Commission's decision -- avoiding increases in charges for basic residential dialtone service and federal/state comity -- afford no basis for "precluding paging carriers from passing through universal service obligations to 'intrastate' service customers."[894] Arch claims that, because paging does not constitute basic residential dialtone service, allowing paging carriers to pass through universal service contributions to all customers will have no impact on rates for basic services. Arch also argues that comity is not a concern because states have no jurisdiction over paging rates.[895] Arch expresses concern that cellular and PCS carriers, which compete with paging carriers but whose customers might more readily be regarded as "interstate" customers, would be given an unfair competitive advantage if paging carriers were not allowed to recover contributions from both interstate and intrastate services.[896]

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[889] CTIA petition at 10. *Accord*, Arch comments at 4-5. *See also* CTIA petition for expedited consideration 4-5.

[890] Comcast Cellular/Vanguard Cellular joint petition at 10.

[891] CTIA petition at 13-18.

[892] CTIA petition at 13-14.

[893] CTIA petition at 10-11.

[894] Arch comments at 4-5.

[895] Arch comments at 4.

[896] Arch comments at 6.

3. Discussion

309. The Commission permitted contributors to recover contributions to the federal universal service support mechanisms through rates on interstate services, in order to ensure the continued affordability of residential dialtone service and to promote comity between the federal and state governments.[897] We agree with petitioners that these considerations do not apply to CMRS providers. Because section 332(c)(3) of the Act alters the "traditional" federal-state relationship with respect to CMRS by prohibiting states from regulating rates for intrastate commercial mobile services, allowing recovery through rates on intrastate as well as interstate CMRS services would not encroach on state prerogatives. Further, allowing recovery of universal service contributions through rates on all CMRS services will avoid conferring a competitive advantage on CMRS providers that offer more interstate than intrastate services. If CMRS carriers were permitted to recover contributions through their interstate services only, carriers that offer mostly intrastate services would be required to recover a higher percentage of interstate revenues from their customers than carriers that offer mostly interstate services. We therefore will permit CMRS providers to recover their contributions through rates charged for all their services.

H. Technical Corrections Regarding Calculation of Contribution Factors

1. Background

310. In the *NECA Report and Order*, the Commission established an administrative process by which quarterly universal service contribution factors will be calculated.[898] The Commission stated that the Universal Service Administrative Company (USAC) would be responsible for processing Universal Service Worksheets, FCC Form 457s, forms that require contributors to list their end-user telecommunications revenues.[899] The Commission also stated that the USAC, Schools and Libraries Corporation, and Rural Health Care Corporation must submit their projections of demand and administrative expenses for their respective programs to the Commission at least 60 days before the start of each quarter.[900] The Commission further stated that it would publish those projections and the contribution factors in a Public Notice and that USAC could not use those contribution factors to calculate individual contributions until

[897] *Order*, 12 FCC Rcd at 9198-9199, 9203-9204.

[898] *NECA Report and Order* at paras. 47-48.

[899] *NECA Report and Order* at para. 43.

[900] *NECA Report and Order* at para. 47.

those factors were deemed approved by the Commission.[901] The contribution factors will be deemed approved if the Commission takes no action within 14 days of the publication of the Public Notice announcing the contribution factors.[902] These findings were codified in section 54.709 of the Commission's rules.[903]

2. Discussion

311. Consistent with the Commission's findings in the *NECA Report and Order*, we issue a technical clarification to section 54.709(a) of our rules. We clarify that the Commission, not USAC, shall be responsible for calculating the quarterly universal service contribution factors. We also clarify that, based on Universal Service Worksheets, USAC must submit the total contribution bases, interstate and international and interstate, intrastate, and international end-user telecommunications revenues, to the Commission at least sixty days before the start of each quarter.

I. NECA/USAC Affiliate Transactions Rules

1. Background

312. In the *NECA Report and Order*, the Commission directed NECA to create an independent subsidiary, USAC, to administer temporarily portions of the new federal support mechanisms.[904] The Commission also stated that transactions between NECA and USAC will be subject to the Commission's affiliate transactions rules.[905] The affiliate transactions rules, established by the Commission in the *Joint Cost Order*,[906] apply to local exchange carriers subject to the Commission's Part 32, Uniform System of Accounts (USOA).[907] The affiliate

[901] *NECA Report and Order* at para. 48.

[902] *NECA Report and Order* at para. 48.

[903] 47 C.F.R. § 54.709.

[904] *NECA Report and Order* at para. 1.

[905] *NECA Report and Order* at para. 74.

[906] *See* Separation of Costs of Regulated Telephone Service from Costs of Nonregulated Activities, *Report and Order*, CC Docket No. 86-111, 2 FCC Rcd 1298 (1987) (*Joint Cost Order*), *modified on recon.*, 2 FCC Rcd 6283 (1987) (*Joint Cost Reconsideration Order*), *modified on further recon.*, 3 FCC Rcd 6701 (1988) (*Further Reconsideration Order*), *aff'd sub nom. Southwestern Bell Corp. v. FCC*, 896 F.2d 1378 (D.C. Cir. 1990).

[907] 47 C.F.R. Part 32.

transactions rules govern how LECs are to value and record transactions with affiliates in their regulated books of account.[908] The affiliate transactions rules contain several types of valuation methods for these transactions.[909] The Commission established the affiliate transactions rules to prevent abuses that may occur when a regulated carrier engages in transactions with its nonregulated affiliates.

2. Discussion

313. NECA is not a local exchange carrier subject to Part 32 and USAC is not a nonregulated affiliate engaged in a competitive business. NECA and USAC, however, must file annual cost accounting manuals with the Commission identifying their administrative costs.[910] We find that it is not practical to require NECA to follow the affiliate transactions rules as they are applied to local exchange carriers subject to Part 32. Because NECA does not provide services pursuant to tariff and does not provide more than 50 percent of its services to third parties, if NECA were subject to the affiliate transactions rules, it would be required to determine the fair market value of the services provided to USAC.[911] We find that the burden of making such a determination outweighs the benefit of imposing this requirement. On our own motion, we clarify that NECA is subject to the affiliate transactions rules only to the extent necessary to ensure that transactions between NECA and USAC are recorded fairly. We conclude that NECA would satisfy this requirement by valuing and recording transactions with USAC at fully distributed cost in accordance with its Cost Accounting and Procedures Manual on file with the Commission. Consistent with this finding, we conclude that section 32.27 of the Commission's rules, to the extent that it requires regulated carriers to record transactions with affiliates at the tariffed rate, if a tariffed rate exists, at the prevailing market rate, if a prevailing market rate exists, or at the higher of estimated fair market value or cost, is not applicable to transactions between NECA and USAC.[912]

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[908] 47 C.F.R. § 32.27.

[909] 47 C.F.R. § 32.27. The affiliate transactions rules require that regulated carriers record transactions with affiliates at the tariffed rate, if a tariffed rate exists, or at the prevailing market rate, which applies only if 50 percent of sales are made to unaffiliated entities. If no tariffed rate or prevailing market rate exist, carriers must record transactions based upon which direction the transaction flows. Transactions flowing from the carrier to the affiliate are recorded at the higher of estimated fair market value or cost. Transactions flowing from the affiliate to the carrier are recorded at the lower of estimated fair market value or cost.

[910] *See* 47 C.F.R. §§ 54.701, 69.604(H), 69.603.

[911] 47 C.F.R. § 32.27.

[912] *See* 47 C.F.R. § 32.27.

VIII. . FINAL REGULATORY FLEXIBILITY ANALYSIS

314. As required by the Regulatory Flexibility Act (RFA), *see* 5 U.S.C. § 603, an Initial Regulatory Flexibility Analysis (IRFA) was incorporated in the *Notice of Proposed Rulemaking and Order Establishing Joint Board*.[913] In addition, the Commission prepared an IRFA in connection with the *Recommended Decision*, seeking written public comment on the proposals in the *NPRM* and *Recommended Decision*.[914] A Final Regulatory Flexibility Analysis (FRFA) was included in the previous *Order*.[915] The Commission's Final Regulatory Flexibility Analysis (FRFA) in this order conforms to the RFA, as amended.[916]

315. To the extent that any statement contained in this FRFA is perceived as creating ambiguity with respect to our rules or statements made in preceding sections of this order, the rules and statements set forth in those preceding sections shall be controlling.

A. Need for and Objectives of this Report and Order and the Rules Adopted Herein.

316. The Commission is required by section 254 of the Act, as amended by the 1996 Act, to promulgate rules to implement promptly the universal service provisions of section 254. On May 8, 1997, the Commission adopted rules whose principle goal is to reform our system of universal service support so that universal service is preserved and advanced as markets move toward competition. In this order, we clarify and reconsider those rules.

B. Summary and Analysis of the Significant Issues Raised by Public Comments in Response to the IRFA.

317. Summary of the Initial Regulatory Flexibility Analysis. The Commission performed an IRFA in the *NPRM*[917] and an IRFA in connection with the *Recommended Decision*.[918] In the IRFAs, the Commission sought comment on possible exemptions from the

[913] *NPRM*, 11 FCC Rcd at 18,152-18,153.

[914] 61 Fed. Reg. 63,778, 63,796 (1996).

[915] *Order*, 12 FCC Rcd at 9219-9260.

[916] *See* 5 U.S.C. § 604. The Regulatory Flexibility Act, 5 U.S.C. § 601 *et seq*., was amended by the Contract with America Advancement Act of 1996, Pub. L. No. 104-121, 110 Stat. 847 (1996) (CWAAA). Title II of CWAAA is the "Small Business Regulatory Enforcement Fairness Act of 1996" (SBREFA).

[917] *NPRM*, 11 FCC Rcd at 18,152-18,153.

[918] 61 Fed. Reg. at 63,796.

proposed rules for small telecommunications companies and measures to avoid significant economic impact on small entities, as defined by the RFA.[919] The Commission also sought comment on the type and number of small entities, such as schools, libraries, and health care providers, potentially affected by the recommendations set forth in the *Recommended Decision*.[920]

318. No comments in response to the IRFAs, other than those described in the *Order*,[921] were filed. In response to the FRFA, RTC argues that the Commission did not satisfy the requirements of the RFA by considering alternatives to the cap on recovery of corporate operations expenses.[922] We note that the majority of commenters in the *Order* generally supported limiting the amount of corporate operations expense that can be recovered through the universal service support mechanisms.[923] Some commenters suggested that universal service support should not be allowed at all for corporate operating expenses; however, the Commission found that the amount of corporate operating expense per line that is supported through the universal service support mechanisms should fall within a range of reasonableness.[924] The Commission weighed all alternatives relating to corporate operating expenses in the *Order* and the previous FRFA in reaching its conclusion.[925]

C. Description and Estimates of the Number of Small Entities to Which the Rules Adopted in This Report and Order will Apply.

319. In the FRFA to the *Order*, we described and estimated the number of small entities that would be affected by the new universal service rules. The rules adopted here will apply to the same telecommunications carriers and entities affected by the universal service rules. We therefore incorporate by reference paragraphs 890-925 of the *Order*, which describe and estimate the number of affected telecommunications carriers and other entities affected by the

[919] *NPRM*, 11 FCC Rcd at 18,153.

[920] 61 Fed. Reg. at 63,799.

[921] *Order*, 12 FCC Rcd at 9220-9224.

[922] RTC petition to *July 10 Order* at 8, n.11 *citing* 5 U.S.C. § 603.

[923] *Order*, 12 FCC Rcd at 8930-8931.

[924] *Order*, 12 FCC Rcd at 8931.

[925] *Order*, 12 FCC Rcd at 8930-8932, 9249.

universal service rules.[926] We summarize that analysis as follows:

1. Telephone Companies (SIC 4813)

320. Total Number of Telephone Companies Affected. Many of the decisions and rules adopted herein may have a significant effect on a substantial number of the small telephone companies identified by the SBA. The United States Bureau of the Census ("the Census Bureau") reports that, at the end of 1992, there were 3,497 firms engaged in providing telephone services, as defined therein, for at least one year.[927]

321. Wireless (Radiotelephone) Carriers. SBA has developed a definition of small entities for radiotelephone (wireless) communications companies. The Census Bureau reports that there were 1,176 such companies in operation for at least one year at the end of 1992.[928] According to SBA's definition, a small business radiotelephone company is one employing no more than 1,500 persons.[929] The Census Bureau also reported that 1,164 of those radiotelephone companies had fewer than 1,000 employees. Thus, even if all of the remaining 12 companies had more than 1,500 employees, there would still be 1,164 radiotelephone companies that might qualify as small entities if they are independently owned and operated.

2. Cable System Operators (SIC 4841)

322. The SBA has developed a definition of small entities for cable and other pay television services that includes all such companies generating less than $11 million in revenue annually.[930] This definition includes cable systems operators, closed circuit television services, direct broadcast satellite services, multipoint distribution systems, satellite master antenna systems, and subscription television services. According to the Census Bureau, there were 1,758 total cable and other pay television services and 1,423 had less than $11 million in revenue.[931]

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[926] *Order*, 12 FCC Rcd at 9227-9241.

[927] United States Department of Commerce, Bureau of the Census, *1992 Census of Transportation, Communications, and Utilities: Establishment and Firm Size*, at Firm Size 1-123 (indicating only the number of such firms engaged in providing telephone service and not the size of such firms) (1995) (*1992 Census*).

[928] United States Department of Commerce, Bureau of the Census, *1992 Census of Transportation, Communications, and Utilities: Establishment and Firm Size*, at Firm Size 1-123 (1995) (*1992 Census*).

[929] 13 C.F.R. § 121.201, Standard Industrial Classification (SIC) Code 4812.

[930] 13 C.F.R. § 121.201, SIC 4841.

[931] U.S. Department of Commerce, Bureau of Census, *1992 Economic Census Industry and Enterprise Receipts Size Report*, Table 2D, SIC 4841 (Bureau of the Census data under contract to the Office of Advocacy of the SBA).

We note that cable system operators are included in our analysis due to their ability to provide telephony.

3. Municipalities

323. The term "small government jurisdiction" is defined as "government of . . . districts with populations of less than 50,000."[932] The most recent figures indicate that there are 85,006 governmental entities in the United States.[933] This number includes such entities as states, counties, cities, utility districts, and school districts. Of the 85,006 governmental entities, 38,978 are counties, cities, and towns. The remainder are primarily utility districts, school districts, and states. Of the 38,978 counties, cities, and towns, 37,566 or 96%, have populations of fewer than 50,000. Consequently, we estimate that there are 37,566 "small government jurisdictions" that will be affected by our rules.

4. Rural Health Care Providers

324. Neither the Commission nor the SBA has developed a definition of small, rural health care providers. Section 254(h)(5)(B) defines the term "health care provider" and sets forth the seven categories of health care providers eligible to receive universal service support.[934] We estimate that there are: (1) 625 "post-secondary educational institutions offering health care instruction, teaching hospitals, and medical schools," including 403 rural community colleges,[935] 124 medical schools with rural programs,[936] and 98 rural teaching hospitals;[937] (2) 1,200 "community health centers or health centers providing health care to migrant;"[938] (3) 3,093 "local health departments or agencies" including 1,271 local health departments[939] and 1,822 local

[932] 5 U.S.C. § 601(5).

[933] *1992 Census of Governments.*

[934] *See* 47 U.S.C. § 254(h)(5)(B).

[935] Letter from Kent A. Phillippe, American Association of Community Colleges, to John Clark, FCC, dated March 31, 1997 (AACC March 31 *ex parte* at 2).

[936] Letter from Donna J. Williams, Ass'n of American Medical Colleges, to John Clark, FCC, dated September 9, 1996 (AAMC September 9 *ex parte*).

[937] Letter from Kevin G. Serrin, Ass'n of American Medical Colleges, to John Clark, FCC, dated September 5, 1996 (AAMC September 5 *ex parte*).

[938] Letter from Richard C. Bohrer, Division of Community and Migrant Health, HHS, to John Clark, FCC, dated March 31, 1997 (HHS March 31 *ex parte* at 2).

[939] Telephone contact by John Clark, FCC, with Carol Brown, National Association of County Health Officials, May

boards of health;[940] (4) 2,000 "community mental health centers;"[941] (5) 2,049 "not-for-profit hospitals;"[942] and (6) 3,329 "rural health clinics."[943] We do not have sufficient information to make an estimate of the number of consortia of health care providers at this time. The total of these categorical numbers is 12,296. Consequently, we estimate that there are fewer than 12,296 health care providers potentially affected by the rules in this order.

5. Schools (SIC 8211) and Libraries (SIC 8231)

325. The SBA has established a definition of small elementary and secondary schools and small libraries as those with under $5 million in annual revenues.[944] The most reliable source of information regarding the total number of kindergarten through 12th grade (K-12) schools and libraries nationwide of which we are aware appears to be data collected by the United States Department of Education and the National Center for Educational Statistics. Based on that information, it appears that there are approximately 86,221 public and 26,093 private K-12 schools in the United States (SIC 8211).[945] It further appears that there are approximately 15,904 libraries, including branches, in the United States (SIC 8231).[946] Consequently, we estimate that there are fewer than 86,221 public and 26,093 private schools and fewer than 15,904 libraries that may be affected by the decisions and rules adopted in this order.

D. Summary Analysis of the Projected Reporting, Recordkeeping, and Other Compliance Requirements and Significant Alternatives and Steps Taken to Minimize the Significant Economic Impact on a Substantial

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2, 1997.

[940] Letter from Ned Baker, Nat'l Ass'n of Local Boards of Health, to John Clark, FCC, dated April 2, 1997 (Nat'l Ass'n of Local Boards of Health April 2 *ex parte*).

[941] Telephone contact by John Clark, FCC, with Mike Weakin, Center for Mental Health Services, HHS, on May 2, 1997.

[942] American Hospital Association Center for Health Care Leadership, *A Profile of Nonmetropolitan Hospitals 1991-95* at 5 (1997).

[943] Letter from Patricia Taylor, ORHP/HHS, to John Clark, FCC, dated May 2, 1997 (ORHP/HHS May 2 *ex parte*).

[944] 13 C.F.R. § 121.201, SIC 8211 and 8231.

[945] Letter from Emilio Gonzalez, to Mark Nadel, FCC, dated November 4, 1996 (U.S. Department of Education November 4 *ex parte*).

[946] National Center for Education Statistics, *Public Library Structure and Organization in the United States*, Tbl. 1 (March 1996).

Number of Small Entities Consistent with Stated Objectives.

326. Structure of the Analysis. In this section of the FRFA, we analyze the projected reporting, recordkeeping, and other compliance requirements that may apply to small entities and small incumbent LECs as a result of this order.[947] As a part of this discussion, we mention some of the types of skills that will be needed to meet the new requirements. We also describe the steps taken to minimize the economic impact of our decisions on small entities and small incumbent LECs, including the significant alternatives considered and rejected.[948] Section numbers correspond to the sections of the order.

Summary Analysis: Section II
DEFINITION OF UNIVERSAL SERVICE

Summary of Projected Reporting, Recordkeeping, and Other Compliance Requirements.

327. We conclude that Mobile Satellite Service (MSS) providers in localities that have implemented E911 service, like other wireless providers, may petition their state commission for permission to receive universal service support for the designated period during which they are completing the network upgrades required to offer access to E911. We also affirm that MSS providers in localities that have implemented E911 service must demonstrate that "exceptional circumstances" prevent them from offering access to E911. We note that we are not imposing any new reporting requirements beyond those established in the May 8, 1997 *Order*.

Significant Alternatives and Steps Taken to Minimize Significant Economic Impact on a Substantial Number of Small Entities Consistent with Stated Objectives.

328. We recognize that exceptional circumstances may prevent some carriers, such as MSS providers, from offering access to E911. To promote competitive and technological neutrality, however, we permit MSS providers that are incapable of providing access to E911 service, but that wish to receive universal service support, to demonstrate to their state commissions that "exceptional circumstances" prevent them from offering such access.

Summary Analysis: Section III
CARRIERS ELIGIBLE FOR UNIVERSAL SERVICE SUPPORT

Summary of Projected Reporting, Recordkeeping, and Other Compliance Requirements.

[947] *See* 5 U.S.C. § 604(a)(4).

[948] *See* 5 U.S.C. § 604(a)(5).

329. As of January 1, 1998, the temporary Administrator may not disburse support to carriers that have not been designated as eligible under section 214(e). Thus, if a carrier has not been designated as eligible by its state commission by January 1, 1998, it may not receive support until such time as it is designated an eligible telecommunications carrier. Additionally, we encourage Sandwich Isles and the relevant Hawaiian state agencies to resolve their dispute over which entity should designate eligible telecommunications carriers to serve the Hawaiian Home Lands. If they are unable to do so, we encourage them to bring this fact to our attention so that we may complete action on the pending petitions on this matter. Neither of these determinations impose any new reporting, recordkeeping, or other compliance requirements on small entities.

Significant Alternatives and Steps Taken to Minimize Significant Economic Impact on a Substantial Number of Small Entities Consistent with Stated Objectives.

330. In the *Order* and subsequent public notices, we have emphasized to state commissions that they must designate eligible telecommunications carriers by January 1, 1998, so that carriers that are eligible for universal service support may receive such support beginning January 1, 1998. State commissions that are unable to designate any eligible telecommunications carrier in a service area by January 1, 1998 may, upon completion of the designation, file with the Commission a petition for a waiver requesting that the designated carrier receive universal service support retroactive to January 1, 1998.

Summary Analysis: Section IV
HIGH COST, RURAL, AND INSULAR SUPPORT

Summary of Projected Reporting, Recordkeeping, and Other Compliance Requirements.

331. Section 54.303 of the Commission's rules provides the method by which the Administrator will calculate and distribute DEM weighting assistance (or local switching support). Although that section sets forth the method for calculating the local switching support factor, it does not specify the method for calculating the annual unseparated local switching revenue requirement. Accordingly, we amend the Commission's Part 54 rules to provide the method by which the Administrator will calculate the unseparated local switching revenue requirement. Specifically, we direct the Administrator to use Part 32 account data as suggested by NECA to determine the unseparated local switching revenue requirement. Consistent with our adoption of a methodology that relies upon Part 32 account data, we authorize the Administrator to issue a data request annually to the carriers that serve study areas with 50,000 or fewer access lines. We anticipate that of the approximately 1,288 carriers that will be required to file Part 32 account data with the Administrator in order to receive DEM weighting assistance, all but approximately 192 already provide this information to NECA.

332. We adopt no additional reporting, recordkeeping, or other compliance

requirements with respect to the remaining high cost, DEM weighting and LTS issues addressed in this order.

Significant Alternatives and Steps Taken to Minimize Significant Economic Impact on a Substantial Number of Small Entities Consistent with Stated Objectives.

333. We considered an alternative method of calculating the unseparated local switching revenue requirement that would not have imposed an additional reporting requirement on those carriers that currently do not file Part 32 account data with NECA. We concluded, however, that GVNW's proposal to calculate the local switching revenue requirement by dividing the interstate local switching revenue requirement by the interstate DEM weighting factor that is used to assign the local switching investment to the interstate jurisdiction under Part 36 of our rules would not provide an accurate measure of the unseparated local switching revenue requirement. If all local switching expenses and investment used to determine the revenue requirement for the local switching rate element were allocated between the interstate and intrastate jurisdictions on the basis of weighted DEM, the formula suggested by GVNW would result in an accurate calculation of the unseparated local switching revenue requirement. Weighted DEM, however, is only one of several mechanisms used to allocate local switching expenses and investment between the interstate and intrastate jurisdictions for purposes of determining local switching access charges. The Commission's rules prescribe different allocators for other local switching expenses and related investment, such as those associated with general support facilities. We conclude that the approach adopted in this order, to the extent that it allocates local switching expenses and related investment in a manner that is consistent with the allocation methods prescribed under Parts 36 and 69 of our rules, provides a more accurate method for calculating the unseparated local switching revenue requirement.

334. Although we adopt no additional reporting, recordkeeping, or other compliance requirements with respect to the cap on recovery of corporate operations expenses, we note that several petitioners challenged the Commission's decision to limit recovery of corporate operations expenses. These petitioners argue that the Commission's decision in the *Order* to limit such expenses ignores Congress's intent to limit or reduce burdens on small, rural, and insular carriers and, in fact, disproportionately burdens smaller incumbent LECs.[949] ITC argues that federal regulatory expenses should not be included within the limitation to ensure that small companies will be able to participate in the federal regulatory process.[950]

335. In general, the Commission's decision to limit recovery of corporate operations

[949] *See, e.g.*, GVNW petition at 9-12; Western Alliance petition at 8-11; Virgin Islands Tel. Co. reply to *July 10 Order* at 8-9 (citing 47 U.S.C. § 254(b)(3)'s reference to insular areas)

[950] ITC petition at 7-9.

expenses carefully considers the needs of smaller carriers. The Commission concludes that all carriers currently have little incentive to minimize these expenses because the current mechanism allows carriers to recover a large percentage of their corporate operations expenses. Smaller carriers possess even fewer incentives to minimize corporate operations expenses because the Commission has a limited ability to ensure, through audits, that smaller companies properly assign corporate operations expenses to appropriate accounts and that carriers do not spend at excessive levels. The Commission, and frequently state commissions, cannot justify auditing smaller carriers because the cost of a full-scale audit is likely to exceed any expenses found to be improper by that audit. We therefore conclude that imposing a cap that is relatively generous to small carriers but still imposes a limitation is a prudent way to encourage correct allocation of expenditures and to discourage excessive expenditures. Under this approach, we are providing carriers with an incentive to control their corporate operations expenses without requiring all carriers, including small carriers, to incur the costs associated with a full Commission audit. As the Commission indicated in its *Order* and as explained above, carriers that contend that the limitation provides insufficient support may request a waiver from the Commission. Therefore, only carriers whose expenses are significantly above the average and who contend that the capped amount is insufficient will be required to provide additional justification for their expenditures. We therefore conclude that this limitation deters improper recovery of universal service funds while minimizing the administrative burden on the Commission and on all carriers, including smaller carriers. Moreover, individual companies that are required to incur unusually high corporate operations expenses, such as small companies, Alaskan companies, or insular companies, are able to apply for a waiver with the Commission to demonstrate that these expenses are necessary to the provision of the supported services.

336. In adopting the limitation on corporate operations expenses, the Commission considered whether to exclude recovery of all corporate operations expenses, as it had originally proposed in 1995.[951] The Commission concluded, however, that it should limit recovery of such expenses, in part to protect smaller recipients of high cost universal service support. When developing the formula that will calculate the limit on recovery of corporate operations expense, the Commission took into account the lesser economies of scale of smaller carriers and adopted a limit that is more generous to smaller carriers. Additionally, the Commission adopted an industry proposal to add a minimum annual cap of $300,000 that is favored, among others, by petitioners representing smaller, rural carriers.[952] This minimum cap will assist the smallest carriers -- those with fewer than approximately 600 lines. Further, when developing the formula

[951] *See* Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket No. 80-286, *Notice of Inquiry*, 9 FCC Rcd 7404 at 7416-17 (1994) (*1994 NOI*); Amendment of Part 36 of the Commission's Rules and Establishment of a Joint Board, CC Docket 80-286, *Notice of Proposed Rulemaking and Notice of Inquiry*, 10 FCC Rcd 12,309, 12,324 (*1995 NPRM*).

[952] *See, e.g.*, GVNW petition at 9-10.

to limit recovery of corporate operations expenses, the Commission chose not to limit recovery to the average corporate operations expenses, but instead added a 15 percent "buffer" to protect all carriers, including smaller carriers, with expenses that are slightly higher than average. We reject ITC's request to exclude all federal regulatory expenses from the limitation because, while some expenditures may be necessary to participate in the federal regulatory process, the need for such expenditures are not without limit and many carriers, including smaller carriers, fulfill legal and regulatory requirements and participate in the federal regulatory process while incurring costs below the Commission's limit.

Summary Analysis: Section V
SUPPORT FOR LOW-INCOME CONSUMERS

Summary of Projected Reporting, Recordkeeping, and Other Compliance Requirements.

337. There are no new reporting, recordkeeping, or compliance requirements required by this section.

Significant Alternatives and Steps Taken to Minimize Significant Economic Impact on a Substantial Number of Small Entities Consistent with Stated Objectives.

338. We reconsider the Commission's decision that eligible telecommunications carriers must provide both toll blocking and toll control to qualifying low-income consumers. We find that eligible telecommunications carriers that cannot provide both toll blocking and toll control may provide either toll blocking or toll control to qualifying low-income consumers. Small carriers that are not capable of providing both toll blocking and toll control will benefit from this decision by remaining eligible for universal service when providing one but not both of these services to qualifying low-income consumers.

Summary Analysis: Section VI
SCHOOLS AND LIBRARIES AND RURAL HEALTH CARE PROVIDERS

Summary of Projected Reporting, Recordkeeping, and Other Compliance Requirements.

339. In the order, we affirm the Commission's previous decision to require service providers to "look back" three years to determine the lowest corresponding price charged for similarly situated non-residential customers. We also affirm the Commission's previous decision to require schools and libraries to conduct an internal assessment of the components necessary to use effectively the discounted services they order, submit a complete description of the services they seek, and certify to certain criteria under penalty of perjury. We also affirm the Commission's previous decision to require schools and libraries to obtain independent approval of their technology plans. We note that we are not imposing any new reporting requirements

beyond those established in the May 8, 1997 *Order*.

340. We do not require that the Schools and Libraries Corporation and the Rural Health Care Corporation post RFPs submitted by schools, libraries, and rural health care providers on the websites. Instead, schools and libraries will submit FCC Form 470 and rural health care providers will submit FCC Form 465, containing a description of services requested, and the Schools and Libraries Corporation and Rural Health Care Corporation will post only the information contained in these forms on the websites. We affirm the Commission's prior decision that the Schools and Libraries Corporation may review technology plans when a state agency is unable or unwilling to do so within a reasonable time. In an effort to ensure that eligible schools and libraries are not penalized by this requirement, we will allow such entities to indicate on FCC Form 470 that their technology plan has either been approved, will be approved by a state or other authorized body, or will be submitted to the Schools and Libraries Corporation for approval. Applicants will be required to certify on FCC Form 471 that they will strive to ensure that the most disadvantaged schools and libraries will receive the full benefit of the discounts to which they are entitled. These reporting requirements were set forth in either the *Order* or the *July 10 Order*. These tasks may require some administrative, accounting, clerical, and legal skills.

341. We conclude that state telecommunications networks that procure telecommunications from service providers and make such services available to consortia of schools and libraries will be permitted to secure discounts on eligible telecommunications from service providers on behalf of eligible schools and libraries. In addition, we conclude that state telecommunications networks that provide access to the Internet and internal connections may either secure discounts on such telecommunications and pass on such discounts to eligible schools and libraries, or receive direct reimbursement from universal service support mechanisms for providing Internet access and internal connections. In order to receive universal service discounts that will be passed through to eligible schools and libraries, state telecommunications networks will request that service providers apply appropriate discount amounts on eligible telecommunications. The service providers will submit to the state telecommunications network a bill that includes the appropriate discounts on the portion of eligible telecommunications rendered to eligible entities. The state telecommunications network then will direct the eligible consortia members to pay the discounted price. Eligible consortia members may pay the discounted price to their state telecommunications network, which will then pay the discounted amount to the service providers. State telecommunications networks should retain records listing eligible schools and libraries and showing the basis on which the eligibility determinations were made. Such networks also must keep careful records demonstrating the discount amount to which each eligible entity is entitled and the basis for such a determination. We note that this is not a new reporting requirement. In addition, we require consortia to certify that each individual institution listed as a member of the consortia and included in determining the discount rate will receive an appropriate share of the shared services

within five years of the filing of the consortium application. We further conclude that, to the extent schools and libraries build and purchase wide area networks to provide telecommunications, the cost of purchasing such networks will not be eligible for universal service discounts.

Significant Alternatives and Steps Taken to Minimize Significant Economic Impact on a Substantial Number of Small Entities Consistent with Stated Objectives.

342. We affirm the Commission's decision to require service providers to "look back" three years to determine the lowest corresponding price charged for similarly situated non-residential customers. In doing so, we do not adopt the proposal of GTE to reduce this requirement to one year. We note that we do not consider this provision to be unduly burdensome on providers, some of whom may qualify as small entities, as the records to be reviewed are limited to those relating to similarly situated non-residential customers for similar services. Moreover, we expect that providers would voluntarily perform such a review in most cases to determine the rate to charge in a competitive environment.

343. We affirm the Commission's decision to require schools and libraries to comply with certain reporting requirements including conducting an internal assessment of the components necessary to use effectively the discounted services they order, submit a complete description of the services they seek, and certify to certain criteria under penalty of perjury. We do not find these requirements to be unduly burdensome on schools and libraries and believe that they will assist schools and libraries in obtaining and utilizing supported services in an efficient and effective manner. We also affirm the Commission's decision to require schools and libraries to submit and receive approval of technology plans. We do not adopt the suggestion of a few petitioners that we postpone or eliminate this requirement in an effort to equalize the ability of non-public schools and libraries to obtain independent approval. We do, however, adopt measures to assist non-public entities, many of whom may qualify as small entities, from being disadvantaged by this requirement. For example, we authorize the Schools and Libraries Corporation to review technology plans when the state is unwilling or unable to do so in a reasonable time. Eligible entities that are not required by state or local law to obtain state approval for technology plans and telecommunications expenditures may apply directly to the Schools and Libraries Corporation for review of their technology plan. In addition, FCC Form 470 will allow applicants to indicate that their technology plans either have been approved, will be approved by a state or other entity, or will be submitted to the Schools and Libraries Corporation for approval. This will allow non-public schools and libraries to proceed with the application process in a timely manner while obtaining approval of their technology plans. Support will not, however, be provided prior to approval of the technology plan.

344. We reconsider the definition of existing contracts established in the *July 10 Order* that are exempt from the competitive bid requirement. We conclude that any contract signed on

or before July 10, 1997 will be considered an existing contract. Contracts signed after July 10, 1997 but before the websites are fully operational will be considered existing contracts for those services provided through December 31, 1998. We extend the existing contract exemption that we establish in this Order to rural health care providers, many of whom identify themselves as small entities. We believe that this determination will assist many small entities by allowing them to negotiate lower rates through long-term contracts and avoid penalties associated with breaking contracts that they entered into prior to the date that the website is fully operational. We do not adopt the suggestion that we eliminate all restrictions on contracts signed prior to the date that the schools and libraries websites become fully operational. Although schools and libraries have a strong incentive to negotiate contracts at the lowest possible pre-discount prices in an effort to reduce their costs, we affirm our initial finding that competitive bidding is the most efficient means of ensuring that eligible schools and libraries are informed about the choices available to them and receive the lowest prices.

345. Requiring state telecommunications networks to retain records listing eligible schools and libraries should be minimally burdensome because we require such networks to gather and retain basic information, such as the names of consortia members, addresses, and telephone numbers. Requiring state networks to keep records demonstrating the discount amount to which each eligible entity is entitled and the basis on which such a determination was made should be minimally burdensome, because such information should be readily available from the eligible entities. Additionally, consistent with the *Order*, service providers must keep and retain careful records showing how they have allocated the costs of facilities shared by eligible and ineligible entities in order to charge such entities the correct amounts. As we determined in the *Order*, this should be minimally burdensome, because state networks will be required to inform the service provider of what portion of shared facilities purchased by the consortia should be charged to eligible schools and libraries (and discounted by the appropriate amounts). We find that these recordkeeping and reporting requirements described above are necessary to provide the level of accountability that is in the public interest.

Summary Analysis: Section VII
ADMINISTRATION

Summary of Projected Reporting, Recordkeeping, and Other Compliance Requirements.

346. Section 254(d) states "that all telecommunications carriers that provide interstate telecommunications services shall make equitable and nondiscriminatory contributions" toward the preservation and advancement of universal service. We shall continue to require all telecommunications carriers that provide interstate telecommunications services and some providers of interstate telecommunications to contribute to the universal service support mechanisms. Contributions for support for programs for high cost areas and low-income consumers will be assessed on the basis of interstate and international end-user

telecommunications revenues. Contributions for support for programs for schools, libraries, and rural health care providers will be assessed on the basis of interstate, intrastate, and international end-user telecommunications revenues. As provided in the *Order*, contributors will be required to submit information regarding their end-user telecommunications revenues. Approximately 4,500 telecommunications carriers and providers will be required to submit contributions. We note that we do not impose any new reporting requirements beyond those established in the *Order*. These tasks may require some administrative, accounting, and legal skills.

Significant Alternatives and Steps Taken to Minimize Significant Economic Impact on a Substantial Number of Small Entities Consistent with Stated Objectives.

347. In accordance with section 254(d), we affirm the Commission's decision that all telecommunications carriers that provide interstate telecommunications services shall make equitable and nondiscriminatory contributions toward universal service. We reject the contention of various telecommunications carriers that they should not be required to contribute or should be allowed to contribute at a reduced rate. For example, we reject the suggestion of some petitioners that CMRS providers, many of whom may qualify as small businesses, should not be required to contribute, or should be allowed to contribute at a reduced rate, due to their contention that they may not be eligible to receive universal service support. We note that section 254(d) provides no such exemption for CMRS providers or other carriers regardless of whether they receive universal service support.[953] We affirm the Commission's decision, however, that entities that provide only international telecommunications services are not required to contribute to universal service support because they are not telecommunications carriers that provide interstate telecommunications services. We also clarify that the lease of space segment capacity by satellite providers does not constitute the provision of telecommunications and therefore does not trigger universal service contribution requirements.

348. We exempt from the contribution requirement systems integrators that obtain a *de minimis* amount of their revenues from the resale of telecommunications. We exempt from the contribution requirement schools, libraries, and rural health care providers that are eligible to receive universal service support. We also agree with petitioners' suggestions that the *de minimis* exemption take into account the Administrator's collection costs and contributor's reporting compliance costs. We find that if a contributor's contribution to universal service in any given year is less than $10,000, that contributor will not be required to submit a contribution for that year. We believe that small entities will benefit under the *de minimis* exemption as interpreted in the Order. We also believe that small payphone aggregators, such as grocery store owners, will be exempt from contribution requirements pursuant to our *de minimis* exemption.

[953] 47 U.S.C. § 254(d).

E. Report to Congress

349. The Commission shall send a copy of this FRFA, along with this Report and Order, in a report to Congress pursuant to the Small Business Regulatory Enforcement Fairness Act of 1996, 5 U.S.C. § 801(a)(1)(A). A copy or summary of the Report and Order and this FRFA will also be published in the Federal Register, *see* 5 U.S.C. § 604(b), and will be sent to the Chief Counsel for Advocacy of the Small Business Administration.

IX. ORDERING CLAUSES

350. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 1-4, 201-205, 218-220, 214, 254, 303(r), 403, and 410 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151-154, 201-205, 218-220, 214, 254, 303(r), 403, and 410, the FOURTH ORDER ON RECONSIDERATION IS ADOPTED, effective 30 days after publication of the text in the Federal Register. The collections of information contained within are contingent upon approval by the Office of Management and Budget.

351. IT IS FURTHER ORDERED that Parts 36, 54, and 69 of the Commission's rules, 47 C.F.R. §§ 36, 54, and 69, are amended as set forth in Appendix A hereto, effective 30 days after publication of the text thereof in the Federal Register.[954]

352. IT IS FURTHER ORDERED that, pursuant to section 5(c)(1) of the Communications Act of 1934, as amended, 47 U.S.C. § 155(c)(1), authority is delegated to the Chief, Common Carrier Bureau, to review, modify, and approve the formula submitted by the Administrator pursuant to section 54.303(f) of the Commission's rules, 47 C.F.R. § 54.303(f).

353. IT IS FURTHER ORDERED that United States Telephone Association's Petition for Clarification is DISMISSED AS MOOT.

354. IT IS FURTHER ORDERED that Florida Public Service Commission's Petition for Declaratory Statement is GRANTED. IT IS FURTHER DETERMINED that the Florida Commission's state Lifeline program qualifies as a program that provides intrastate matching funds and, therefore, the Florida Commission may set its own consumer qualification standards. IT IS FURTHER ORDERED that Florida Public Service Commission's Petitions for Waiver are DISMISSED AS MOOT, and that its Request for Expedited Ruling and Petition for Clarification

[954] We also take this opportunity to codify corrections made to the Commission's rules, as announced in an errata released by the Accounting and Audits Division of the Commission's Common Carrier Bureau on December 3, 1997. Federal-State Joint Board on Universal Service and Changes to the Board of Directors of the National Exchange Carrier Association, Inc., CC Dockets. 96-45, 97-21, *Errata*, DA 97-2477 (Comm. Carr. Bur., Acct. & Audits Div. rel. Dec. 3, 1997).

are GRANTED.

355. IT IS FURTHER ORDERED that if any portion of this Order or any regulation implementing this Order is held invalid, either generally or as applied to particular persons or circumstances, the remainder of the Order or regulations, or their application to other persons or circumstances, shall not be affected.

356. IT IS FURTHER ORDERED that the Commission's Office of Public Affairs, Reference Operations Division, SHALL SEND a copy of this Report and Order, including the Final Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

Magalie Roman Salas
Secretary