

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

In the Matter of	)	
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	

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**COMMENTS OF THE  
NEW JERSEY DIVISION OF RATE COUNSEL**

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April 17, 2008

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**I. INTRODUCTION AND SUMMARY**

**A. INTRODUCTION**

The Federal Communications Commission (“FCC” or “Commission”) seeks comments on three important aspects of universal service:<sup>1</sup>

- High-Cost Distribution Reform;<sup>2</sup>
- Identical Support Rule;<sup>3</sup> and

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<sup>1</sup> / See *Identical Support Rule NPRM*, 73 Fed. Reg. 11580; *Reverse Auctions NPRM*, 73 Fed. Reg. 11591; *Joint Board Comprehensive Reform NPRM*, 73 Fed. Reg. 11587. In a public notice announcing the establishment of comment cycles, it was noted that parties may file consolidated comments and reply comments in response to all three Notices. *Comment Cycles Established for Commission’s Notices of Proposed Rulemaking Regarding the Identical Support Rule, the Use of Reverse Auctions to Set High-Cost Universal Service Support, and the Federal-State Joint Board on Universal Service’s Recommendations for Comprehensive Reform of High-Cost Universal Service Support*, WC Docket No. 05-337, CC Docket No. 96-45, Public Notice, DA 08-499 (rel. Mar. 4, 2008). The Commission extended the comment cycle to April 17, 2008 and May 19, 2008. In the Matter of High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45, Order, released March 24, 2008.

<sup>2</sup> / In the Matter of High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-22, rel. January 29, 2008 (“Joint Board Comprehensive Reform NPRM”).

- Reverse Auctions.<sup>4</sup>

The New Jersey Division of Rate Counsel (“Rate Counsel”) is submitting this single, integrated filing in each of the Commission’s three rulemakings, and looks forward to addressing these important matters further in reply comments.

## **B. INTEREST OF RATE COUNSEL**

Rate Counsel is an independent New Jersey State agency that represents and protects the interests of all utility consumers, including residential, business, commercial, and industrial entities. Rate Counsel participates actively in relevant Federal and state administrative and judicial proceedings. The above-captioned proceeding is germane to Rate Counsel’s continued participation and interest in implementation of the Telecommunications Act of 1996 (“Act” or “1996 Act”).<sup>5</sup>

Specifically, New Jersey consumers’ interests, among others, include the following:

- As net contributors to the high cost fund, New Jersey consumers have an interest in ensuring that the high cost fund is sufficient but not excessive. Ultimately, consumers pay higher rates to support universal service.
- The high cost portion of the universal service fund (“USF”) more than doubled between 1998 and 2007 (from approximately \$1.7 billion to \$4.3 billion).<sup>6</sup> As users of the public switched network, seeking to communicate with consumers throughout the nation, including consumers located in high cost areas, New Jersey

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<sup>3</sup> / In the Matter of High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-4, rel. January 29, 2008 (“Identical Support Rule NPRM”).

<sup>4</sup> / In the Matter of High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-5, rel. January 29, 2008 (“Reverse Auctions NPRM”).

<sup>5</sup> / Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (“1996 Act”). The 1996 Act amended the Communications Act of 1934. Hereinafter, the Communications Act of 1934, as amended by the 1996 Act, will be referred to as “the 1996 Act,” or “the Act,” and all citations to the 1996 Act will be to the 1996 Act as it is codified in the United States Code.

<sup>6</sup> / Federal-State Joint Board on Universal Service, Universal Service Monitoring Report 2007 (Data Received Through June 2007) (“2007 Monitoring Report”), Table 3.14.

consumers have an interest in ensuring that high cost funds are sufficient to enable rural consumers to pay charges that are reasonably comparable to those in urban areas. However, increasing USF assessments on New Jersey consumers' bills thwart universal service, which discourages subscribership, thereby denying consumers throughout the country the positive externality associated with interconnectedness.

- As users and potential users of the nation's evolving broadband network, New Jersey users benefit from affordable broadband access, which continues to foster innovative applications that society is integrating rapidly into everyday work and home routines. There are areas in New Jersey that lack affordable broadband access. For example, only 42% of households in the Newark system subscribe to cable service; in the Jersey City system, only 47% subscribe to cable service; and in the Paramus-Hillsdale system, only 40% of households subscribe to cable service.<sup>7</sup>
- As consumers who must ultimately pay for USF charges, New Jersey consumers have an interest in a high cost fund mechanism that encourages economically efficient implementation.
- The public interest is furthered by supporting a nationwide multi-tiered network that provides all consumers with affordable access to wireline, broadband, and mobile services, deployed in an economically efficient manner and funded fairly.
- The identical support rule should be eliminated because it presently burdens New Jersey consumers without any direct benefit to New Jersey consumers.
- Ten states receive non-rural high cost support, which means that the vast majority of states, including New Jersey, contribute to the growing fund, but do not withdraw from the fund.

### C. SUMMARY

Rate Counsel supports the Commission in its long-overdue, comprehensive reform of high cost support. Rate Counsel's comments discuss the following:

- *The high-cost fund is long overdue for comprehensive reform:* During the past twelve years, consumers have been bearing the cost of an increasingly expensive

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<sup>7</sup> / Cable Facts 2005, New Jersey Board of Public Utilities, at 32 (available at <http://www.bpu.state.nj.us/bpu/pdf/cablepdfs/cablefacts2005.pdf>).

high cost subsidy, and, as Table 1 shows, in total, have paid almost \$40 billion to industry. Rate Counsel acknowledges that the purpose of the high cost fund is to make urban and rural rates comparable,<sup>8</sup> and to facilitate competition by making implicit support explicit,<sup>9</sup> but urges the Commission to assess whether consumers have benefited by a commensurate amount. Among other things, by supporting high cost areas, the USF should make it possible for carriers to lower rates in low-cost areas, yet Rate Counsel is unaware of rate reductions (or other benefits) that, in sum, yield a consumer benefit comparable to the approximate \$40 billion in USF subsidies provided to industry.<sup>10</sup>

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<sup>8</sup> / 1996 Act, § 254(b).

<sup>9</sup> / The 1996 Act expressly states that the support a carrier receives “should be explicit and sufficient to achieve the purposes of this section.” 1996 Act, at Section 254(e). See, also, In the Matter of Access Charge Reform; Price Cap Performance Review for LECs; Low-Volume Long Distance Users; Federal-State Joint Board on Universal Service, FCC CC Docket Nos. 96-262, 94-1, 99-249, 96-45, Order on Remand, Rel. July 10, 2003, at para. 5, stating: “One of the primary purposes of universal service support is to help provide access to telecommunications service in areas where the cost of such service otherwise might be prohibitively expensive. Historically, this purpose has been achieved both through explicit monetary payments and implicit support flows that enable carriers to serve high-cost areas at below-cost rates. Congress established principles for the preservation and advancement of universal service in the Telecommunications Act of 1996, directing the Commission to create explicit universal service support mechanisms that will be specific, predictable, and sufficient. The Commission has approached this goal by, among other things, pursuing reforms intended to make universal service explicit and portable to competitive carriers.”

<sup>10</sup> / Instead, in many jurisdictions where ILECs have been granted regulatory flexibility, they have raised rates. See, e.g., In the Matter of Petitions of the Verizon Telephone Companies for Forbearance Pursuant to 47 U.S.C. §160(c) in the Boston, New York, Philadelphia, Pittsburgh, Providence and Virginia Beach Metropolitan Statistical Areas, FCC WC Docket No. 06-172, Memorandum Opinion and Order, ex parte filing, Pennsylvania Office of Consumer Advocate, November 7, 2007. The following is a link to these comments:  
[http://fjallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native\\_or\\_pdf=pdf&id\\_document=6519810330](http://fjallfoss.fcc.gov/prod/ecfs/retrieve.cgi?native_or_pdf=pdf&id_document=6519810330).

**Table 1<sup>11</sup>**

**The Present Value of Total High Cost Funds Since 1996 Is Almost \$40 Billion**

<b>Year</b>	<b>Nominal Dollars</b>	<b>2008 Dollars</b>
1996	\$1,188,000,000	\$1,623,625,565
1997	\$1,263,000,000	\$1,675,295,113
1998	\$1,690,305,004	\$2,210,238,229
1999	\$1,717,980,381	\$2,210,920,648
2000	\$2,234,771,101	\$2,786,225,218
2001	\$2,591,627,306	\$3,120,861,779
2002	\$2,934,995,831	\$3,494,592,899
2003	\$3,265,232,900	\$3,775,258,356
2004	\$3,468,375,683	\$3,943,368,056
2005	\$3,796,234,466	\$4,190,108,636
2006	\$4,096,321,267	\$4,364,324,168
2007	\$4,286,733,000	\$4,459,466,222
Total Disbursements, 1996-2007	\$32,533,576,939	\$37,854,284,890

Note: Nominal disbursements are inflated to 2008 dollars using the Consumer Price Index for All Urban Consumers (All Items). The CPI for February 2008, 211.7, is divided by the CPI for February of each year, and multiplied by the nominal amount of support for that year. This yields the 2008 value of support for past years.

- *USF support for broadband in unserved and underserved areas:* Rate Counsel has been a long-time advocate of expanding universal service to include affordable broadband access.<sup>12</sup> Therefore Rate Counsel supports the Commission’s proposed inclusion of affordable broadband as a supported service. Furthermore, any grants should be awarded to states proportionally, based either on population or households.

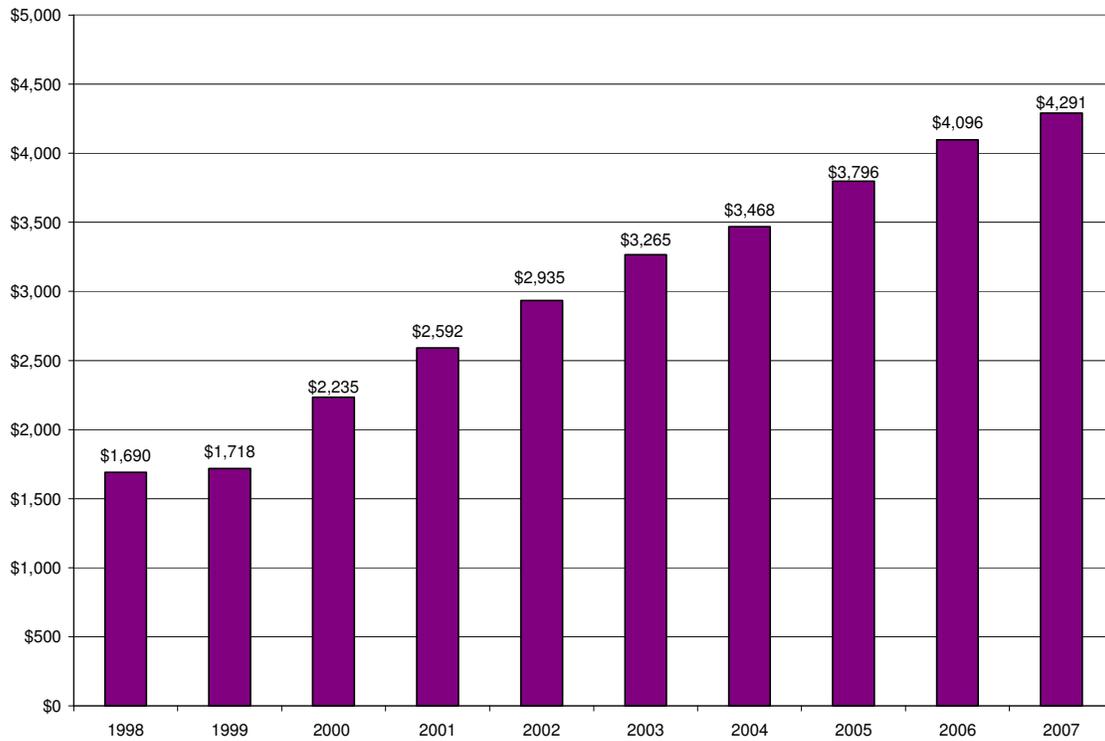
<sup>11</sup> / 2007 Monitoring Report, Tables 3.1 and 3.14.

<sup>12</sup> / *See, e.g.*, In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Comments of the New Jersey Division of The Ratepayer Advocate, September 30, 2005 (“Rate Counsel 2005 USF Initial Comments”), at 26.

- *Capping the spiraling costs associated with the existing eligible telecommunications carrier (“ETC”) rule is essential:* Purportedly to further universal service, high cost funds presently are subsidizing wireless deployment that, for the most part, does not substitute for wireline nor does it serve unserved and underserved areas. Rate Counsel supports the imposition of an immediate cap on competitive eligible telecommunications carrier (“CETC”) funds. Figure 1 shows the escalating costs of high cost support.

**Figure 1<sup>13</sup>**

**High-Cost Support Payments  
(millions)**



<sup>13</sup> / 2007 Monitoring Report, Table 3.14.

- *Excessive USF assessments will jeopardize USF goals:* Because consumers pay for USF, as USF assessments increase, telephone service becomes less affordable, thereby thwarting the achievement of universal service.
- *Some states are contributing disproportionately to USF programs:* In addition to the apparently limitless increases to the high-cost fund, some states are bearing a disproportionate share of the USF burden because they contribute vastly more to the fund than is distributed to them by the fund. As Table 2 shows, ten states receive non-rural high cost support, which means that the vast majority of states contribute to the growing fund, but do not withdraw from the fund.

**Table 2<sup>14</sup>**

**Non-Rural High Cost Support Payments by State or Jurisdiction  
(2000 through 2007)**

	2000	2001	2002	2003	2004	2005	2006	2007
Alabama	\$51,743,652	\$46,445,571	\$42,927,069	\$42,116,427	\$42,621,753	\$45,789,693	\$45,684,349	\$44,671,947
Kentucky	\$1,165,656	\$0	\$3,262,920	\$3,189,189	\$16,315,065	\$16,997,301	\$17,991,503	\$16,958,527
Maine	\$10,775,778	\$8,873,436	\$5,480,907	\$5,653,734	\$2,137,286	\$2,044,395	\$2,111,690	\$2,148,746
Mississippi	\$103,707,456	\$103,996,830	\$120,595,569	\$120,967,993	\$136,773,388	\$146,626,579	\$198,419,990	\$198,762,670
Montana	\$1,541,526	\$4,383,033	\$10,887,342	\$10,757,091	\$17,806,404	\$19,867,213	\$24,526,415	\$20,641,830
Nebraska	\$0	\$0	\$0	\$0	\$4,189,576	\$7,084,560	\$13,215,293	\$10,753,528
South Dakota	\$0	\$0	\$0	\$0	\$1,536,621	\$2,455,359	\$3,278,097	\$2,550,483
Vermont	\$15,103,584	\$10,007,652	\$9,117,498	\$9,646,596	\$10,792,938	\$10,294,152	\$10,088,233	\$9,891,391
West Virginia	\$31,234,866	\$25,875,165	\$30,651,192	\$31,654,752	\$25,846,873	\$26,327,823	\$27,868,317	\$26,941,756
Wyoming	\$3,399,585	\$6,150,825	\$9,879,543	\$10,044,726	\$15,405,661	\$14,353,070	\$14,330,469	\$13,764,103
Total	\$218,672,103	\$205,732,512	\$232,802,040	\$234,030,508	\$273,425,565	\$291,840,145	\$357,514,356	\$347,084,981

Table 3 below shows the amount of total high cost support that each state or jurisdiction receives, ranked by the absolute levels of distribution. Consumers throughout the country pay USF contributions based on their telephone bills. As a result, consumers in many states and jurisdictions contribute significantly (and by

<sup>14</sup> / *Id.*, Table 3.9. States not listed did not receive any High-Cost Model Support from 2000 through 2007.

increasing amounts), but receive little from the fund. As consumers' contributions to the fund increase, these USF assessments jeopardize the affordability of telephone service, thwarting the achievement of universal service.

**Table 3<sup>15</sup>**  
**Total High Cost Support**  
**By State or Jurisdiction, 1998 and 2007**  
**(ranked from least to most, based on 2007 distributions)**

<u>State / Jurisdiction</u>	<u>1998</u>	<u>2007</u>	<u>State / Jurisdiction</u>	<u>1998</u>	<u>2007</u>
District of Columbia	\$0	\$0	Arizona	\$32,845,473	\$75,109,935
Rhode Island	\$0	\$34,629	North Carolina	\$40,762,084	\$76,875,816
Delaware	\$0	\$262,428	South Carolina	\$44,424,832	\$78,999,654
N. Mariana Islands	\$4,236,713	\$998,397	Virginia	\$12,440,891	\$80,250,078
New Jersey	\$2,976,024	\$1,343,961	Montana	\$42,065,201	\$80,881,527
Connecticut	\$1,212,720	\$1,797,312	Colorado	\$43,928,578	\$82,598,364
Massachusetts	\$489,687	\$2,553,294	Florida	\$20,036,950	\$82,938,054
American Samoa	\$0	\$2,735,706	North Dakota	\$21,101,916	\$86,249,343
Maryland	\$569,028	\$4,393,797	Nebraska	\$19,868,058	\$89,938,135
Guam	\$1,006,872	\$9,393,681	South Dakota	\$16,924,254	\$91,951,968
New Hampshire	\$8,487,987	\$9,824,853	Missouri	\$47,215,940	\$91,989,138
Utah	\$9,928,920	\$24,451,608	Kentucky	\$24,460,486	\$98,331,778
Virgin Islands	\$16,199,322	\$25,034,148	California	\$52,643,600	\$99,817,854
Vermont	\$12,539,982	\$31,733,581	Georgia	\$74,656,229	\$111,964,104
Nevada	\$10,462,430	\$31,745,628	Alabama	\$38,830,293	\$112,840,101
Maine	\$18,175,357	\$36,543,758	Washington	\$40,942,959	\$114,021,990
Ohio	\$14,040,836	\$41,624,598	Iowa	\$25,990,409	\$121,217,451
Hawaii	\$286,766	\$46,556,142	Oklahoma	\$59,502,768	\$129,397,671
Idaho	\$28,885,473	\$51,495,363	Arkansas	\$68,338,557	\$129,432,693
New York	\$35,363,672	\$52,416,777	Minnesota	\$37,439,032	\$133,422,702
Tennessee	\$27,395,910	\$53,251,977	Wisconsin	\$49,669,554	\$142,031,877
Pennsylvania	\$22,169,364	\$58,512,894	Louisiana	\$65,332,257	\$148,693,794
Wyoming	\$20,786,386	\$58,755,622	Alaska	\$64,131,034	\$160,071,648
Illinois	\$22,589,490	\$63,117,972	Puerto Rico	\$138,864,798	\$185,631,099
West Virginia	\$24,421,006	\$63,645,337	Kansas	\$59,007,494	\$215,837,688
Michigan	\$31,188,240	\$65,217,555	Texas	\$123,089,671	\$239,740,953
New Mexico	\$33,552,080	\$67,147,917	Mississippi	\$26,793,296	\$281,209,066
Indiana	\$16,278,436	\$70,649,289			
Oregon	\$35,755,689	\$73,912,629	<b>Total</b>	<b>\$1,690,305,004</b>	<b>\$4,290,595,334</b>

New Jersey receives approximately \$50 million in total USF support,<sup>16</sup> of which only \$1.3 million is high-cost support, and, as Table 4 shows, pays approximately

<sup>15</sup> / *Id.*, Table 3.14. In New Jersey, Verizon, which serves the vast majority of lines, did not receive any high cost support. *Id.*, at Table 3.30.

\$248 million in total USF support.<sup>17</sup> In other words, New Jersey pays 3.69% of the nation's USF and receives 0.75% of the nation's support.

**Table 4<sup>18</sup>**

**Universal Service Support Mechanisms by State:  
Annual Payments and Contributions (2006)  
(Thousands)**

<u>State / Jurisdiction</u>	<u>Contribution</u>	<u>% of Total</u>	<u>State / Jurisdiction</u>	<u>Contribution</u>	<u>% of Total</u>
Alabama	\$100,753	1.50%	Nebraska	\$37,456	0.56%
Alaska	\$22,002	0.33%	Nevada	\$65,681	0.98%
American Samoa	\$249	0.00%	New Hampshire	\$35,867	0.53%
Arizona	\$127,607	1.90%	New Jersey	\$247,748	3.69%
Arkansas	\$60,848	0.91%	New Mexico	\$44,762	0.67%
California	\$730,849	10.88%	New York	\$413,887	6.16%
Colorado	\$121,905	1.82%	North Carolina	\$201,024	2.99%
Connecticut	\$102,686	1.53%	North Dakota	\$14,892	0.22%
Delaware	\$25,757	0.38%	N. Mariana Islands	\$1,051	0.02%
Dist. of Columbia	\$32,689	0.49%	Ohio	\$230,522	3.43%
Florida	\$469,930	7.00%	Oklahoma	\$73,973	1.10%
Georgia	\$217,680	3.24%	Oregon	\$81,119	1.21%
Guam	\$3,935	0.06%	Pennsylvania	\$280,967	4.18%
Hawaii	\$27,938	0.42%	Puerto Rico	\$57,810	0.86%
Idaho	\$33,796	0.50%	Rhode Island	\$21,882	0.33%
Illinois	\$275,354	4.10%	South Carolina	\$97,199	1.45%
Indiana	\$126,200	1.88%	South Dakota	\$16,639	0.25%
Iowa	\$61,954	0.92%	Tennessee	\$130,517	1.94%
Kansas	\$58,993	0.88%	Texas	\$445,509	6.63%
Kentucky	\$84,622	1.26%	Utah	\$50,314	0.75%
Louisiana	\$94,640	1.41%	Vermont	\$17,433	0.26%
Maine	\$31,423	0.47%	Virgin Islands	\$7,745	0.12%
Maryland	\$152,393	2.27%	Virginia	\$193,667	2.88%
Massachusetts	\$156,510	2.33%	Washington	\$142,810	2.13%
Michigan	\$193,406	2.88%	West Virginia	\$42,958	0.64%
Minnesota	\$107,048	1.59%	Wisconsin	\$113,556	1.69%
Mississippi	\$60,094	0.89%	Wyoming	\$15,116	0.23%
Missouri	\$128,950	1.92%			
Montana	\$23,457	0.35%	Total	\$6,715,770	100.00%

<sup>16</sup> / *Id.*, at Table 1.12. The \$50 million encompasses support for Lifeline and Schools and Hospitals programs.

<sup>17</sup> / *Id.*

<sup>18</sup> / 2007 Monitoring Report, Table 1.12. The monies shown are for all universal service programs.

- *Reverse auctions should be explored on a pilot basis:* Rate Counsel acknowledges the theoretical appeal of reverse auctions as a way to identify the most efficient supplier, but opposes the use of reverse auctions for distributing high cost funds. The benefits of reverse auctions are not sufficient to warrant the substantial administrative resources that would be associated with designing and implementing such a plan to replace the existing high-cost mechanism. Rate Counsel supports the use of a reverse auction on a pilot basis to target support to deploy broadband in underserved and unserved areas.
- *The Commission should cap the entire high cost fund:* As Rate Counsel has stated in its other universal service pleadings, consumers ultimately pay for universal service programs. Therefore Rate Counsel supports the Commission’s proposal to cap high cost funds and to transition the support to a Mobility Fund, a Broadband Fund, and a Provider of Last Resort Fund, such that the combined total of the three funds stays within that cap.
- *Definitional issues remain unresolved:* For example, the Mobility Fund would support the construction of wireless voice in unserved areas with “*a significant population density.*”<sup>19</sup> The Joint Board proposes to support broadband and wireless in those regions of the country in which there is not “*a plausible economic case*” for deployment, which presumably means in those instances, where the industry would not consider deployment to be profitable.<sup>20</sup> Rate Counsel urges the Commission to define these terms explicitly.

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<sup>19</sup> / Recommended Decision, at para. 16 (emphasis added).

<sup>20</sup> / *Id.*, at para. 12 (broadband) and para. 16 (mobility) (emphasis added).

## II. PRINCIPLES AND CONSUMER IMPACT

### A. PRINCIPLES

Universal service is a cornerstone of sweeping legislation enacted more than a decade ago. The roadmap to achieve universal service continues, however, to elude the nation. In some ways, the nation has succeeded: the overall telephone penetration rate for the United States is 94.6% as of March 2007, although for those in the lowest income bracket under analysis (households earning less than about \$20,000), the penetration rate is only 88.4%.<sup>21</sup> In other ways, the system is flawed, with the universal service fund growing without control from \$2.3 billion to nearly \$7 billion between 1998 and 2007.<sup>22</sup>

The USF, which is funded through line items on consumers' telephone bills, has risen substantially, despite purported competition (which should drive down costs). Without reform, the USF will continue to increase, further burdening customers. For diverse reasons,<sup>23</sup> the United States does not yet offer affordable ubiquitous broadband

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<sup>21</sup> / FCC, Telephone Penetration by Income by State, Rel. March 2008, at Table 4. The overall penetration rate for New Jersey is 96.1% as of March 2007. The lowest income bracket in New Jersey had a penetration rate of just 90.8%, while the highest income bracket, households earning more than about \$80,000, had a penetration rate of 98.6%.

<sup>22</sup> / USAC 2007 Annual Report, at 2 and 51. These amounts include all USF programs (i.e., High Cost, Rural Health Care, Schools and Libraries, and Low Income programs).

<sup>23</sup> / For example, Rate Counsel continues to disagree respectfully with the Commission's landmark decision in 2005, in which it determined that broadband is an information service, and thereby thwarted national and federal state policy makers' opportunities for requiring ubiquitous broadband deployment. *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities, Universal Service Obligations of Broadband Providers*, CC Docket No. 02-33, et al., *Report and Order and Notice of Proposed Rulemaking*, 20 FCC Rcd 14853 (2005) ("Wireline Broadband Order"). As a result, the digital divide has become more entrenched, as incumbent local exchange carriers have deployed broadband where they can reap high profits (which accrue to the unregulated line of business) and have ignored consumers in areas that are not financially attractive. Leaving broadband deployment up to the unilateral decision-making of ILECs, who are beholden to shareholders and not consumers, has placed federal and state regulators in the unenviable position of needing to extract broadband promises as part of alternative regulation plans, merger approvals, and sales of their operations. See e.g., *Investigation into a Successor Incentive Regulation Plan for Verizon New England Inc., d/b/a Verizon Vermont*, Vermont Public Service Board Docket No. 6959, *Investigation into Tariff Filing of Verizon New England Inc., d/b/a Verizon Vermont, in re: Compliance Filing in Docket 6959*, Vermont PSB Docket No. 7142, Order Adopting Amended Plan, April 27, 2006, at page 4; *In the Matter of SBC Communications Inc. and AT&T Corp.*

access, and, instead, its deployment and broadband subscription fall well short of global standards.

Rate Counsel, therefore, welcomes the Commission's rulemakings, in which it seeks to limit growth in the USF and to ensure that consumers throughout the country have affordable access to wireline, wireless and broadband services. Rate Counsel has contributed regularly to the Commission's USF<sup>24</sup> and broadband<sup>25</sup> proceedings, and welcomes the Commission's efforts to identify and to implement comprehensive reform to the nation's USF programs.

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*Applications for Approval of Transfer of Control*, WC Docket No. 05-65, Memorandum Opinion and Order, Rel. November 17, 2005, at Appendix F; *Verizon New England, Inc., Bell Atlantic Communications, Inc., Nynex Long Distance Co., Verizon Select Services, Inc. And Fairpoint Communications, Inc. - Petition for Authority to Transfer Assets and Franchise*, New Hampshire PUC Docket No. DT 07-011, Order Approving Settlement Agreement with Conditions, February 25, 2008, at 24-26. This approach has created a nonsensical patchwork of availability and rates where consumers' access to an increasingly essential capability depends not on ILECs' historic obligation to serve but rather on regulatory bartering.

<sup>24</sup> / In 2005, the Federal Communications Commission, issued "Federal-State Joint Board on Universal Service Seeks Comment on Proposals to Modify the Commission's Rules Relating to High-Cost Universal Service Support," Public Notice, FCC 05J-1, August 17, 2005 ("Public Notice"). In response, Rate Counsel submitted initial and reply comments in CC Docket No. 96-45 (September 30, 2005 and October 31, 2005, respectively). See also, In the Matter of Comprehensive Review of Universal Service Fund Management, Administration, and Oversight, WC Docket No. 05-195, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Schools and Libraries Universal Service Support Mechanism, CC Docket No. 02-6, Rural Health Care Support Mechanism, WC Docket No. 02-60, Lifeline and Link-Up, WC Docket No. 03-109, Changes to the Board of Directors for the National Exchange Carrier Association, Inc., CC Docket No. 97-21, Comments of The New Jersey Division of The Ratepayer Advocate, October 18, 2005; In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, High-Cost Universal Service Support, WC Docket No. 05-337, Comments of the New Jersey Division of The Ratepayer Advocate, March 27, 2006, Reply Comments of the New Jersey Division of The Ratepayer Advocate, May 26, 2006.

<sup>25</sup> / See, e.g., In the Matter of Consumer Protection in the Broadband Era, WC Docket No. 05-271, Initial Comments of the New Jersey Division of the Ratepayer Advocate, Initial Comments, January 17, 2006; In the Matter of Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996, Comments of the New Jersey Division of Rate Counsel, May 16, 2007; In the Matter of Development of Nationwide Broadband Data to Evaluate Reasonable and Timely Deployment of Advanced Services to All Americans, Improvement of Wireless Broadband Subscribership Data, and Development of Data on Interconnected Voice over Internet Protocol (VoIP) Subscribership, WC Docket No. 07-38, Comments of the New Jersey Division of Rate Counsel, June 15, 2007, and Reply Comments of the New Jersey Division of Rate Counsel, July 16, 2007.

With the economy declining, gasoline prices rising, fuel costs increasing, food costs rising, and housing prices declining, affordable access to basic and advanced services has become yet more critically important, as has the efficient and fair design of national universal service funds.

The principles of universal service set forth in Section 254(b) of the Act include:

(1) *Quality and Rates* – Quality services should be available at just, reasonable, and affordable rates.

(2) *Access to Advanced Services* – Access to advanced telecommunications and information services should be provided in all regions of the Nation.

(3) *Access in rural and high cost areas* – Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.

(4) *Equitable and Nondiscriminatory contributions* – All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.

(5) *Specific and predictable support mechanisms* – There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.

(6) *Access to Advanced Telecommunications Service for Schools, Healthcare, and Libraries*- Elementary and secondary schools and classrooms, health care providers, and libraries should have access to advanced telecommunications services as described in subsection (h).

(7) *Additional principles* – Such other principles as the Joint Board and the Commission determine are necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act.

## B. CONSUMER IMPACT

As a threshold matter, Rate Counsel urges the Commission to consider the impact of any USF programs on consumers.<sup>26</sup> The increasing fund (and thus USF fees on consumer bills) threatens the affordability of basic services, and this is especially true in a state like New Jersey where carriers receive no non-rural high cost support yet consumers continue to pay increasing USF fees.<sup>27</sup> As noted by the Court in *Qwest II*: “excessive subsidization arguably may affect the affordability of the telecommunications services, thus violating the principle in §254(b)(1).”<sup>28</sup> Figure 2 below shows that high cost support per line increased 36% from 2002 to 2006.

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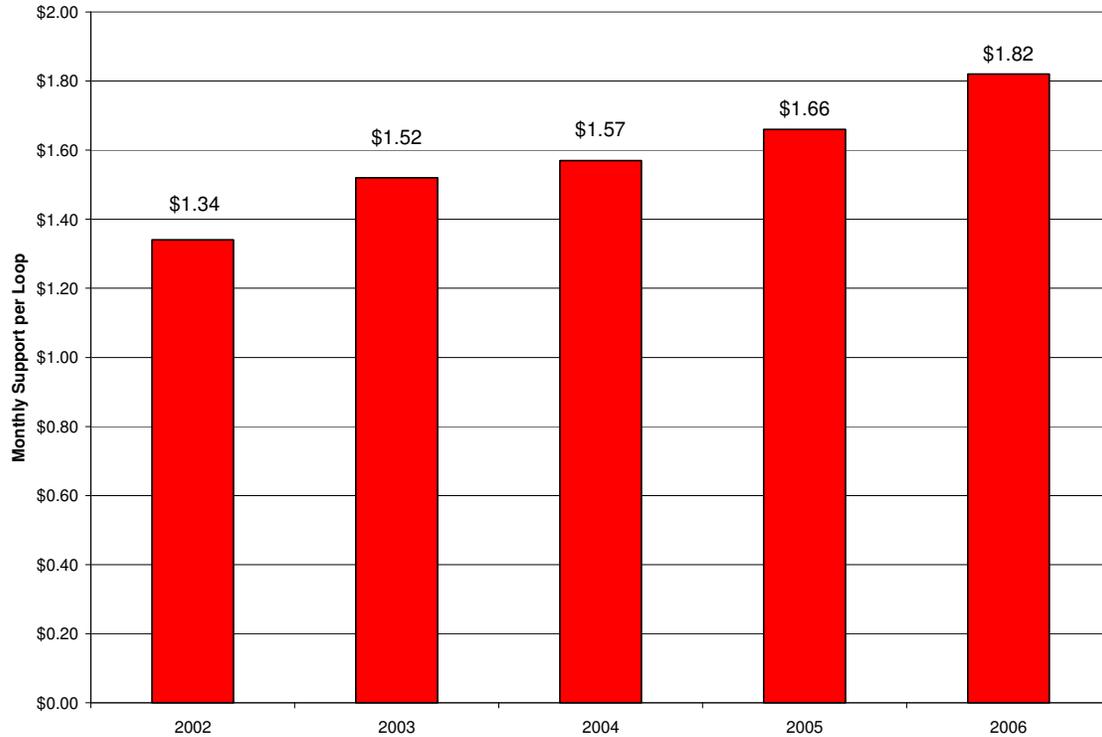
<sup>26</sup> / As stated by Commissioner Tate, “we must remain mindful that it is consumers who ultimately pay universal service contributions, and any increase in the fund size will increase the burden on consumers.” Recommended Decision, Statement of Commissioner Deborah Taylor Tate, at 30.

<sup>27</sup> / Rate Counsel has raised similar concerns previously. See In the Matter of High-Cost Universal Service Support, WC Docket No. 05-337; Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Comments of the New Jersey Division of Rate Counsel, March 27, 2006 (“Rate Counsel 2006 Initial Comments”), at 12-13.

<sup>28</sup> / *Qwest Corp. v. FCC*, 398 F.3d 1222 (10<sup>th</sup> Cir. 2005) (“Qwest II”), at 1234, citing *Qwest Corp. v. FCC*, 258 F.3d 1191 (10<sup>th</sup> Cir. 2001) (“Qwest I”), at 1200.

Figure 2<sup>29</sup>

**Average Monthly High Cost Support per Loop, Nationwide**



Furthermore, as Rate Counsel has previously stated, the Commission’s resolution of reforms to the high cost funding mechanism relates directly to other pending proceedings. For example, Rate Counsel cautioned the Commission against using universal service funding to protect ILECs from the effects of competition stating:

[Rate Counsel] also cautions the Commission against creating a bloated universal service fund to address ILECs’ request to be protected against revenue erosion. [Rate Counsel] concurs with the statement of the New York Department of Public Service that it “is especially important that federal universal service funding not be used as a mechanism to shield significant portions of the ILECs’ revenues from competitive erosion.”<sup>30</sup>

<sup>29</sup> / Federal-State Joint Board on Universal Service, Universal Service Monitoring Reports, 2003 - 2007.

<sup>30</sup> / In the Matter of Developing a Unified Intercarrier Compensation Regime, CC Docket No. 01-92, Reply Comments of the New Jersey Division of the Ratepayer Advocate, Reply Comments, July 25, 2005, at 8, citing Comments of the New York Department of Public Service at 5.

Universal Service has become essentially a pass-through by which consumers provide a guaranteed revenue stream to service providers.<sup>31</sup>

Rate Counsel has previously raised concerns about the use of funds for CETCs and asserted that CETCs should be required to demonstrate specifically how they are using the high cost funds to narrow the urban/rural gap. Throwing money at the problem might satisfy the Court's mandate but would seriously disserve consumers, who ultimately pay higher rates. CETCs should be required to demonstrate that they are more efficient than the incumbent wireline carrier.<sup>32</sup> Similarly, any expansion of universal service support should only subsidize the most efficient carriers.

As a result of the 1996 Act and in the name of replacing purportedly eroded implicit support for high cost areas, non-rural carriers are receiving millions of dollars that they would not otherwise have received. Meanwhile, the local competition (which Congress believed would jeopardize incumbents' implicit support) has not materialized, and now, consumers are harmed in multiple ways. Competitive choice is diminishing in the wake of major mergers, and yet consumers must simultaneously pay for high cost support.<sup>33</sup> All else being equal, if universal service funds are increasing in order to make implicit support explicit, then those rates which previously provided implicit support should be declining. Rate Counsel is unaware of any significant pattern of rate

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<sup>31</sup> / See In the Matter of High-Cost Universal Service Support, WC Docket No. 05-337; Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Reply Comments of the New Jersey Division of Rate Counsel, June 13, 2007 ("Rate Counsel 2007 USF Reply"), at 3.

<sup>32</sup> / See also Rate Counsel, In the Matter of High-Cost Universal Service Support, WC Docket No. 05-337; Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Rate Counsel 2006 Initial Comments, at 16.

<sup>33</sup> / *Id.*, at 2.

reductions, and, instead, has expressed concern to the Commission in other proceedings regarding a pattern of rate increases imposed by ILECs.

Also, several years ago, Rate Counsel recommended that carriers' receipt of universal service funds be linked to the demonstration of the provision of quality service throughout their supported areas.<sup>34</sup> This is more important than ever as states grapple with how to address declining service quality,<sup>35</sup> and as ILECs file forbearance petitions with the Commission, seeking to discontinue service quality reporting.<sup>36</sup>

### **III. HIGH-COST DISTRIBUTION REFORM**

#### **A. INTRODUCTION**

The Commission seeks comment on the Recommended Decision, released on November 20, 2007, of the Federal-State Joint Board on Universal Service ("Joint Board").<sup>37</sup> Rate Counsel welcomes the Joint Board's efforts to "address the long-term

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<sup>34</sup> / Rate Counsel 2005 USF Initial Comments, at 9.

<sup>35</sup> / *See, e.g.*, Verizon's Quality of Service Performance, New Hampshire Public Utilities Commission DT 04-019, Order Establishing Status Conference, Order No. 24,551, December 1, 2005; Verizon New England, Inc., Bell Atlantic Communications, Inc., NYNEX Long Distance Co., Verizon Select Services, Inc. and FairPoint Communications, Inc. Petition for Authority to Transfer Assets and Franchise, New Hampshire Public Utilities Commission Docket No. 07-011, Order Approving Settlement Agreement with Conditions, Order No. 24,823, February 25, 2008, at 71; New York Public Service Commission Press Release, "PSC Adopts Verizon's Service Improvement Plan," March 19, 2008; In The Matter of the Commission's Investigation Into Verizon Maryland Inc.'s Service Performance and Service Quality Standards, Maryland Public Service Commission Case No. 9114.

<sup>36</sup> / *See, e.g.*, *In the Matter of Petition of Embarq Local Operating Companies for Forbearance Under 47 U.S.C. §160(c) From Enforcement of Certain of ARMIS Reporting Requirements*, WC Docket No. 07-204; *In the Matter of Petition of Frontier and Citizens ILECs for Forbearance Under 47 U.S.C. §160(c) From Enforcement of Certain of the Commission's ARMIS Reporting Requirements*, WC Docket No. 07-204; *Petition of Verizon For Forbearance Under 47 U.S.C. §160(c) From Enforcement of Certain of the Commission's Recordkeeping and Reporting Requirements*, WC Docket No. 07-273; *In the Matter of Petition of Qwest Corporation for Forbearance from Enforcement of the Commission's ARMIS and 492 Reporting Requirements Pursuant to 47 U.S.C. §160(c)*, WC Docket No. 07-204; *In the Matter of Petition of AT&T Inc. for Forbearance Under 47 U.S.C. § 160 (c) from Enforcement of Certain of the Commission's ARMIS Reporting Requirements*, WC Docket No. 07-139.

<sup>37</sup> / Joint Board Comprehensive Reform NPRM, at para. 1; Federal-State Joint Board on Universal Service, WC Docket No. 05-337, CC Docket No. 96-45, Recommended Decision, FCC 07J-4, rel. November 20, 2007 ("Recommended Decision") (attached as Appendix A to Joint Board Comprehensive NPRM).

reform issues facing the high-cost universal service support system” and to “make fundamental revisions in the structure of existing Universal Service mechanisms.”<sup>38</sup> The Joint Board recommends three separate funds: the purpose of the Broadband Fund would be to facilitate construction of facilities for new broadband services to unserved areas; the Mobility Fund would seek to deploy wireless voice services to unserved areas; and a Provider of Last Resort (“POLR”) Fund would support carriers of last resort.<sup>39</sup> The Joint Board further recommends that the three funds operate within an overall funding cap “that is consistent with the current amount of high-cost funding,” with existing programs being transitioned “over a period of years” to the new three-fund structure.<sup>40</sup> Rate Counsel addresses each of these areas in these initial comments, and will elaborate further on reply, based on its review of others’ initial comments.

## **B. BROADBAND**

### **Universal service should encompass affordable broadband access at reasonable speed.**

Rate Counsel agrees with the Joint Board’s recommendation that the nation’s universal service goals should include the universal availability of broadband services.<sup>41</sup> Furthermore, any expansion of national universal service support to encompass broadband should ensure that broadband support is disbursed in proportion to states’ populations, and that broadband access is affordable. Although, for example, New Jersey may lack high-cost areas, there are many areas in New Jersey that lack broadband access that is affordable to the consumers in those communities. Rate Counsel has previously

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<sup>38</sup> / Recommended Decision, at para. 1.

<sup>39</sup> / *Id.*, at para. 11.

<sup>40</sup> / *Id.*

<sup>41</sup> / *Id.*, at para. 56.

supported inclusion of affordable broadband in supported services, for example, stating in comments filed in the 2006 USF proceeding that “[i]n order to fulfill the nation’s objective of universal service, advanced services must be available to and affordable by all consumers, regardless of geography or income.”<sup>42</sup>

In 2005, Rate Counsel also stated, among other things:

*The societal implications of the technology haves and have-nots.* Based on the [Rate Counsel’s] comprehensive examination of information provided in state and federal proceedings regarding mega-mergers between SBC and AT&T, and between Verizon and MCI, [Rate Counsel] is concerned that the merged companies’ priorities will veer even further toward big business, enterprise, and global customers and further away from the historic mission of providing basic local exchange service customers. Simultaneously, in pursuit of deploying fiber to the home, the companies will be targeting affluent, technologically-savvy households. The Commission should consider carefully the implications of a society with such widely disparate access to communications technology.

*Disparate levels of access to the Internet by diverse demographic groups* continues to provide evidence of a sobering digital divide that conflicts with the directive in the 1996 Act that “Consumers in all regions of the Nation, including low-income consumers...should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.” As the Commission recently stated, “[t]he availability of the Internet has had a profound impact on American life. This network of networks has fundamentally changed the way we communicate.” Not only should the Commission consider how best to promote universal service in rural areas, but also the Commission should evaluate the disparate levels of access to broadband and to the Internet throughout the country.<sup>43</sup>

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<sup>42</sup> / Rate Counsel 2006 Initial USF Comments, at 25.

<sup>43</sup> / Rate Counsel 2005 Initial USF Comments, citing to In the Matter of Transfer of Control filed by SBC Communications Inc. and AT&T Corp., FCC WC Docket No. 05-65; Joint Petition of SBC Communications Inc. and AT&T Corp., Together with its Certificated Subsidiaries for Approval of Merger, New Jersey Board of Public Utilities Docket No. TM05020168; In the Matter of Verizon Communications

Rate Counsel commends the Joint Board for its recommendation to expand the definition of universal service to comport with the reality of today's use of technology and telecommunications.

**The Commission should elicit detailed deployment data to facilitate mapping to support its achievement of broadband goals.**

Last month, the Commission adopted an Order and Further Notice of Proposed Rulemaking ("FNPRM") that seeks to improve its broadband subscribership data collection program. The Order will:

- Expand the number of broadband reporting speed tiers to capture more precise information about upload and download broadband speeds in the marketplace;
- Require broadband providers to report numbers of broadband subscribers by Census Tract, broken down by speed tier and technology type; and
- Improve the accuracy of information the Commission gathers about mobile wireless broadband deployment.<sup>44</sup>

In his statement, Commissioner Michael J. Copps highlights why these issues affect consumers: "Good data . . . is essential to making sure that markets work and consumers are protected."<sup>45</sup> Commissioner Copps further states:

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Inc. and MCI, Inc. Applications for Approval of Transfer of Control, FCC WC Docket No. 05-75; Joint Petition of Verizon Communications Inc. and MCI, Inc. for Approval of Merger, New Jersey Board of Public Utilities Docket No. TM05030189; In the Matters of Appropriate Framework for Broadband Access to the Internet over Wireline Facilities, CC Docket No. 02-33, Policy Statement, released September 23, 2005; and "Internet Access Disparity Hits Kids Hardest, Report Says," TR Daily, September 27, 2005; Are We Really A Nation Online? Ethnic and Racial Disparities in Access to Technology and Their Consequences, Report for the Leadership Conference on Civil Rights Education Fund Robert W. Fairlie, University of California, Santa Cruz and National Poverty Center, University of Michigan; "A Nation Online: Entering the Broadband Age," US Department of Commerce, Economics and Statistics Administration, National Telecommunications and Information Administration, September 2004, Appendix Tables 1 through 4, available at <http://www.ntia.doc.gov/reports/anol/NationOnlineBroadband04.doc>; Harris Interactive, Consumers and Communications Technologies: Current and Future Use, prepared for National Consumers League, final report June 29, 2005, at page 7.

<sup>44/</sup> Federal Communications Commission News Release, "FCC Expands, Improves Broadband Data Collection," March 19, 2008.

Equally important, the lack of high-quality broadband data has also been a huge impediment to formulating good policy. It affects the FCC, Congress, and all the other branches of government that have responsibility for the supply- and/or demand-side of the broadband equation. Surely by now—by 2008—we should be able to calculate the value proposition of American broadband—price per bit—and compare it to other countries, including those that have pursued more aggressive unbundling and/or national infrastructure approaches to building broadband. That would give us enormously important feedback on our own regulatory policies. Surely by now, we should be able to understand how demographic variables like income, race, gender, age and so forth are related to broadband adoption and availability. But we don't because of the indefensible way we have gone about gathering data—and still gather it today.<sup>46</sup>

Rate Counsel commends the Commission on its progress in updating data collection efforts, but notes that more information is needed to address the supply-side of the issue. The first task in extending broadband facilities to all Americans is to determine what areas currently lack broadband. The Commission should require all broadband service providers to self-report, in a consistent and comparable format, exactly where broadband is *available to consumers* today. It is not enough to enumerate the zip codes where “service is available,” which is the current reporting requirement. Nor is the demand-side reporting at the census tract level, which is the requirement of the new broadband data reporting regime, adequate to show where consumers have the *option* to purchase broadband service. If broadband is to be considered a “universal service,” as it should, then policymakers require greater deployment detail from broadband suppliers.

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<sup>45/</sup> Statement of Commissioner Michael J. Copps, Approving in Part and Concurring in Part, Re: In the Matter of Development of Nationwide Broadband Data to Evaluate Reasonable and Timely Deployment of Advanced Services to All Americans, Improvement of Wireless Broadband Subscribership Data, and Development of Data on Interconnected Voice over Internet Protocol (VoIP) Subscribership, WC Docket No. 07-38, R&O and FNPRM, March 19, 2008 (“Copps Data Collection Statement”). The Order and FNPRM have not yet been released.

<sup>46/</sup> *Id.*

Broadband service providers already have the data necessary to determine where service is available on an address-by-address basis.<sup>47</sup> These data should be incorporated into a geographic information system (“GIS”) application that allows for neighborhood-by-neighborhood mapping of service availability. Examining broadband availability over large regions does little to reveal whether households in particular neighborhood have access to broadband. For example, only 42% of households in the Cablevision of Newark’s system subscribe to cable service; in Comcast’s Jersey City cable system, only 47% subscribe to cable service; and in US Cable’s Paramus-Hillsdale cable system, only 40% of households subscribe to cable service.<sup>48</sup> The administration of statewide mapping programs and the determination of areas lacking affordable broadband service are tasks ideally delegated to states.

Although some carriers might balk at providing detailed deployment data, all carrier data could be masked upon receipt by the body collecting the data. Furthermore, the goal of data collection is not to show where carriers *do provide* service, but rather to show where they *do not*. The final product of state-based data collection would show only the areas that are currently *unserved* and *underserved*.<sup>49</sup>

As Commissioner Copps noted in his statement regarding the Broadband Data Reporting FNPRM,<sup>50</sup> broadband availability mapping data should be segmented into

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<sup>47</sup> / See, for example, the websites of Verizon (<http://www22.verizon.com/Content/ConsumerDSL/CheckByAddress/CheckByAddress.htm>), Comcast (<https://www.comcast.com/Localization/Localize.ashx?Referer=/Shop/Buyflow/Default.ashx&area=6>), and Cox (<https://secure.cox.com/service/offers/availableservices.aspx>), which have web-based dialogs through which a consumer can determine whether broadband service is available at his/her home address.

<sup>48</sup> / Cable Facts 2005, New Jersey Board of Public Utilities, at 32 (available at <http://www.bpu.state.nj.us/bpu/pdf/cablepdfs/cablefacts2005.pdf>).

<sup>49</sup> / Many households cannot afford broadband, and, therefore, are underserved.

<sup>50</sup> / Copps Data Collection Statement.

residential and business components. Because some carriers (typically small broadband providers) only serve business customers, and others (e.g., some cable companies) serve only residential customers, aggregating the two types of customers could give the Commission an overly optimistic picture of broadband availability. Mapping should clearly differentiate between the availability of broadband service for residential customers and for business customers.

**State-based mapping is feasible and necessary.**

The mapping efforts conducted by the ConnectKentucky (now ConnectedNation) have received mixed reviews,<sup>51</sup> but the general approach of states gathering data for analysis is essential in order to identify where market failures exist, that is, where consumers lack broadband access.<sup>52</sup> ConnectedNation shows the feasibility of widespread mapping and the importance of using company-based data and expertise to map deployment.

In addition to obtaining current deployment data from current service providers, Rate Counsel recommends that the Commission obligate those supported by the Broadband Fund to report the projected broadband build-out that would result from USF support with detailed geographic information. Furthermore, at the conclusion of the

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<sup>51</sup> / Public Knowledge's Art Brodsky argued that "Connect Kentucky is nothing more than a sales force and front group for AT&T paid for by the telecommunications industry and by state and federal governments that has achieved far more in publicity than it has in actual accomplishment." See "Connect Kentucky Provides Uncertain Model for Federal Legislation," January 9, 2008, available at <http://www.publicknowledge.org/node/1334>.

<sup>52</sup> / Rate Counsel is aware that other states have attempted valuable, but less thorough broadband mapping programs. For example, the Massachusetts Technology Collaborative, through its John Adams Innovation Institute, recently completed a mapping project showing broadband coverage in Massachusetts community-by-community. Rather than relying on actual deployment data from service providers, however, this mapping was based on surveys sent to residential and business consumers, asking about the availability of broadband service. The resulting report categorized Massachusetts' 351 communities according to whether the community is "unserved" (entire town has no access to broadband), "underserved" (broadband is available in a limited area), "monopoly," "duopoly," or "competitive" (three or more broadband providers). See <http://www.mtpc.org/broadband>.

support term, the grantees should be required to compare actual deployment with planned deployment. Because the purpose of the Broadband Fund is to support deployment, if any carrier is not demonstrating increased broadband deployment as a result of the subsidy it receives, its participation should be curtailed.

**The growth in subscribership and deployment is slowing.**

Regulators currently lack sufficient data to allow for complete analysis of current broadband deployment. As a proxy for deployment, however, Figure 3 shows the residential broadband subscribership data collected by the Commission from December 1999 through June 2007.<sup>53</sup> The chart shows that broadband subscribership has increased substantially during every six-month period since broadband reporting began in December 1999, implying that broadband deployment is proceeding well without special efforts from the Commission.

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<sup>53</sup> / FCC, High-Speed Services for Internet Access: Status as of June 30, 2007, Released March 2008, at Table 4. This table presents data for “Advanced Services Lines,” which are defined by the FCC as those capable of transmitting at least 200 kpbs in each direction. Because not all consumers purchase broadband service where it is available, subscription data necessarily underestimates deployment.

**Figure 3**

**Demand for Residential Broadband**

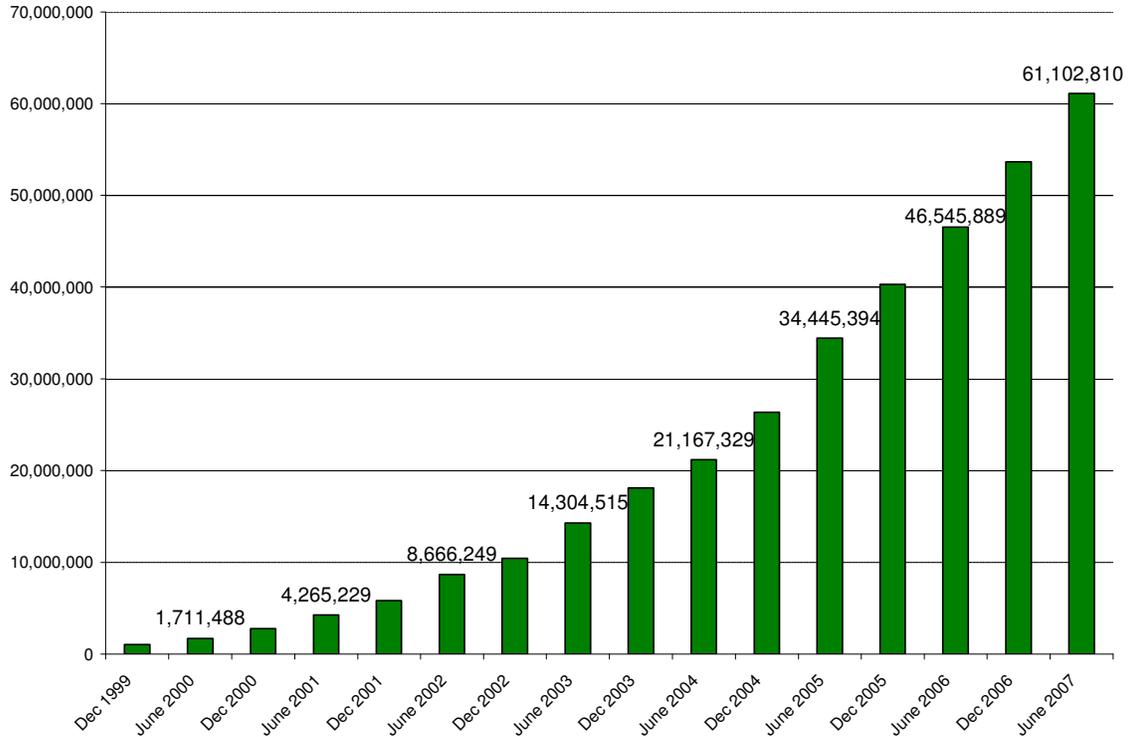
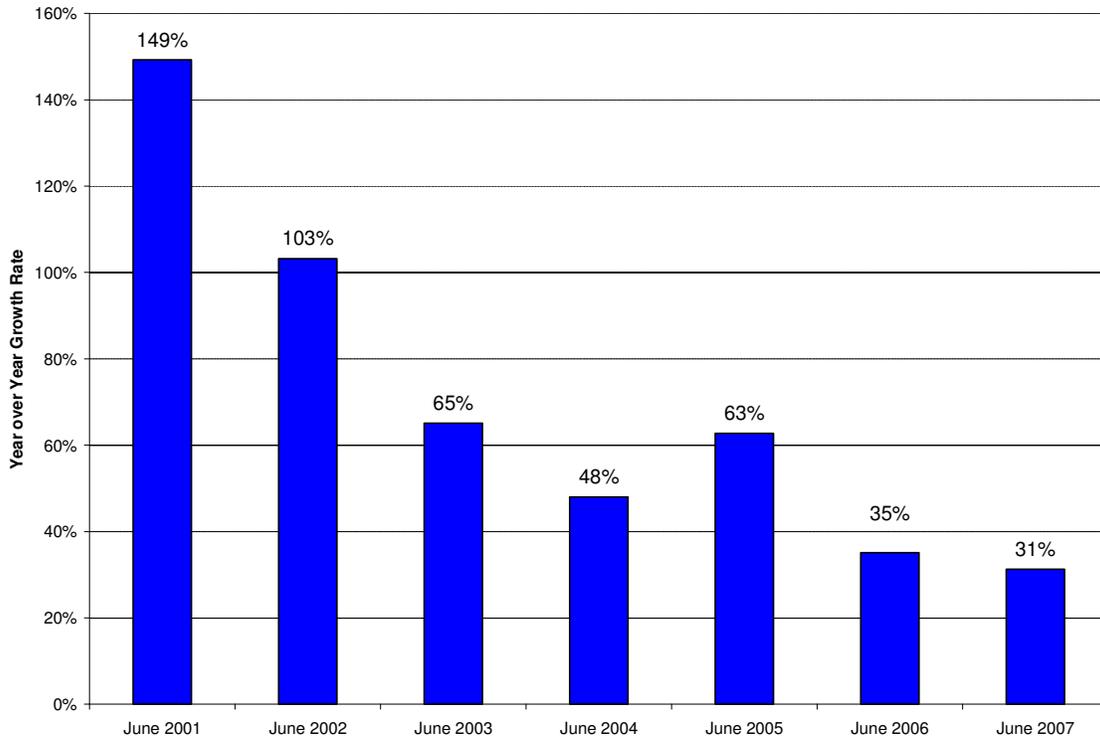


Figure 4 presents the same data included in Figure 3, but instead shows the year-over-year growth in broadband subscribership. When considered in this way, the data show that growth in subscribership is slowing. Several factors could explain the slowing growth in subscribership: 1) the previous success in signing-up customers where broadband is already available (which diminishes the number of people likely to subscribe), 2) the slowing deployment of broadband capability to hard-to-reach and sparsely-populated areas (which reduces overall availability), and 3) consumers' budget constraints (particularly where broadband is not affordable). The first reason is positive: customers are adopting broadband technology where it is available. The second and third

reasons justify universal service support: those in unserved or underserved areas are unable to adopt broadband.

**Figure 4<sup>54</sup>**

**Growth in Demand for Residential Broadband**



The areas that today remain without access to broadband service likely include those that are unprofitable, and yet, deployment of broadband to these areas will have positive effects and externalities far in excess of the ability of consumers to surf the Internet. As was stated recently, the increased deployment of broadband services “is an equalizing tool that will help not only with employment, but education and health care as well.”<sup>55</sup> Citizens in unserved and underserved areas deserve the support of the

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<sup>54</sup> / *Id.*

<sup>55</sup> / TR Daily, April 3, 2008. TR Daily quoted Representative Sheila Jackson, of Texas as saying, “Put a computer in front of somebody, and you open their eyes to the world.” *Id.*

Commission in connecting to the modern information economy. Furthermore, broadband needs not only to be *available* but also *affordable*. Rate Counsel supports the Joint Board’s recommendation to make broadband eligible for USF support.<sup>56</sup>

Cable companies and ILECs earn huge returns on their broadband investment, without any offsetting compensation to regulated services. Therefore, Rate Counsel concurs with Commissioner Copps that the Commission should include broadband “on both the distribution and contribution side of the ledger.”<sup>57</sup> Rate Counsel first computed an estimate of the Bells’ DSL revenues in 2006, and, specifically, estimated that Verizon, AT&T, Qwest, and BellSouth generated between \$3.3 billion and \$11.9 billion in DSL revenues.<sup>58</sup> Using the same methodology (multiplying the number of broadband connections by the lowest and highest priced plans available from each BOC), Rate Counsel estimates BOC broadband revenues of between \$4.9 billion and \$18 billion for 2007, as Table 5 shows.

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<sup>56</sup> / Recommended Decision, at para. 56.

<sup>57</sup> / Reverse Auctions NPRM, Statement of Commissioner Michael J. Copps, Approving in FCC 08-22, Approving in FCC 08-4, Approving in Part, Dissenting in Part in FCC 08-5, at 31.

<sup>58</sup> / In the Matter of Jurisdictional Separations and Referral to the Federal-State Joint Board, CC Docket No. 80-286, Comments of The National Association of State Utility Consumer Advocates, The New Jersey Division of Rate Counsel and The Maine Office of The Public Advocate, at 5-8; Affidavit of Susan M. Baldwin on behalf of the New Jersey Division of Rate Counsel and the National Association of State Utility Consumer Advocates, August 22, 2006, at Table 2 (estimate of 2005 revenues).

**Table 5<sup>59</sup>**

**Estimates of Bells' DSL Revenues (2007)**

	Number of Connections	Monthly Rates		Estimated 2007 Revenues	
		Lowest Price	Highest Price	Low Estimate	High Estimate
AT&T	14,586,000	\$12.99	\$54.99	\$2,273,665,680	\$9,625,009,680
Qwest	2,611,000	\$26.99	\$62.33	\$845,650,680	\$1,952,923,560
Verizon	8,235,000	\$17.99	\$64.99	\$1,777,771,800	\$6,422,311,800
Total RBOCs	25,432,000			\$4,897,088,160	\$18,000,245,040

Notes: The Low Estimate is calculated by multiplying the number of DSL connections by the lowest advertised monthly rate for DSL service, times 12. The High Estimate is calculated by multiplying the number of DSL connections by the highest advertised monthly rate, times 12. AT&T connections include DSL, AT&T U-verse high speed Internet and satellite broadband services. Verizon connections include approximately 1.5 million FiOS connections.

Statements in the companies' quarterly reports show that even rough estimates such as these have some merit. For example, AT&T states, "AT&T's broadband revenues totaled \$1.4 billion in the fourth quarter, up 13.7 percent versus the year-earlier quarter,"<sup>60</sup> which implies that AT&T's broadband revenues were approximately \$5 billion for the year. Qwest reported \$1.2 billion in revenue for mass market data, internet, and video products in 2007.<sup>61</sup> Verizon provides a revenue summary for all of its data services together: "For the full year, data revenues were \$18.1 billion, an increase of 12.4 percent over 2006" and further states that "[t]his reflects increasing revenues from consumer broadband, such as FiOS services and Verizon High Speed Internet (DSL), as well as from wholesale data transport and sales of Verizon Business data services."<sup>62</sup>

<sup>59</sup> / Websites for AT&T, Qwest, and Verizon, visited 4/10/2008; AT&T *4Q 2007 Investor Briefing*; Qwest *Historical Financial Information As of December 31, 2007*; Verizon *Investor Quarterly 4Q 2007*.

<sup>60</sup> / AT&T Investor Briefing 4Q 2007, at 14.

<sup>61</sup> / Qwest Communications International, Inc., "Historical Financial Information As of December 31, 2007."

<sup>62</sup> / Verizon Communications, Inc. Investor Quarterly 4Q 2007, at page 8.

The major broadband providers continue to earn large returns on their broadband investments, and the ILECs continue to earn large returns on interstate special access,<sup>63</sup> a necessary input for competitors to offer broadband service.

In the “old-fashioned” framework of rate of return regulation (“RORR”), the low-cost/high-revenue broadband deployment would subsidize the high-cost/low-revenue broadband deployment, thereby achieving universal broadband service. However, regulators lack the RORR tools they once possessed to ensure universal service. Instead, a serious fall-out of the Commission’s decision to consider DSL as an information service is that ILECs can pick and choose where they deploy broadband. Second, because the DSL revenues are considered unregulated, shareholders, not consumers benefit from the substantial revenue flow resulting from ILECs’ DSL deployment. Therefore, Rate Counsel urges the Commission to identify and to implement ways to assess USF charges on ILECs’ DSL services to correct the unfair situation that now prevails within today’s regulatory framework.<sup>64</sup>

Broadband providers likely have already picked the low-hanging fruit; that is, they have already deployed broadband to those areas where they can expect to make a profit.<sup>65</sup> Because we may have reached the limit of what the competitive market will

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<sup>63</sup> / See In the Matter of Special Access Rates for Price Cap Local Exchange Carriers, WC Docket No. 05-25, AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Service, RM-10593, Comments of the New Jersey Division of rate Counsel, August 8, 2007, at Table 1 (showing RBOCs’ increasing rates of return on Special Access) and Table 2 (showing Verizon NJ’s increasing rates of return on Special Access).

<sup>64</sup> / The rationale for assessing ILECs (and not cable companies for their broadband access) is that ILECs are using the common loop to provide DSL.

<sup>65</sup> / DSL availability in Maine, New Hampshire, and Vermont typifies the way in which rural areas are often left behind in broadband deployment. As of June 2007, only 68%, 61%, and 66% of Maine, New Hampshire, and Vermont residents, respectively, had access to DSL service where the ILEC offered voice service. This contrasts to the nationwide average of 82%, and statewide averages of 91% in Georgia, 90% in Nevada, and 89% in Florida and California. (FCC, High-Speed Services for Internet Access: Status as of June 30, 2007, Released March 2008, at Table 14.)

provide on its own, Rate Counsel supports a Broadband Fund, provided that it is carefully structured, has a clear sunset date, and is distributed proportionally to all states and jurisdictions (based on population or households).

Rate Counsel previously proposed putting assistance into the hands of consumers, rather than service providers:

[T]he Commission should focus not only on the *supply* of advanced services but also the *demand* for advanced services. A logical first step would be to expand the Lifeline and Linkup programs to encompass a steep discount for broadband access, which a consumer could use for any supplier. Any attempts by the Commission to narrow the digital divide should address not only high cost areas, but also low-income communities.<sup>66</sup>

Rate Counsel also stated that it

opposes the expansion of the non-rural high cost mechanism as a way to achieve broadband ubiquity; instead, the Lifeline program should be expanded to encompass broadband services. By using the Lifeline program, the Commission could ensure that subsidies flow to consumers rather than to carriers, thereby linking USF support to rates, as *Qwest II* requires.<sup>67</sup>

While maintaining the thrust of its previous position, especially the need to restrain growth of the Broadband Fund, Rate Counsel acknowledges that *demand*-side assistance (e.g., providing consumers with vouchers) cannot be relied upon to encourage greater *supply*. To this end, Rate Counsel encourages the Commission to move forward with enabling financial incentives for build-out to unserved and underserved areas. Rate Counsel also previously stated,

If there are areas of the country that are either underserved or entirely neglected, the boundaries of those areas should be defined clearly, with state-of-the-art mapping technology. If the reason for the lack of advanced services is that the anticipated revenues from

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<sup>66</sup> / Rate Counsel 2006 USF Initial Comments, at 22-23.

<sup>67</sup> / *Id.*, at 23.

the advanced services would not cover the anticipated cost of deployment, the areas should be opened to high-cost bidding by competitors to serve the area. Competitors should then be required to commit to specified minimum service quality requirements, maximum pricing constraints, and minimum years of commitment to service. The competitor requiring the least amount of high cost support should be awarded the unique opportunity to serve the area for a specified period of time, until it can be demonstrated that the geographic area can support multiple suppliers. Alternatively, consumers should be awarded high cost/advanced services funds directly to be used as an offset against a broadband bill.<sup>68</sup>

In order to restrain growth of the high cost components of the USF, Rate Counsel recommends that the Broadband Fund provide support to only one broadband service provider in a given area. Areas that require broadband support (that is, areas with market failure, i.e., in which a “plausible economic case” cannot be made) likely will have only a single service provider. Therefore, continuing oversight of the quality of the broadband service provided by the carrier that receives USF support is essential so that, in those areas that lack competition, a digital divide is not created. Furthermore, audits and enforcement mechanisms may be necessary to ensure that suppliers receiving Broadband Fund support are accountable for their use of funds.

**The recommended level of initial funding is inadequate.**

The Joint Board recommends an initial funding level of \$300 million per year for the Broadband Fund.<sup>69</sup> While some of the funding will come from federal sources, the Joint Board recommends that some portion of the \$300 million come from funds reassigned from legacy POLR programs.<sup>70</sup> Also, the Joint Board recommends that

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<sup>68</sup> / *Id.*, at 23-24.

<sup>69</sup> / Recommended Decision, at para. 29.

<sup>70</sup> / *Id.*, at para. 29.

federal funds could be “stretched” by encouraging states to provide matching funds,<sup>71</sup> with all states provided a base level of support regardless of participation, and a higher, supplemental level for states providing at least a minimum, “perhaps 20%,” matching fund.<sup>72</sup> Rate Counsel agrees that states should be encouraged to participate financially in achieving the goal of universal broadband service. However, even with matching funds from the states, the level of funding recommended by the Joint Board is inadequate to the task at hand. Rate Counsel agrees with Commissioner Copps’ view that the recommended level of funding is “like fighting a bear with a fly-swatter.”<sup>73</sup>

Broadband deployment that has been achieved thus far, without subsidies or mandates (and therefore, presumably in locations where a “plausible economic case” *could* be made), has been expensive. In comments recently submitted in another proceeding, Comcast stated that “Comcast and other cable operators raised and invested more than \$110 billion” deploying broadband in the U.S.<sup>74</sup> This massive expenditure extended broadband capabilities to locations that, presumably are the *easiest* to reach and the most *profitable*. Reaching out to remaining areas, the “fringe,” will be more expensive on a per-connection basis.

Two recent examples in New England serve to highlight the potential cost of deploying broadband to unserved and underserved areas. Massachusetts Governor Deval Patrick recently announced an effort to deploy broadband to the one-third of Massachusetts that currently lacks service. His plan involves spending \$25 million to

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<sup>71</sup> / *Id.*, at para. 29.

<sup>72</sup> / *Id.*, at para. 50.

<sup>73</sup> / *Id.*, Statement of Commissioner Michael J. Copps Approving in Part, Concurring in Part.

<sup>74</sup> / In the Matter of Broadband Industry Practices, WC Docket No. 07-52, Comments of Comcast Corporation, February 12, 2008, at 7.

encourage service providers to reach the 32 Massachusetts communities that are currently unserved by broadband providers.<sup>75</sup> More recently, Verizon, the ILEC serving Massachusetts, announced plans to extend FiOS to 30 communities that already have broadband capabilities, and to extend DSL service to 23 other communities that are currently without *any* broadband service. Even with this push to extend the reach of broadband, “Verizon expects High Speed Internet service will be available to *an average of 70 percent* of its customer lines in the 23 towns” and expects that the “new broadband deployment of Verizon’s High Speed Internet network will reach *two-thirds* of the western Massachusetts communities identified by the state as having no high-speed broadband services.”<sup>76</sup> This expansion of Verizon’s service, which is estimated to cost \$200 million,<sup>77</sup> will still leave many residents in Massachusetts without broadband service.

FairPoint Communication’s recent acquisition of Verizon’s access lines in Maine, New Hampshire, and Vermont also provides information about the cost of expanding deployment of broadband facilities. As one of many conditions for approval from regulators in New Hampshire, FairPoint agreed to spend \$16.4 million to extend broadband to 57,700 access lines that currently have no broadband service provider.<sup>78</sup>

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<sup>75</sup> / Press release, “Governor Patrick Files \$25 Million Broadband Bond Bill,” October 18, 2007. Another 63 communities are only partially served.

<sup>76</sup> / Press release, “Consumers, Businesses in Western Massachusetts to Benefit From Verizon Broadband Expansion Project,” February 28, 2008 (emphasis added).

<sup>77</sup> / Press release, “Verizon to Invest \$200 Million to Expand Broadband in Massachusetts in 2008,” February 28, 2008.

<sup>78</sup> / New Hampshire Public Utilities Commission Docket No. DT 07-011, *Verizon New England, Inc., Bell Atlantic Communications, Inc., Nynex Long Distance Co., Verizon Select Services, Inc. And Fairpoint Communications, Inc. - Petition for Authority to Transfer Assets and Franchise*, FairPoint Exh. 59P, p. 1.

Even this effort still leaves some residents of New Hampshire without options for broadband service.<sup>79</sup>

Clearly, if extending broadband deployment in relatively small states like Massachusetts and New Hampshire is this expensive, then surely \$300 million is far from adequate to extend deployment for the entire country. Of course, more precise estimates of the costs involved will only be possible when comprehensive mapping shows more precisely the locations of the unserved and underserved regions of the country. The Joint Board's recommended initial funding likely is woefully inadequate to achieve the goal of ubiquitous deployment.

### **Other Issues**

The Joint Board recommends that “the Commission request comment as to the appropriate transition plan to wean a provider from Mobility or Broadband support once the objectives of geographic coverage in an area have been met.”<sup>80</sup> Rate Counsel agrees that support should end when the goals of deployment in a given area have been met. The major barrier to providing service in these areas is the large initial sunkcost. Ongoing operational costs should be minor in comparison. Rate Counsel therefore supports aid for the build-out of facilities, but opposes a permanent stream of subsidies to service providers. In this respect, Rate Counsel agrees with Joint Board member Edgar when she states:

As a Joint Board member from a net contributor state, I have concerns that expanding the scope of the fund to include broadband and mobility could inadvertently increase the overall fund size. While I recognize the importance of broadband Internet access and the importance of deploying it to unserved areas, I am

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<sup>79</sup> / *Id.*, at 22.

<sup>80</sup> / Recommended Decision, at para. 38.

wary of what lies beyond that initial objective and what financial impacts such deployment may have on consumers. I view these funding mechanisms as intended to facilitate service to unserved areas and not as long-term entitlements.<sup>81</sup>

The Joint Board recommends a transition of five years, consisting of the gradual reduction of identical support funding to provide the source for Broadband and Mobility Funds.<sup>82</sup> While recognizing that the Commission should not disrupt business plans with erratic policy changes, Rate Counsel recommends a more aggressive timetable, perhaps three years, in order to close the digital divide and to raise the nation's global competitiveness.

Rate Counsel agrees with the Joint Board's recommendation to eliminate the requirement that each CETC must provide all services covered by the USF (broadband, wireless, and wireline services) in order to receive funding.<sup>83</sup>

The Joint Board states that:

The Commission has already sought comment on the current definition of broadband. We note that the current Commission definition of "high speed" data transmission, 200 kilobits per second, has been in place for years. While that standard was once useful, we now believe that a more rigorous requirement may be justified, closer to the capacities more typical of the most common national broadband plans. If so, an objective method would be needed to determine such upload and download capacities, and a regular review would be necessary.<sup>84</sup>

Rate Counsel agrees with this assessment, which it has articulated in other comments filed with the Commission.<sup>85</sup> Rate Counsel reiterates its support for an updated definition

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<sup>81</sup> / *Id.*, Statement of Chairman Lisa Polak Edgar.

<sup>82</sup> / *Id.*, at para. 27.

<sup>83</sup> / *Id.*, at para. 68.

<sup>84</sup> / *Id.*, at para. 72.

<sup>85</sup> / In the Matter of Development of Nationwide Broadband Data to Evaluate Reasonable and Timely Deployment of Advanced Services to All Americans, Improvement of Wireless Broadband Subscribership

of broadband (e.g., a minimum of 1 Mbps downstream), as well as periodic revisions to the definition to correspond with evolving technology and consumer demand.

### C. MOBILITY

The Joint Board recommends that the Mobility Fund subsidize the construction of new facilities in unserved areas meaning “areas with a significant population density but without wireless voice service.”<sup>86</sup> Rate Counsel supports universal service support for mobility, provided any such fund is defined carefully, that mobility support be limited to a single carrier, and that any mobility funds be used first to serve any regions of the country that may lack any telephone service.

Rate Counsel acknowledges the potential benefit of subsidizing the deployment of wireless service for areas that are frequented by the traveling public (such as federal and state highways), regardless of the population in the immediate areas, if it is clear that, absent such support, suppliers would not otherwise enter the market.<sup>87</sup> Access to wireless service enhances the public safety for all consumers, and, as pay phones disappear, wireless deployment has become increasingly important to consumers’ welfare and safety.<sup>88</sup>

A majority of customers subscribe to wireless service. Demand for wireless service now exceeds 230 million, and demand for wireline service approximates 163

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Data, and Development of Data on Interconnected Voice over Internet Protocol (VoIP) Subscribership, WC Docket No. 07-38, Reply Comments of the New Jersey Division of Rate Counsel, July 16, 2007, at 3.

<sup>86</sup> / *Id.*, at para. 16.

<sup>87</sup> / *Id.*

<sup>88</sup> / According to the FCC’s Trends in Telephone Service, payphone deployment peaked in 1999 at 2.1 million payphones in the U.S. Since then, payphone deployment has declined steadily. The most recent data (from 2005) indicates that the U.S. now has only 1 million payphones. (Trends in Telephone Service, February 2007, at Table 7.6). See, also “Busy signals: Pay phones may appear to be gathering dust, but hold on just a minute,” Irene Sege, *Boston Globe*, March 10, 2008.

million.<sup>89</sup> One could easily misconstrue these demand patterns as suggesting that wireless is replacing wireline. Instead, the vast majority of households continue to rely on wireline service despite this explosive growth in demand for wireless service, suggesting that most consumers consider wireless service to supplement wireline service rather than to replace it.

The wireless market continues to evolve. Expectations about wireless service have and continue to change, with handsets becoming smaller, wireless coverage greater, and expectations of service quality rising. The market is still dynamic, which complicates regulatory intervention. Wireless providers continue to deploy facilities to provide wireless services.<sup>90</sup> The number of cell sites has grown from 96,000 in 2000 to 210,000 in 2007, according to CTIA, the telecommunications industry's trade group.<sup>91</sup>

Rate Counsel is concerned that in a market undergoing such substantial change, a new Mobility Fund could result in subsidizing deployment that might have occurred *without* the subsidy, and that, indeed, the expectation of a subsidy could deter private investment that might have otherwise occurred. For these reasons, Rate Counsel recommends that if the Commission decides to use USF monies to subsidize wireless deployment, the Commission do so on a trial basis and seek to avoid creating a societally inefficient economic incentive – such as causing carriers' postponement of wireless facilities deployment in anticipation of possible USF support.

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<sup>89</sup> / Recommended Decision, at para. 65. See FCC, Local Telephone Competition: Status as of June 30, 2007, March 2008, at Tables 7 and 14.

<sup>90</sup> / See, e.g., "City settles on cell tower off Interstate 95," Stephen Tait, *The Daily News*, March 15, 2008, [http://www.newburyportnews.com/punews/local\\_story\\_075070559.html](http://www.newburyportnews.com/punews/local_story_075070559.html).

<sup>91</sup> / Smaller Towns Gaining The Attention Of Wireless Carriers Monday, February 11, 2008, <http://deadcellzones.blogspot.com/>

The critical and challenging issue for the Commission, working in collaboration with states, is to identify those areas that, absent universal service support, would remain unserved or underserved. In other words, regulatory intervention should occur only where market forces will not lead to the desired societal outcome of reliable wireless service throughout the country. An area that is served adequately today was once, of course, an unserved or underserved area. The challenge for the Commission and the states is to identify those locations that warrant wireless coverage, but that are unlikely to attract private capital, and that, therefore, require USF support. It would be inefficient and burdensome to consumers if the Commission were to subsidize wireless deployment in areas that suppliers would have served anyway, that is, areas that are in the planning phases of potential suppliers.

Defining reasonable parameters for assessing whether a “plausible economic case” can be made is essential. The Joint Board also states that a “secondary purpose of the Mobility Fund would be to provide continuing operating subsidies to carriers serving areas where service is essential but where usage is so slight that a plausible economic case cannot be made to support construction and ongoing operations, even with a substantial construction subsidy.”<sup>92</sup> “[A]ccess to at least one carrier that provides a reliable signal,”<sup>93</sup> is a desirable outcome, but Rate Counsel recommends that the Commission define more explicitly how one would assess whether a “plausible economic case” can be made. Multiple factors influence such an analysis (e.g., the use of the discount rate over which the business case is applied, the time horizon of the financial analysis, assumptions about demand and price, the use of a net-present-value analysis or

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<sup>92</sup> / Recommended Decision, at para. 16.

<sup>93</sup> / *Id.*

an internal rate of return analysis, etc.). The wireless industry should be encouraged to submit specific recommended parameters that the Commission and states could use to assess the economic plausibility of serving areas.

Rate Counsel also concurs with the Joint Board that states should partner with the Commission in administering Mobility Fund awards.<sup>94</sup> Rate Counsel further concurs that states should award Mobility Fund grants to only one provider in a geographic area,<sup>95</sup> Indeed, at such time as more than one provider serves an underserved or unserved area, the ongoing need for Mobility Fund support should be seriously questioned.

Rate Counsel also supports the Joint Board recommendation that states “be required to provide a detailed map of areas not served by by wireless voice service.”<sup>96</sup> Rate Counsel supports the preparation of detailed maps by states, but urges the Commission to direct carriers to provide the relevant information to states, so that such maps can be created. Carriers that fail to submit necessary information to states should be disqualified from receiving Mobility Fund support.

The Joint Board does not recommend a specific algorithm for allocating state grants, but does raise the possibility that states might be required to provide matching funds.<sup>97</sup> Rate Counsel recommends that any state grants be awarded based simply on population, with monies flowing in proportion to residents. If states, because of the unique physical characteristics of their states (topography, population density, etc.),

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<sup>94</sup> / *Id.*, at para. 17.

<sup>95</sup> / *Id.*, at para. 18.

<sup>96</sup> / *Id.*

<sup>97</sup> / *Id.*, at paras. 17-18.

require support in addition to the federal grants, Rate Counsel recommends that the Commission encourages states to provide such supplemental funds.

Rate Counsel acknowledges that rural areas may be more likely to lack adequate wireless coverage than do urban areas, but reminds the Commission that consumers ultimately bear the cost of universal service support. Therefore, the Commission should balance carefully any additional costs that consumers ultimately must bear. Federal grants can certainly help to mitigate the cost of deploying wireless in remote regions of the country, but should not be the exclusive source of funding. Instead, individual states also should be prepared to contribute to the cost of ensuring that their consumers have access to reliable wireless access. In some states, the magnitude of such supplemental funding might “match” the federal funds and in other jurisdictions the state funds might be lower than or exceed the federal funds.

Multiple factors affect the cost of living in different regions of the country, with the prices for essential items varying significantly. For example, while consumers in rural areas may confront relatively higher costs related to wireless deployment, consumers in urban areas may confront higher housing costs. Accordingly, the goal of the Mobility Fund should not be to shift substantial new costs onto urban consumers (who face other high costs) but rather to encourage and to support in part the deployment of wireless throughout the country and equally important, to encourage states’ own financial participation in achieving that goal.

Rate Counsel commends the Joint Board on its forward-thinking approach to telecommunications services and on its recognition of the increasingly important role that wireless service has in today’s society. However, Rate Counsel is also concerned that the

Mobility Fund, though appealing in overall concept and direction, lacks critical information about specific aspects of its operation, such as key definitional issues (e.g., “significant population density” and “plausible economic case”). For these reasons, Rate Counsel urges the Commission to target any Mobility Fund first to areas that entirely lack telephone service (whether wireline or wireless) and secondarily to use limited funds on a trial basis to improve wireless access in underserved or unserved areas. Without adequate constraints and clear implementation objectives, a Mobility Fund could simply lead to unlimited burdens on consumers throughout the country.

#### **D. PROVIDER OF LAST RESORT**

The Joint Board recommends that the POLR Fund consist of all existing ILEC support mechanisms, with some possible funding reductions.<sup>98</sup> Among other things, the Joint Board states the following:

- Support mechanisms presently differ for rural and non-rural carriers, with support for consumers varying depending on which carrier serves them, which, in turn, “can exacerbate the differences in treatment between comparable situated customers.”<sup>99</sup>
- Support mechanisms do not recognize all costs, and, for example, although support is substantial for loop costs, it is less so for most switching costs, and “nonexistent for transport costs.”<sup>100</sup>
- The high-cost support mechanisms “need to be modernized in several ways.”<sup>101</sup>

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<sup>98</sup> / *Id.*, at para. 19.

<sup>99</sup> / *Id.*, at para. 20. See also footnote 22 in which the Joint Board observes that “[i]ndeed, the Commission has repeatedly failed to demonstrate to the courts that funding for the customers of non-rural carriers is sufficient,” citing to *Qwest Corp. v. FCC*, 258 F.3d 1191 (10<sup>th</sup> Cir. 2001) (“Qwest I”); *Qwest Corp. v. FCC*, 398 F.3d 1222 (10<sup>th</sup> Cir. 2005) (“Qwest II”).

<sup>100</sup> / *Id.*, at para. 21.

<sup>101</sup> / *Id.*, at para. 22.

Rate Counsel concurs with the Joint Board that none of “the mechanisms in place reflect the increased importance of non-regulated revenues generated by telecommunications plant.”<sup>102</sup> The way in which ILECs assign and allocate common plant and expenses harms consumers because they bear the full cost of plant and yet ILECs use the common platform to provide lucrative unregulated services, the revenues from which flow to shareholders. Rate Counsel opposes providing high-cost support to ILECs unless their unregulated services are assessed for USF contributions.

Section 254(b)(1) requires as the first principle of Universal Service that services be “available at just, reasonable, and affordable rates.”<sup>103</sup> Under the current system of high cost support, Universal Service remains an incomplete goal. New Jersey, for example contributes to the fund, yet ranks fifty-second out of 56 states and territories receiving high cost universal service support.<sup>104</sup> In any event, neither the rural nor the non-rural high cost fund should become an entitlement program for incumbent local exchange carriers.

**Carriers have failed to demonstrate that consumers are benefiting from the carriers’ high cost support windfall.**

High-cost program payments have grown from approximately \$1.2 billion in 1996 to an estimated \$4.3 billion in 2007. The more than tripling of the high cost fund (costs which consumers ultimately bear) during a period of declining costs in the

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<sup>102</sup> / *Id.*

<sup>103</sup> / 47 U.S.C. §254(b)(1).

<sup>104</sup> / Universal Service Monitoring Report CC Docket No. 98-202, CC Docket No. 96-45, at 3-18 and 3-26 (2006). See Table 3 above (2007 Monitoring Report, Table 3.14).

telecommunications industry is troubling. Rate Counsel supports the Commission's comprehensive reform of this fund to prevent further unwarranted increases in the fund.

New Jersey carriers, which serve approximately four percent of the nation's switched access lines, received a negligible \$1.3 million of the total \$4.3 billion in high-cost support disbursements in 2007 (that is, only three-hundredths of one percent). The Universal Service Fund contribution factor for the second quarter of 2008 is 11.3%;<sup>105</sup> carriers contribute based on "projected, collected, end-user interstate and international telecommunications revenues."<sup>106</sup> The theory that carriers cannot lower urban rates to meet competition without eroding implicit support for rural areas, although superficially appealing, has not been proven. Indeed, the competition that the Act envisioned has not materialized, and now, ILECs are benefiting from a high cost windfall, which was created to replace implicit support purportedly eroded by competition. If such competition truly threatened ILECs, one would expect ILECs to voluntarily *lower* rates in urban areas to meet the competition. Rate Counsel is not aware of ILECs lowering local exchange rates as a result of receiving high cost support. Since 2000, ILECs' non-rural high cost funds have increased from \$218,672,103 to \$347,084,981, an approximate 59 percent increase, without any clear commensurate benefit to the consumer.<sup>107</sup>

Figure 5 shows the growth in non-rural high cost funds disbursed to ILECs since 2000. In the face of purported local competition, mergers, and the deployment of more efficient technology, one would expect ILEC costs to decline, and, in turn, cause a

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<sup>105</sup> / See <http://www.fcc.gov/omd/contribution-factor.html>.

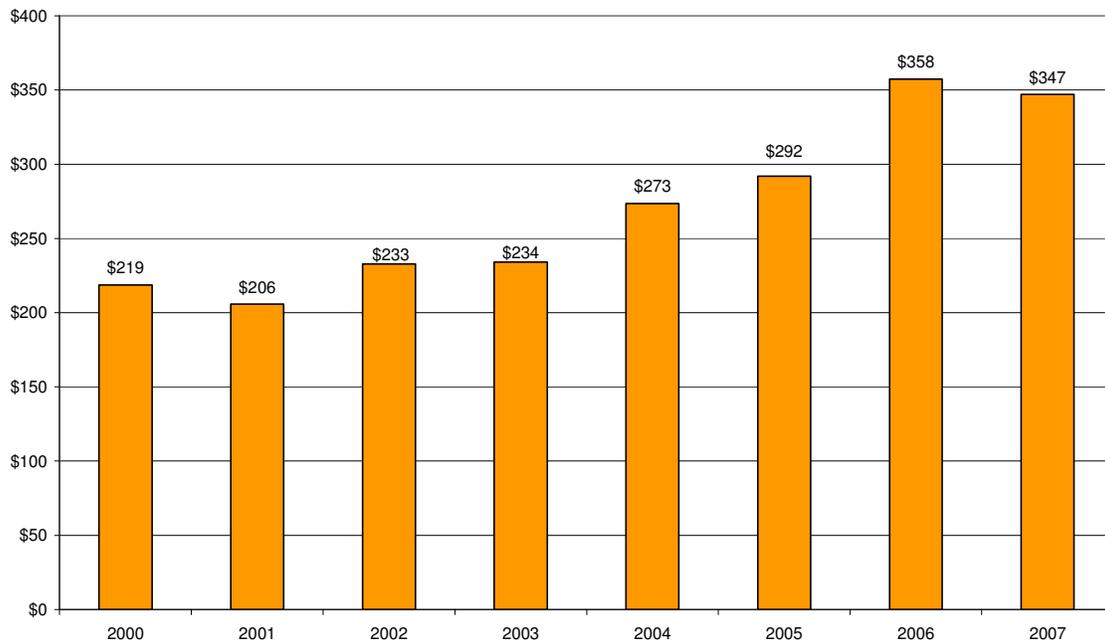
<sup>106</sup> / Prior to the second quarter of 2003, carriers contributed based on historical gross-billed revenues.

<sup>107</sup> / 2007 Monitoring Report, Table 3.9.

decline in the need for high cost funds. The increasing trend in non-rural high cost funds, therefore, is troubling for the consumers who shoulder the burden of the high cost fund.

**Figure 5<sup>108</sup>**

**Total Non-Rural High Cost Support Payments  
(millions of dollars)**



Rate Counsel reiterates the recommendation it has made in previous pleadings that the Commission ensure that any high cost fund mechanism, whether for rural carriers or for non-rural carriers, not become an ILEC entitlement.<sup>109</sup> Rate Counsel has previously advocated and continues to support the sunset of the non-rural high cost fund. Rate Counsel urges the Commission to ensure that the high cost fund does not become an unwarranted revenue windfall for ILECs. The cost of providing basic local exchange service should be considered within the context of many significant factors that offset the

<sup>108</sup> / 2007 Monitoring Report, Table 3.9

<sup>109</sup> / Rate Counsel 2006 USF Initial Comments, at 4-5.

relatively higher costs of serving rural areas within non-rural carriers' territories, most of which Congress likely did not anticipate when it established its universal service mandates ten years ago. These factors include: the substantial stream of revenues that ILECs generate as a direct result of customers' near-monopoly reliance on ILECs for a basic link to the public switched network (e.g. revenues from switched access, toll, vertical features, bundled offerings, etc.); billions of dollars of synergies resulting from multiple mergers in the telecommunications industry; ILECs' supra-competitive earnings from special access services; and the virtual absence of competition. Together these factors provide compelling evidence that the erosion of non-rural ILECs' implicit support has not occurred, and, therefore, the original rationale for explicit non-rural high cost support does not apply to today's telecommunications market. Accordingly, Rate Counsel urges the Commission to establish a near-term sunset date for the non-rural high cost fund<sup>110</sup> and also urges the Commission to consider establishing a sunset date for the rural high cost fund.

Without a provision for sunseting the high cost fund, the Commission implicitly endorses a program whereby, with non-existent accountability, ILECs receive an open-ended subsidy. Moreover, despite changes in technology and the industry, and despite purported competition, the subsidy is *increasing*. The non-rural high cost fund, which was \$218,672,103 in 2000, grew by 59% to \$347,084,981, in 2007. Mississippi, which receives over half of the non-rural high cost funds, experienced a 92 percent growth in its

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<sup>110</sup> / See In the Matter of High-Cost Universal Service Support, WC Docket No. 05-337; Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Reply Comments of the New Jersey Division of Rate Counsel, May 26, 2006, at 3.

non-rural high cost support during this same time period.<sup>111</sup> Transforming implicit universal service support into explicit high cost support does not justify a more than \$4 billion revenue annual windfall for local exchange carriers.

**The Commission’s resolution of outstanding *Qwest II* matters will affect high cost reform.**

As the Joint Board observes, the Commission has not acted on the remand that it received in 2005.<sup>112</sup> Rate Counsel has previously addressed the determination of comparable urban and rural rates. This unresolved issue bears directly on the issues under investigation in this proceeding. Rate Counsel opposes the use of a rate-based support mechanism. There is no evidence that state rates for local service correspond with the associated costs of providing local service. Using rates as a way to assess the need for high cost funds would be administratively impractical, economically inefficient, and create perverse incentives for states to raise rates.<sup>113</sup>

**The Commission should reject any proposals that would distribute high cost support at the wire center level.**

The Joint Board raises the possibility of determining non-rural support on a wire center or sub-wire center basis, rather than the present statewide average cost basis.<sup>114</sup> As the Joint Board recognizes, such a reform “would neglect the economies of scale and scope inherent in non-rural LEC networks.”<sup>115</sup> Furthermore, as the Joint Board also

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<sup>111</sup> / 2007 Monitoring Report, Table 3.9. See also In the Matter of High-Cost Universal Service Support, WC Docket No. 05-337; Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Reply Comments of the New Jersey Division of Rate Counsel, May 26, 2006, at 34-35, citing Federal-State Joint Board Monitoring Reports.

<sup>112</sup> / Recommended Decision, at para. 33.

<sup>113</sup> / Rate Counsel USF 2006 Initial Comments, at 36.

<sup>114</sup> / Recommended Decision, at para. 41.

<sup>115</sup> / *Id.*

states, “the Tenth Circuit upheld the existing statewide averaging mechanism as a reasonable method of support allocation consistent with the Act.”<sup>116</sup>

It is not surprising that ILECs would seek the more granular basis for assessing high-cost support eligibility because such an approach would increase significantly high-cost support. However, Rate Counsel continues to oppose the wire center approach about which the Commission seeks comment, and which AT&T advocated in an earlier phase of this proceeding.<sup>117</sup> AT&T asserted in this earlier phase:

The entire point of the reasonable comparability inquiry is to examine what consumers in rural and high-cost areas actually spend on telephone service and receive for the money relative to what consumers in urban areas actually spend and receive. Combining these very different consumers into a hypothetical ‘statewide average’ consumer is meaningless and guts the very purpose of section 254(b)(3). The analysis should take place on a much more granular basis, such as a wire center.<sup>118</sup>

AT&T suggests that there is readily available data for determining the amount support for individual wire centers or census block groups.<sup>119</sup> Determining carriers’ needs based at the wire center level is excessively granular. Furthermore, a mechanism that is based at the wire center level would overstate ILECs’ costs because it would fail to reflect the significant economies of scale and scope that ILECs have throughout their serving area.

By way of example, assume that an ILEC’s serving territory consists of 6 wire centers, and the costs of serving customers in Wire Centers A through F are \$10, \$20, \$25, \$35, \$40, and \$50. Assume further, for sake of illustration, that the benchmark (that is the value which triggers HCF support) is \$30. The average cost to the ILEC of serving

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<sup>116</sup> / *Id.*, citing *Qwest I*.

<sup>117</sup> / Rate Counsel 2006 USF Reply Comments, , at 18-19.

<sup>118</sup> / AT&T, WC Docket 96-45, March 27, 2006, at 17-18.

<sup>119</sup> / *Id.*, at 18.

customers is \$30 in this simplified example (of course, in reality, the weighted average cost would likely be far less since there would be significantly more lines in the low-cost urban areas). Based on an assessment of the area-wide cost of serving the ILEC's territory, the ILEC would not receive any HCF, which would be a fair and economically efficient result. The pretense of improved accuracy by further disaggregating the geographic area over which high cost need is assessed is misleading. The result is a heads-I-win tails-you-lose situation because for every wire center that is above cost there is another wire center that is below cost yet with the lopsided approach advocated by AT&T, ILECs would withdraw funds from USF for high cost but not put in for low cost. The impact of introducing granularity into the assessment of high-cost eligibility on the size of the high cost fund would be substantial, and is not necessary to achieve universal service goals.

**The POLR Fund should support only one carrier in any given geographic area.**

The POLR fund, as the Joint Board recommends, should support only a single carrier in any geographic area. Alternatively, if multiple carriers consider it profitable to serve an entire area *without support*, then high cost support should not be provided. By adopting the Joint Board's recommendation, the Commission would not then need to modify its ETC rules, other than to cap the ETC funds, and begin the transition to the Mobility Fund.

**A Federal-state partnership would facilitate the achievement of universal service.**

Rate Counsel concurs with the Joint Board that the Commission should strengthen the state-federal partnership for furthering universal service.<sup>120</sup> States are likely to have the most detailed information about areas that require support from the Broadband and Mobility Funds. Rate Counsel urges the Commission, however, in order to eliminate any residual ambiguity, to delegate explicitly to states the authority that Rate Counsel believes states already possess to obtain data, with appropriate confidential treatment, from carriers about the geographic areas that (1) they presently service; (2) they intend to serve; and (3) they are unlikely to serve so that states can target better any universal service support. Absent such information, consumers are exposed to the risk of funding construction and deployment that would have occurred without universal service support.

Rate Counsel concurs with the Joint Board that states should be permitted to employ a competitive bidding process or cost-based mechanism for funding infrastructure projects.<sup>121</sup> Rate Counsel also concurs with the Joint Board that states' awarding of funds should comply with Commission-established rules and guidelines on such matters as defining the quality of the broadband and mobility services to be funded (including broadband transmission speeds).<sup>122</sup>

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<sup>120</sup> / Recommended Decision, at para. 44.

<sup>121</sup> / *Id.*, at para. 47.

<sup>122</sup> / *Id.*

## **E. OTHER HIGH COST REFORM ISSUES**

### **The Broadband and Mobility Funds should be subject to audit.**

The Joint Board states that it “believes [that] it remains in the public interest for the Universal Service Administrative Company (USAC) to continue to distribute universal service funds and conduct periodic audits.”<sup>123</sup> Rate Counsel fully supports periodic audits of universal service funds. If the Commission establishes the Broadband and Mobility Funds (which likely would entail the collection and disbursement of large sums of monies, which consumers ultimately would pay), these funds would be distributed to carriers throughout the country under new programs. Therefore, it is particularly important that all participants in the new funds (carriers, states, the Commission, and USAC) are informed at the outset that the programs will be subject to periodic audit.

Rate Counsel has previously stated that New Jersey consumers have an interest in ensuring they do not ultimately pay for the costs of inefficiencies and fraud associated with the USF programs.<sup>124</sup> Rate Counsel urges the Commission to take the requisite steps to prevent the types of concerns that have been raised with the schools and libraries program. Among other things, Rate Counsel stated:

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<sup>123</sup> / Recommended Decision, at para. 49.

<sup>124</sup> / *In the Matter of Comprehensive Review of Universal Service Fund Management, Administration, and Oversight*, WC Docket No. 05-195; *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45; *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6; *Rural Health Care Support Mechanism*, WC Docket No. 02-60; *Lifeline and Link-Up*, WC Docket No. 03-109; *Changes to the Board of Directors for the National Exchange Carrier Association, Inc.*, CC Docket No. 97-21, *Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking*, rel. June 14, 2005 (“NPRM”), Reply Comments of the New Jersey Division of the Ratepayer Advocate, December 16, 2005, at 2; *see also* Initial Comments of the New Jersey Division of the Ratepayer Advocate, October 18, 2005. Rate Counsel incorporates by reference its initial and reply comments from this proceeding, and, furthermore, recommends that the Commission assess the comments submitted in that proceeding as it establishes mechanisms and auditing procedures for the new Mobility and Broadband Funds.

As stated in [Rate Counsel’s] initial comments, the promised one-year review of USAC’s performance has not been undertaken and the Commission should engage a third-party auditor to examine USAC’s operations. As outlined above, it does not appear that the USF is being administered in “an efficient, effective, and competitively neutral manner.” A recent report approved by the Committee on Energy and Commerce of the U.S. House of Representatives concluded that “While E-rate has arguably benefited the nation’s children, the program falls far short as an example of efficiency, effectiveness, or integrity.”<sup>125</sup>

Rate Counsel supports the Commission’s adoption of a comprehensive mechanism for monitoring and auditing the collection and disbursement of USF fees.

**The Mobility and Broadband Funds should sunset.**

The Joint Board raises an important issue that Rate Counsel urges the Commission to address at the outset. Although the Joint Board indicates that it anticipates that the Mobility and the Broadband support will be available only for a limited period of time, and raises the possible need for an “appropriate transition plan to wean a provider from Mobility or Broadband support once the objectives of geographic coverage in an area have been met,”<sup>126</sup> the Joint Board does not offer any specific sunset date. Rate Counsel urges the Commission to establish clear sunset dates to avoid creating any expectation that the funding will be of indefinite duration, possibly with a provision that the date can be extended by the Commission only if certain specific circumstances are met.

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<sup>125</sup> / *Id.*, at 17, quoting Subcommittee on Oversight & Investigations Bipartisan Staff Report for the Use of the Committee on Energy and Commerce, U.S. House of Representatives, “Waste, Fraud, and Abuse Concerns with the E-Rate Program,” October 18, 2005, other cites omitted.

<sup>126</sup> / Recommended Decision, at para. 38.

### **Implementation, Transition and Review.**

Universal service support sounds “pro-consumer,” but if not structured properly, will burden consumers and jeopardize the affordability of telecommunications services. Consumers ultimately pay for increasing USF fees. Therefore, Rate Counsel concurs with the Joint Board that “[a]ny possible benefit anticipated from increased universal service fund (USF) distributions must be weighed against the added burden on consumers of telecommunications services” and that “[l]arger USF contributions increase the risk that telecommunications services will become unaffordable for some, or even a substantial number of consumers.”<sup>127</sup> Furthermore, as the Joint Board recognizes, “excessive subsidization arguably may affect the affordability of telecommunications services, thus violating one of the principles in Section 254.”<sup>128</sup>

Rate Counsel urges the Commission to adopt the Joint Board’s recommendation for an overall cap on high-cost funding.<sup>129</sup> ILECs’ ability to achieve a fair rate of return on their investment in the public switched network is not at risk.<sup>130</sup> Carriers have merged, yielding billions of dollars of synergies. ILECs are enjoying excessive rates of return on special access (for which, with the acquisitions of AT&T and MCI, any prospect of meaningful special access competition has evaporated, further entrenching

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<sup>127</sup> / *Id.*, at para. 24.

<sup>128</sup> / *Id.*, at para. 24, citing *Qwest I*, at 1200 and *Qwest II*, at 1234.

<sup>129</sup> / *Id.*, at para. 26.

<sup>130</sup> / ILECs’ investment in video and entertainment entails risk. The risks of these unregulated services are appropriately borne by shareholders.

ILECs' ability to earn supra-competitive profits on their special access services).<sup>131</sup> Also, in the dozen years since the enactment of the 1996 Act, RBOCs have obtained the requisite Section 271 authority to provide long distance service, and, have leveraged that authority into enormously successful marketing and sales of bundled services.

Rate Counsel has previously stated in comments submitted to the Commission that the non-rural high cost fund (designed to “protect” ILECs) has become an anachronism, and the FCC should immediately take steps to impose a sunset date for this fund. Congress, with the 1996 Act, did not foresee that seven regional Bell operating companies would dwindle to three (or that the RBOCs would eliminate GTE and Southern New England Telephone Company as stand-alone ILECs), nor did it envision that the RBOCs would acquire AT&T and MCI, their chief competitors. Congress anticipated robust local competition and, with the universal service provisions, sought to protect RBOCs from the erosion of implicit support in the wake of much-anticipated local competition. Instead RBOCs now have the best of all worlds – they continue to dominate the local market, they have rapidly gained long distance market share, *and* they receive the non-rural high cost fund support. Furthermore, the RBOCs have failed to demonstrate that, without such high cost support, they would be unable to offer service at affordable rates. The Commission should end the present regime whereby consumers' phone bills support a seeming black hole of high cost support.

Furthermore, the Commission should, consistent with the Joint Board's recommendation, impose a cap of the total amount of high-cost funding at \$4.5 billion.<sup>132</sup>

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<sup>131</sup> / Rate Counsel calculated that in 2006, AT&T earned a rate of return of 99.6% on special access services; Qwest earned a rate of return of 132.2%; Verizon's rate of return was 51.8%. See Federal Communications Commission, ARMIS Report 43-04, Table I, data run 8/6/2007.

<sup>132</sup> / Recommended Decision, at para. 26.

Rate Counsel supports the gradual elimination of support from the identical support rule, which will, as the Joint Board states, provide a source of monies for the Mobility and the Broadband funds.<sup>133</sup> The Joint Board indicates that shifting funds now provided to eligible telecommunications carriers (“ETCs”) to the Mobility Fund will yield approximately \$1 billion year to support the Mobility goals.<sup>134</sup> As discussed in above, Rate Counsel questions whether \$300 million is sufficient to close the digital divide.

Rate Counsel also supports the Joint Board’s recommendation that each for the five major current high cost support mechanisms be capped at their current levels (high-cost loop; local switching; interstate common line; interstate access; and high cost model).<sup>135</sup>

#### **IV. REVERSE AUCTIONS**

The Commission seeks comment on the merits of using reverse auctions to determine the level of high-cost support to provide to eligible telecommunications carriers.<sup>136</sup> Under a reverse auction system, the lowest bid of a potential provider would determine the high cost support for a particular auctioned area.<sup>137</sup>

The Commission describes diverse ideas for the mechanics of such an auction, including, for example, proposals of the CTIA – The Wireless Association (“CTIA”), Verizon, and Alltel,<sup>138</sup> and raises various issues for comment. Although theoretically appealing as a way to attract the lowest cost supplier for a particular area, Rate Counsel

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<sup>133</sup> / *Id.*, at para. 27.

<sup>134</sup> / *Id.*, at para. 28.

<sup>135</sup> / *Id.*, at para. 32.

<sup>136</sup> / Reverse Auction NPRM, at para. 1.

<sup>137</sup> / *Id.*

<sup>138</sup> / *Id.*, at paras. 5-8.

opposes the widespread use of reverse auctions because of its practical limitations. Rate Counsel concurs with the concerns raised by Commissioner Copps who stated that the Joint Board’s review raised “many more questions than it answered.”<sup>139</sup> He elaborated:

For instance, how do we ensure that the winning bidder provides adequate quality of service? What happens if the winner later decides it is no longer profitable to continue its operation? And who will be responsible for establishing the rules and enforcing them? Ironically, this purportedly market-based approach strikes me as hyper-regulatory.<sup>140</sup>

If the Commission, nonetheless, decides to use reverse auctions as a way to distribute high cost funds, Rate Counsel opposes awarding support to multiple bidders.<sup>141</sup> Certainly if an area is too costly to serve without support, it would be even yet less efficient to subsidize more than one supplier, because potential economies of scale would be lost under such a multiple-winner system. Furthermore, Rate Counsel concurs with the Commission that “if the size of the subsidy is determined by the lowest bid of a non-winning bidder, the per-carrier subsidy would be expected to rise as the number of winners increased.”<sup>142</sup>

Rate Counsel recognizes that a multiple-winner system could yield “more competition” for consumers in a given area than would a single-winner system as a result of the potential presence of multiple suppliers,<sup>143</sup> but urges the Commission not to implement a more costly system for the sake of competition. Ultimately consumers pay

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<sup>139</sup> / *Id.*, Statement of Commissioner Michael J. Copps, Approving in FCC 08-22, Approving in FCC 08-4, Approving in Part, Dissenting in Part in FCC 08-5, at 32.

<sup>140</sup> / *Id.*

<sup>141</sup> / Reverse Auctions NPRM, at paras. 13-17.

<sup>142</sup> / *Id.*, at para. 15.

<sup>143</sup> / *Id.*, at para. 16.

for high-cost support, and the artificial competition resulting from a multiple-winner system would lead to a more costly result, and therefore should not be pursued.

The Commission seeks comment on the appropriate geographic areas to use for reverse auctions.<sup>144</sup> As the Commission indicates, a larger area is more likely to include subsets of customers that are more profitable to serve (because of their relatively lower cost or demand for high-revenue services), which could lower the subsidy required.<sup>145</sup> The Commission tentatively concludes that the wireline ILEC's study area is the appropriate geographic area for reverse auctions and that "further disaggregation is appropriate only if the total support is not increased for the resulting areas, but is capped at the award amount for the original study area."<sup>146</sup> Rate Counsel concurs with this conceptual analysis, but it is not clear whether, if a particular study area is the basis of a reverse auction, would the incumbent carrier, if it lost the auction, then be precluded from serving customers in that area. If not, then the winning bidder would not necessarily serve the "more profitable" customers (if the ILEC continued to do so), yet if the ILEC were precluded from serving the area, consumers could confront disruptions. Again, this idea has hypothetical appeal, but the implementation issues raise serious practical concerns that outweigh the hypothetical benefit.

On the other hand, pinpointing small high cost areas on which to base reverse auctions could lead to astronomical costs because, the greater the disaggregation of the cost analysis, the more "above-average" costs will ensue. As Rate Counsel discusses above, granular high cost analysis will cause the high-cost fund to increase substantially

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<sup>144</sup> / *Id.*, at paras. 19-22.

<sup>145</sup> / *Id.*, at para. 21.

<sup>146</sup> / *Id.*

and will fail to recognize the economies of scale that ILECs otherwise enjoy, not to mention the numerous below-cost areas that they then would serve. Reverse auctions should not be structured so as to raise consumers costs.

Rate Counsel urges the Commission to reject reverse auctions as a way of distributing high cost because of the numerous implementation challenges that would thwart the achievement of its purported goal of achieving an efficient high cost distribution system. Instead, Rate Counsel recommends that the Commission use an auction system on a trial basis to support the deployment of broadband service to unserved and underserved areas.<sup>147</sup> The use of a trial is far preferable to up-ending an existing high cost distribution system and an auction for an area that is presently unserved and underserved would raise fewer implementation issues than would overlaying an auction for service that is already being provided.

Rate Counsel has previously stated:

RBOCs point to new technology as evidence of competition. If, indeed, new technology is becoming the platform for local competition, then any high cost support that the FCC distributes should be used for that new technology. Presently, the monies largely flow to landline incumbents and CETCs. If there are any areas of the nation, served by non-rural carriers, where, absent support, the rates would be prohibitive, boundaries should be drawn and those areas put out for competitive bid to the lowest cost supplier, whether it be broadband over power line, wireless, or VoIP. If the Commission seeks to subsidize services in high-cost areas, those subsidies should at least support new technology so that rural customers of non-rural carriers are not left behind as the nation migrates to a broadband platform. Carriers that receive federal subsidies should deploy broadband throughout their regions. At a minimum, the Commission should consider NASUCA's "Network Investment Incentive Plan" whereby

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<sup>147</sup> / *Id.*, at paras. 50-51.

carriers' non-rural high cost support would decrease if they fail to deploy broadband.<sup>148</sup>

Indeed, as the FairPoint-Verizon transactions demonstrated, Verizon, a non-rural carrier, woefully deployed broadband in the northern three New England states, leaving, for example, New Hampshire last in the nation.<sup>149</sup>

Rate Counsel has previously stated:

To promote the affordable availability of advanced services, incumbent local exchange carriers (“ILEC”) should offer broadband and fiber to the home at POTS prices. If there are areas of the country that are either underserved or entirely neglected, the boundaries of those areas should be defined clearly. If the reason for the lack of advanced services is that the anticipated revenues from the advanced services would not cover the anticipated cost of deployment, the areas should be opened to high-cost bidding by competitors to serve the area. Competitors should then be required to commit to specified minimum service quality requirements, maximum pricing constraints, and minimum years of commitment to service. The competitor requiring the least amount of high cost support should be awarded the unique opportunity to serve the area for a specified period of time, until it can be demonstrated that the geographic area can support multiple suppliers. Alternatively, consumers should be awarded high cost/advanced services funds directly to be used as an offset against a broadband bill.<sup>150</sup>

Rate Counsel also reiterates its support for the Commission’s efforts, in partnership with states, to assess the status of telecommunications and information infrastructures throughout the nation. Such an assessment, however, should not be

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<sup>148</sup> / Rate Counsel 2006 USF Reply Comments, at pages 35-37, citing NASUCA, at 92.

<sup>149</sup> / *Verizon New England, Inc., Bell Atlantic Communications, Inc., Nynex Long Distance Co., Verizon Select Services, Inc. And Fairpoint Communications, Inc. - Petition for Authority to Transfer Assets and Franchise*, New Hampshire PUC Docket No. DT 07-011, Order Approving Settlement Agreement with Conditions; FCC, *High Speed Services for Internet Access: Status as of June 30, 2007*, released March 2008, at Table 14, showing New Hampshire ranked last in terms of DSL availability.

<sup>150</sup> / In the Matter of High-Cost Universal Service Support, WC Docket No. 05-337; Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Comments of the New Jersey Division of Rate Counsel, March 27, 2006, at 24, cite omitted.

limited to a comparison of rural and urban areas, but rather should encompass also a comparison of infrastructures in communities of diverse incomes.<sup>151</sup>

## V. ELIGIBLE TELECOMMUNICATIONS CARRIERS

The origin of the out-of-control CETC portion of the high-cost fund was well-intentioned, namely to promote universal service in a competitively neutral manner. As explained by the Commission, it “adopted the Joint Board’s recommendation that it make incumbent carriers’ support payments ‘portable to other eligible telecommunications carriers’” and “[i]n justifying this portability requirement, both the Joint Board and Commission made clear that they envisioned that competitive ETCs would compete directly against incumbent LECs and try to take existing customers from them.”<sup>152</sup> The expectation had been that CETCs’ would “capture” the lines that ILECs had previously served. As explained further by the Commission:

The predictions of the Joint Board and the Commission have proven inaccurate, however. First, they did not foresee that competitive ETCs might offer supported services that were not viewed by consumers as substitutes for the incumbent LEC’s supported service. Second, wireless carriers, rather than wireline competitive LECs, have received a majority of competitive ETC designations, serve a majority of competitive ETC lines, and have received a majority of competitive ETC support. These wireless competitive ETCs do not capture lines from the incumbent LEC to become a customer’s sole service provider, except in a small portion of households. Thus, rather than providing a complete substitute for traditional wireline service, these wireless competitive ETCs largely provide mobile wireless telephony service in addition to a customer’s existing wireline service.<sup>153</sup>

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<sup>151</sup> / *Id.*, at 26.

<sup>152</sup> / Identical Support NPRM, at para. 8, cite omitted.

<sup>153</sup> / *Id.*, at para. 9, cites omitted.

As a result, the identical support rule has increased the quantity of supported lines, and yet there is no evidence that the support has subsidized the deployment of services to underserved or unserved areas. As the Commission explains, because the level of the ETC's support is based on the support that the ILEC receives, "the competitive ETC has little incentive to invest in, or expand, its own facilities in areas with low population densities, thereby contravening the Act's universal service goal of improving the access to telecommunications services in rural, insular and high-cost areas," and "[i]nstead, competitive ETCs have a greater incentive to expand the number of subscribers, particularly those located in the lower-cost parts of high-cost areas, rather than to expand the geographic scope of their networks."<sup>154</sup>

In addition to remedying the flawed identical support rules, Rate Counsel urges the Commission to consider carefully the potential for unanticipated consequences as it designs the Mobility and Broadband Funds. The identical support rule has resulted in the subsidization of multiple networks and caused the high-cost fund to increase enormously and without control. Rate Counsel concurs wholeheartedly with the Joint Board that "it is no longer in the public interest to use federal universal service support to subsidize competition and build duplicate networks in high-cost areas"<sup>155</sup> and concurs that the Commission should eliminate the identical support rule. Rate Counsel further supports the outcome described by the Joint Board that support should be provided to at most only one wireline, one wireless, and one broadband provider in any given area.<sup>156</sup>

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<sup>154</sup> / *Id.*, at para. 10.

<sup>155</sup> / Recommended Decision, at para. 35.

<sup>156</sup> / *Id.*, at para. 37.

Rate Counsel concurs with the Commission's tentative conclusion that it should eliminate the "identical support" rule.<sup>157</sup> The rule has benefited some suppliers, but has raised consumers' USF contributions without commensurate benefit. Eliminating the identical support rule is long overdue.

High-cost support has increased from approximately \$1.2 billion in 1996 to approximately \$4.3 billion.<sup>158</sup> The competition envisioned by the 1996 Act was intended to benefit consumers and lower rates. The purpose of the high cost fund is to make implicit support explicit. This transition to explicit support, however, should have led to rate *decreases* for other services which, previously, had been providing implicit support. Instead, consumers have experienced a ratcheting up of rates.

Rate Counsel recognizes that a major reason for the growth in high cost support has been the growth in competitive ETC support from under \$17 million in 2001 to \$1.2 billion in 2007.<sup>159</sup> Rate Counsel also concurs with the Commission should fundamentally reform how it distributes support under the high cost fund.<sup>160</sup>

Much of the Commission's Identical Support NPRM concerns how one might compute the costs for competitive ETCs. In no event, should the Commission contemplate providing high cost support at an amount that is *greater* than that provided to the ILEC because consumers should not be funding inefficient entry. If it costs less for the ILEC to serve an area than an alternative carrier, it would be inefficient to subsidize

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<sup>157</sup> / Identical Support NPRM, at para. 1.

<sup>158</sup> / 2007 Monitoring Report, Tables 3.1 and 3.14.

<sup>159</sup> / Identical Support NPRM, at para. 4; USAC 2007 Annual Report, at 45.

<sup>160</sup> / Identical Support NPRM, at para. 5.

the entry of a higher-cost supplier.<sup>161</sup> Rate Counsel welcomes competition that is based on economic efficiency, but opposes costly efforts to bolster competition. Consumer choice among providers, of course, is desirable, but the pursuit of competition should not cloud judgment about potentially expensive programs, for which consumers ultimately must pay.

As the Commission has stated, the wireless competitive ETCs are not capturing lines from the ILEC to become a customer's sole service provider, except in a minority of cases, and "the majority of households do not view wireline and wireless services to be direct substitutes."<sup>162</sup> Under the existing high-cost fund structure, a "competitive ETC has little incentive to invest in, or expand, its own facilities in areas with low population densities, thereby contravening the Act's universal service goal of improving the access to telecommunications services in rural, insular and high-cost areas."<sup>163</sup> The Commission should immediately cap the competitive ETC fund and eliminate the identical support rule.

## V. CONCLUSION

Rate Counsel welcomes the Commission's comprehensive reform of the high cost fund. Among other things, Rate Counsel supports the elimination of the identical support rule, the use of a reverse auction on a pilot basis to support affordable broadband deployment in unserved and underserved regions of the country, establishing a cap on all

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<sup>161</sup> / As stated by the Commission, limiting the amount that competitive ETCs could receive to the amount that the ILEC receives "could avoid rewarding competitive ETCs for being inefficient and reduce incentives for competitive ETCs to inflate their costs." Identical Support NPRM, at para. 25.

<sup>162</sup> / *Id.*, at paras. 9-10. See also, Verizon News Release, "New Survey Shows 83 Percent of Consumers Continue to Rely on Landline Voice Service for Its Quality, Safety Features," March 27, 2008; Centers for Disease Control and Prevention, National Center for Health Statistics, *Wireless Substitution: Early Release of Estimates Based on Data from the National Health Interview Survey, January – June 2007*.

<sup>163</sup> / Identical Support NPRM, at para. 10, citing 47 U.S.C. § 254(b)(5).

high cost support that is no greater than the 2007 high cost support, and eliminating high cost support for Bell operating companies.

Respectfully submitted,

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