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

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	
	)	
National Exchange Carrier Association, Inc. and Universal Service Administrative Company	)	CC Docket No. 96-45
	)	
	)	
2007 Modification of Average Schedule Universal Service Formulas	)	
	)	

ORDER

Adopted: January 9, 2007 **Released: January 9, 2007**

By the Associate Chief, Wireline Competition Bureau:

I. INTRODUCTION

1. Each year, the Commission must review and approve or modify any proposed modifications to the formulas used to calculate Part 36 high-cost loop support and local switching support for average schedule companies.[1] The National Exchange Carrier Association, Inc. (NECA) files the annual average schedule company formula modifications for the Part 36 high-cost loop support. Pursuant to section 54.301(f) of the Commission's rules, the Universal Service Administrative Company (USAC) submits the proposed formula for local switching support.[2] The Commission's rules require that these formulas simulate the disbursements that would be received by a company that is representative of average schedule companies.[3]

2. On August 30, 2006, NECA filed proposed modifications to the current high-cost loop universal service formula for average schedule companies, and it requested that they take effect on January 1, 2007, and remain in effect through December 31, 2007.[4] On September 22, 2006, USAC filed proposed modifications to the current local switching support formula for average schedule companies which, if approved, will be effective from January 1, 2007, through December 31, 2007.[5] On October 18,

[1] *See* 47 C.F.R. § 69.606; 47 C.F.R. § 36.613.

[2] 47 C.F.R. § 54.301(f).

[3] *See* 47 C.F.R. § 69.606; 47 C.F.R. § 54.301(f).

[4] *See* 2007 NECA Modification of the Average Schedule Universal Service High Cost Loop Support Formula, National Exchange Carrier Association, Inc., CC Docket No. 96-45 (filed Aug. 30, 2006) (*NECA 2007 Filing*).

[5] *See* Letter from Karen M. Majcher, USAC, to Marlene H. Dortch, FCC, CC Docket No. 96-45 (filed Sept. 22, 2006) (*USAC 2007 Filing*) (attaching 2007 average schedule local switching support formula). In the *NECA 2005 Filing,* NECA notified the Commission that beginning on October 1, 2005, pursuant to section 54.301(f)(1) of the Commission's rules, USAC, instead of NECA, would file with the Commission the average schedule local

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2006, the Wireline Competition Bureau (Bureau) issued a public notice soliciting comments on NECA's and USAC's proposed formulas.[6] For the reasons discussed below, we approve NECA's proposed high-cost loop formula and USAC's proposed local switching support formula. As we have done previously, we direct NECA and USAC to provide support to average schedule carriers consistent with this Order retroactive to January 1, 2007.[7]

II. LOCAL SWITCHING SUPPORT FORMULA

3. The local switching support formula is used to determine the amount of support for switching costs that will be provided to average schedule companies from the Commission's universal service high-cost support mechanism.[8] The current interstate local switching support formula was approved on January 12, 2006.[9] In its September 22, 2006, filing, USAC proposes a formula for 2007 which, if approved, would increase annual payments for local switching support from approximately $86.2 million in 2006 to approximately $86.3 million in 2007, an increase of less than one percent.[10] We have reviewed USAC's filing and the supporting information in *NECA's 2006 Modification of Average Schedules* and find that the methodology used to develop this year's proposed formula is the same methodology used to develop the formula we approved during the last payment period.[11] Consistent with the Bureau's prior orders, we approve USAC's proposed 2007 average schedule local switching support

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switching support formula for each subsequent year. *See 2005 NECA Modification of Average Schedule Universal Service Formulas*, National Exchange Carrier Association, Inc. at II-12, n.10 (filed Sept. 29, 2004) (*NECA 2005 Filing*).

[6] *See Wireline Competition Bureau Seeks Comment on 2007 Modification of Average Schedule Universal Service High-Cost Loop Support Formula and the 2007 Average Schedule Company Local Switching Support Formula*, Public Notice, CC Docket No. 96-46, 21 FCC Rcd 11769 (2006). The Bureau received comment in support of the *NECA 2007 Filing* from the Organization for the Promotion and Advancement of Small Telecommunications Companies.

[7] *See National Exchange Carrier Association, Inc. Proposed 2002 Modification of Average Schedule Formulas*, CC Docket No. 96-45, Order, 17 FCC Rcd 14236 (Wireline Comp. Bur. 2002) (*2002 Order*).

[8] Local switching support is a portion of the settlements that average schedule companies receive for providing interstate local switching access service. Average schedule companies recover the remaining costs of providing interstate local switching access costs through NECA's local switching access charges.

[9] *See National Exchange Carrier Association, Inc. 2006 Modification of Average Schedule Universal Service Formulas*, CC Docket 96-45, Order, 21 FCC Rcd 188 (Wireline Comp. Bur. 2006) (*2006 Order*).

[10] Initially, USAC estimated the proposed local switching support formula for 2007 would produce local switching support totaling approximately $92.4 million. *See USAC 2007 Filing* at Attachment. In a supplemental filing, however, USAC stated that, subsequent to its *USAC 2007 Filing* submitted on September 22, 2006, carrier data for 2007 became available and provided a "more accurate estimate" of 2007 local switching support for average schedule companies. USAC revised its estimate of total local switching support to $86.3 million. *See* Letter from Karen M. Majcher, USAC, to Marlene H. Dortch, FCC, CC Docket No. 96-45 (filed Nov. 22, 2006) (attaching 2007 estimate of local switching support for average schedule companies).

[11] USAC's average schedule local switching support formula is developed by studies documented in NECA's annual modification of average schedules filing. *See* National Exchange Carrier Association, Inc., 2006 Modification of Average Schedules, WC Docket No. 05-347 (filed Dec. 29, 2005) (*NECA's 2006 Modification of Average Schedules*); Letter from Karen M. Majcher, USAC, to Marlene H. Dortch, FCC, CC Docket No. 96-45 (filed Sept. 30, 2005) (*USAC 2006 Filing*) (attaching 2006 average schedule local switching support formula), CC Docket No. 96-45; *2006 Order*, 21 FCC Rcd 188, 189, para. 3.

formula.[12]

III. PART 36 HIGH-COST SUPPORT FORMULA

A. Background

4. Part 36 high-cost support, also known as the loop expense adjustment, is intended to provide universal service support to carriers with high loop costs based on the degree that an individual company's cost per loop exceeds the national average.[13] Because average schedule companies are not required to perform company-specific cost studies – the basis upon which a carrier's expense adjustment is calculated – the Commission has permitted expense adjustments for average schedule companies pursuant to formulas developed by NECA and approved or modified annually by the Bureau.[14] These formulas are developed by NECA using data from a sample group of average schedule carriers and from similarly situated companies that file cost data, and are used to determine support amounts for all average schedule carriers.

5. In its 1999, 2000, and 2001 orders, the Bureau rejected NECA's proposed expense adjustment per loop formula (EAPL formula) because it failed to provide a reasonable estimate of the cost per loop of the sample companies.[15] In each instance, the Bureau instead retained the existing formula with an adjustment for growth in the number of loops.[16] The Bureau also indicated in each of the orders

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[12] *See, e.g., Federal State Joint Board on Universal Service/National Exchange Carrier Association, Inc. 2005 Modification of Average Schedule Universal Service Formulas*, 19 FCC Rcd 24998, 24999, para. 2 (Wireline Comp. Bur. 2005) (*2005 Order*); *2006 Order*, 21 FCC Rcd 188, 189, para. 3.

[13] *See* 47 C.F.R. Part 36, subpart F. The Commission's rules permit a rural carrier that has significantly higher than average loop costs to shift a portion of its loop costs from the intrastate jurisdiction to the interstate jurisdiction. The carrier then receives federal universal service support equal to this expense adjustment.

[14] *See National Exchange Carrier Association, Inc. Proposed Modifications to the 1998-99 Interstate Average Schedule Formulas*, Order, 15 FCC Rcd 1819, 1819-20, para. 2 (1999) (*Commission 1999 Order*). Average schedule companies have been permitted by the Commission to estimate their access settlements and universal service support through the use of average schedules to avoid the difficulties and expenses involved with conducting company-specific cost studies. *See*, *e.g.*, *ALLTEL Corp. v. FCC*, 838 F.2d 551, 553 (D.C. Cir. 1998).

[15] *National Exchange Carrier Association, Inc. Proposed Modifications to the 1998-99 Interstate Average Schedule Formulas*, Order, 14 FCC Rcd 4049, 4051-55, paras. 6-12 (Acc. Saf. Div. 1999) (*Bureau 1999 Order*); *National Exchange Carrier Association, Inc. Proposed 2000 Modification of Average Schedule Universal Service Formulas*, Order, 15 FCC Rcd 5065, 5067-68, paras. 5-7 (Acc. Saf. Div. 2000) (*2000 Order*), *application for review pending (see* National Exchange Carrier Association, Inc. Proposed 2000 Modification of Average Schedule Universal Service Formulas, ASD 99-43, *Application for Review*, filed Apr. 17, 2000); *National Exchange Carrier Association, Inc. Proposed 2001 Modification of Average Schedule Formulas*, Order, 16 FCC Rcd 25 (Acc. Saf. Div. 2001) (*2001 Order*), *application for review pending* (*see* National Exchange Carrier Association, Inc. Proposed 2001 Modification of Average Schedule Universal Service Formulas, ASD 00-42, *Application for Review*, filed Jan. 26, 2001).

[16] *See Bureau 1999 Order*, 14 FCC Rcd 4049, 4055-56, paras. 13-14; *2000 Order*, 15 FCC Rcd 5065, 5068, para. 7; *2001 Order*, 16 FCC Rcd 25, 30, para. 8. The Commission denied NECA's Petition for Review of the *Bureau 1999 Order*, concluding that the Bureau could properly reject NECA's proposed EAPL formula because it failed to accurately predict costs per loop. *See Commission 1999 Order*, 15 FCC Rcd 1819, 1820-22, para. 4, n.15. NECA subsequently appealed the Commission's order to the U.S. Court of Appeals for the District of Columbia, claiming that the decision to reject the proposed EAPL formula and instead adjust the expense adjustment by growth in lines was arbitrary and capricious. *See National Exchange Carrier Association, Inc. v. FCC*, 253 F.3d 1 (2001). The court denied NECA's appeal, concluding that NECA "fail[ed] to articulate an intelligible explanation of its

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that it would prefer a formula that more accurately predicted cost per loop.[17] For each of the years from 2003 through 2006, NECA again proposed its EAPL formula, but also provided a Cost per Loop (CPL) formula for the Bureau's consideration.[18] NECA contended that the EAPL formula better estimated the support that average schedule carriers would receive if they were to begin filing cost studies.[19] The Bureau concluded, however, that the CPL formula better estimated the cost per loop of average schedule companies, in the aggregate, than the proposed EAPL formula and therefore approved the CPL formula for use for 2003, through 2006.[20]

6. Contrary to NECA's prior years' proposals, NECA, for 2007, only proposes the CPL formula for calculating high-cost loop support payments for average schedule companies and does not propose the EAPL formula.[21] NECA states that, "[r]ecognizing the Commission's preference for the CPL approach, however, as well as the fact that the differences between the two approaches have now diminished substantially, NECA proposes for 2007 the updated CPL formula described herein."[22] The proposed CPL formula for 2007 is developed using the same methodology as in prior years.[23] The current high-cost support formula is expected to provide $45.3 million in payments for 2006 to 408 study areas.[24]

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substantive claim . . . ." *Id.* at 2. The court also denied NECA's procedural claim that the Commission failed to follow notice and comment rulemaking procedures required under the Administrative Procedures Act. *Id.* at 4.

[17] *2000 Order*, 15 FCC Rcd 5065, 5068, para. 7; *2001 Order*, 16 FCC Rcd 25, 30, para. 8.

[18] *See* 2003 NECA Modification of Average Schedule Universal Service Formulas, National Exchange Carrier Association, Inc., at I-13 (dated Oct. 1, 2002) (NECA 2003 Filing); NECA 2004 Filing at I-13 to I-14; *NECA 2005 Filing* at III-2 to III-36; *NECA 2006 Filing* at 1 to 3.

[19] *See, e.g., NECA 2005 Filing* at I-12 to I-16.

[20] *National Exchange Carrier Association, Inc. Proposed 2003 Modification of Average Schedule Formulas*, CC Docket 96-45, Order, 17 FCC Rcd 26204, 26207-08, para. 8 (Wireline Comp. Bur. 2002) (*2003 Order*) *recon. pending*; *National Exchange Carrier Association, Inc. Proposed 2004 Modification of Average Schedule Formulas*, CC Docket 96-45, Order, 18 FCC Rcd 26619, 26622, para. 6 (Wireline Comp. Bur. 2003) (*2004 Order*); *2005 Order*, 19 FCC Rcd 24998, 25001, para 6; *2006 Order*, 21 FCC Rcd 188, 192, para. 8. In particular, the Bureau found that the CPL formula, for average schedule carriers as a whole, was a more accurate predictor of costs per loop than the EAPL formula. The Bureau noted that NECA agreed that the CPL formula was an unbiased predictor of costs per loop. *See id*.

[21] *See NECA 2007 Filing* at 1-25.

[22] *See id.* at i.

[23] NECA uses regression analyses to develop the CPL formula. NECA collects account data from a sample group of average schedule carriers. To estimate current year costs, NECA applies forecasted growth factors to data collected from sample average schedule carriers one and two years prior to the current year. NECA then applies cost allocation factors—developed from the cost studies of similarly situated cost companies—to the account balances of each sample average schedule company to estimate a CPL for each of the sample companies. NECA then uses regression analyses to predict CPLs for all average schedule carriers. Each average schedule company's derived CPL is then used to calculate the appropriate support amount. *See NECA 2007 Filing* at 1-25.

[24] We note that the current amount of $45.3 million is less than the amount that was indicated in the *NECA 2006 Filing* using the CPL formula. The *NECA 2006 Filing* estimated the CPL formula would result in total payments of $49.99 million. Because of adjustments made to the national average cost per loop in order to assure that the high-cost loop fund remains under the cap, however, payments to all cost companies and average schedule companies were reduced. *See NECA 2007 Filing* at 1.

NECA's proposed formula, if approved, would provide an estimated $56.1 million payable to 396 study areas for 2007, an increase of 23.8 percent over 2006 year payments.[25]

B. Discussion

7. Consistent with our reasoning in prior Orders, we approve NECA's proposed CPL formula for purposes of calculating average schedule company expense adjustments for 2007. The Bureau has consistently held, and the Commission has upheld, that the appropriate high-cost loop support formula should reasonably approximate the cost per loop of the sample average schedule companies and allocate funds accurately to average schedule companies.[26] Because NECA's submission of the results derived from the CPL formula appear to be accurate and complete, we approve the CPL formula as provided in NECA's August 30, 2006, submission.

8. Although, based on the current record, we approve NECA's CPL formula for 2007, which is essentially the same CPL formula filed since 2002 adjusted for changes in the sample cost data, we are concerned about yearly increases in high-cost loop support. For the three years beginning with 2004, and ending with the estimate of high-cost loop support for 2006, high-cost loop support provided to average schedule companies has increased by 16.4 percent, 38.7 percent, and 41.6 percent, respectively.[27] NECA has stated that increases in support are primarily driven by the increases in costs reported by sample average schedule companies.[28] We note that, while high-cost loop support for 2007 is estimated to increase by 23.8% over 2006 payments, the 2007 rate of increase is significantly less than the rate of increases for 2005 and 2006. We expect NECA to take precautions to avoid unreasonable growth in high-cost loop support for average schedule companies.[29]

IV. ORDERING CLAUSES

9. Accordingly, IT IS ORDERED, pursuant to sections 0.91 and 0.291 of the Commission's rules, 47 C.F.R. §§ 0.91, 0.291, that the universal service support formula proposed by the Universal Service Administrative Company on September 22, 2006, for local switching support IS ADOPTED, effective retroactively as of January 1, 2007.

10. IT IS FURTHER ORDERED, pursuant to sections 0.91 and 0.291 of the Commission's rules, 47 C.F.R. §§ 0.91, 0.291, that the average schedule cost per loop formula proposed by the National Exchange Carrier Association, Inc. on August 30, 2006, for high-cost loop support IS ADOPTED, effective retroactively as of January 1, 2007.

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[25] *See id.*

[26] *See supra* note 20. *See also Commission 1999 Order*, 15 FCC Rcd 1819, 1820-22, para. 4, n.15; *2001 Order*, 16 FCC Rcd 25, 27-30, paras. 5-8; *2002 Order*, 17 FCC Rcd 14236, 14239-41, paras. 8-11.

[27] *See 2004 Order*, 18 FCC Rcd 26619, 26622, para. 5; *2005 Order*, 19 FCC Rcd 24998, 25002, para. 7; *2006 Order*, 21 FCC Rcd 188, 193. para.9.

[28] *See, e.g., NECA 2006 Filing* at 22-23.

[29] In the *2006 Order*, we required NECA and USAC to disclose when a Commission order or rule change causes a change in aggregate high-cost loop support and local switching support, respectively, to average schedule companies by more than five percent of the previous year's universal service support. We remind NECA and USAC that this disclosure requirement remains in effect indefinitely. *See 2006 Order*, 21 FCC Rcd 188, 193, para. 9

11. IT IS FURTHER ORDERED, pursuant to section 4(i) of the Communications Act of 1934, as Amended, 47 U.S.C. § 154(i), and sections 0.91 and 0.291 of the Commission's rules, 47 C.F.R. §§ 0.91, 0.291, that THIS ORDER IS EFFECTIVE UPON ITS RELEASE.

FEDERAL COMMUNICATIONS COMMISSION

Donald K. Stockdale
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Wireline Competition Bureau