

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

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| 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
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I. INTRODUCTION AND SUMMARY

A. INTRODUCTION

The New Jersey Division of Rate Counsel (“Rate Counsel”), with this filing,¹ replies to comments submitted in response to the three Notices of Proposed Rulemaking (“NPRM”) issued by the Federal Communications Commission (“FCC” or “Commission”).² The complexity of the issues encompassed by the three NPRMs is

¹ / On May 15, 2008, the Commission extended the deadline for reply comments until June 2, 2008. Rate Counsel is submitting this single, integrated filing in each of the Commission’s three rulemakings.

² / Approximately ninety commenters filed more than one thousand pages. In the Matter of High-Cost Universal Service Support, FCC WC Docket No. 05-337; Federal-State Joint Board on Universal Service, FCC CC Docket No. 96-45, Motion for Extension of Time filed by Independent Telephone and Telecommunications Alliance (ITTA), National Exchange Carrier Association (NECA), National Telecommunications Cooperative Association (NTCA), Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO), United States Telecom Association (USTelecom), and Western Telecommunications Alliance (WTA), May 1, 2008, at 2. Furthermore, two proposals were submitted subsequent to the filing of initial comments: Qwest submitted a proposal on May 5, 2008; Sprint Nextel submitted a proposal on May 12, 2008. Ex Parte Letter from R. Steven Davis, Senior Vice President – Public Policy and Shirley Bloomfield, Senior Vice President- Federal Relations, Qwest, to Ms. Marlene H. Dortch, Secretary, Federal Communications Commission, Re: In the Matters of Federal-State Joint Board on Universal Service, High-Cost Universal Service Support, CC Docket No. 96-45, WC Docket No. 05-337, May 5, 2008, Attachment: “Proposal for Implementing the Tenth Circuit’s Remand in Qwest II” (“Qwest Wire Center Proposal”); Ex Parte Letter from Anthony M. Alessi, Senior Counsel,

daunting but the need for high-cost reform is great, and making affordable broadband service available to all Americans is essential. Many issues that the NPRMs raise are inter-related, and, therefore, to avoid repetition, Rate Counsel frequently cross-references sections within its reply comments.

Rate Counsel commends the Commission on its ambitious undertaking and urges the Commission, where feasible, not to implement major new programs that would be costly and time-consuming to implement. Instead, the Commission should be scaling back existing programs and judiciously using pilot programs to assess the merits of new funding mechanisms. Also, Rate Counsel recommends that the Commission adopt mechanisms for carriers' accountability to consumers and establish unambiguous sunset dates. Rate Counsel also urges the Commission to continue to take steps to rein in the high cost fund ("HCF"), whose costs ultimately are borne by consumers. As the HCF increases, so too do consumers' telecommunications bills. As a result of mega-mergers among incumbent local exchange carriers ("ILEC"), states' decisions to deregulate local exchange service in numerous markets, technological advances, and emerging competition, the need for high cost support should be diminishing. Furthermore, in no event should the universal service fund ("USF") be used as a shield to insulate ILECs from the effects of competition.

The regulatory status of broadband service (*e.g.*, the Commission's 2005 determination that broadband is an information and not a telecommunications service) further complicates the Commission's pursuit of universal service. Indisputably, affordable access to broadband service, offered at reasonable upload and download

Sprint Nextel, to Ms. Marlene H. Dortch, Secretary, Federal Communications Commission, Re: WC Docket No. 05-337; CC Docket No. 96-45, May 12, 2008, Attachment: "Universal Service Reform: High Cost Support Four-Step Plan" ("Sprint Nextel Proposal").

speeds, is essential in today's economy. Therefore, Commission efforts in the 21st century to support the widespread availability of broadband service are as important as were historic efforts in the 20th century to ensure widespread affordable dial tone service. The Commission should therefore impose USF fees on broadband services (whether offered by telecommunications or cable companies) for the purpose of generating funds to support broadband deployment to underserved populations (*e.g.*, where income constraints discourage broadband demand, and, therefore, where Lifeline subsidies are warranted) and unserved areas (*e.g.*, in rural, high-cost areas where such deployment has not already been funded through the rural high cost fund or as a result of regulatory bartering with state commissions). Furthermore, new funds should augment and not replace private investment: only as much funding as is necessary to make an unsound business case a sound one should be provided through the federal USF.

On May 1st, the FCC released an order adopting the recommendation of the Federal-State Joint Board on Universal Service (“Joint Board”) to place an “interim, emergency cap” on the amount of high-cost support that competitive eligible telecommunications carriers (“CETCs”) may receive.³ As of the date of the Order, annual CETC support for each state will be capped at the March 2008 annualized level. The FCC adopted two exceptions. First, a competitive ETC can file its own cost data demonstrating that its costs meet the support threshold (similar to ILECs). Second, a “limited” exception was adopted for CETCs serving tribal lands and Alaska Native regions.

³ / In the Matter of High-Cost Universal Service Support, WC Docket No. 05-337; Federal-State Joint Board on Universal Service, CC Docket 96-45, Alltel Communications, Inc. et al. Petitions for Designation as Eligible Telecommunications Carriers, RCC Minnesota, Inc. and RCC Atlantic, Inc. New Hampshire ETC Designation Amendment, *Order*, rel. May 1, 2008 (“CETC Cap Order”), at para. 1.

In the May 1st Order, the FCC “commits to completing a final order on comprehensive [Universal Service] reform as quickly as feasible after the comment cycle is completed on the pending Commission Notices regarding comprehensive reform.”⁴ However, FCC Commissioner Copps expressed concern in his dissenting statement accompanying the Order that the cap will be a “band-aid” that may put “real reform on the back-burner.”⁵ Some parties have suggested that an interim cap is needed as an initial first step to reform USF comprehensively. However, CETCs have complained that they are taking the brunt of reforms and have expressed concern that once such a cap is implemented, it will never be removed. ILECs now lack a compelling incentive to “come to the table” with respect to wholesale Universal Service reform in the wake of this decision because the FCC has addressed, at least on an interim basis, the most egregious aspect of the existing USF.

Various specific plans for reforming high cost support and subsidizing wireless and broadband deployment have been proposed. Rate Counsel urges the Commission first to adopt major policy positions and then to work out the necessary details of universal service program implementation once those major decisions have been made. For the most part, these reply comments focus primarily on the major policy matters that the Commission’s NPRMs raise.

B. SUMMARY

In this section, Rate Counsel reiterates its major analyses and recommendations regarding high cost reform, programs to ensure that all Americans have affordable access to broadband service, the deployment of wireless facilities to unserved areas, and the

⁴ / *Id.*

⁵ / *Id.*, Dissenting Statement of Commissioner Michael J. Copps, at 112.

overall achievement of universal service goals in an economically efficient and fair manner. The timely resolution of these complex matters bears directly on the affordability of telecommunications services for consumers, efficient market signals for private investment, and the health of the United States' economy.

Summary of analyses

Based on its economic and regulatory analysis of industry developments and the initial comments submitted in this proceeding, Rate Counsel's major conclusions are:

- *Mergers and acquisitions by Bell operating companies ("BOC"), their use of consumer-funded common networks for unregulated services, and their high profits are evidence that high cost subsidies are no longer needed:* As a result of multiple mergers and their use of a common network platform to provide unregulated, high-revenue services, high cost support for Bell operating companies is no longer needed in order to achieve the goals of the Telecommunications Act of 1996 ("Act" or "1996 Act").⁶ Rate Counsel notes that Verizon and AT&T had profits margins of 10% and 6% in 2007 despite heavy investment in FiOS and U-Verse, respectively. Qwest, in contrast, is not currently pursuing a fiber-to-the-premises strategy, and had a profit margin of 21% in 2007.⁷
- *Competition and technological advances should drive down the cost of USF:* Instead, the high cost fund has been increasing.
- *Consumers bear the cost of high cost support:* Because consumers ultimately pay for USF, the Commission should ensure that any support is essential, efficiently and fairly collected and distributed, and subject to periodic and rigorous regulatory scrutiny.
- *Where markets have been declared competitive, subsidies should no longer be required:* Where ILECs have been granted rate deregulation, high cost support is no longer necessary or appropriate because, where rates are deregulated (presumably based on a finding of effective competition), ILECs can set market-based rates.

⁶ / 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.

⁷ / AT&T 2007 Annual Report, page 26; Verizon 2007 Annual Report, page 17; Qwest 2007 Annual Report, page 55.

- *High-cost support distributed on a granular basis would overlook economies of scale and scope:* Targeting high cost support on a wire center basis offers a misleading impression of economic efficiency. Instead, this proposal, which ILECs have advanced for many years, would inflate high cost support unnecessarily and ignore ILECs' economies of scale and scope.
- *The high administrative costs of implementing new programs (such as reverse auctions) should be considered carefully before embarking on such programs:* Where the Commission wishes nonetheless to pursue new programs or substantially new ways of distributing funds, it should use a pilot program to test the waters.
- *Until the Commission addresses the Court's Qwest II directive to determine "reasonably comparable" rates, the Commission cannot gauge whether the universal service goals of the 1996 Act are being achieved.* Determining benchmarks for assessing the reasonable comparability of urban and rural rates is an essential component of high cost reform.⁸ Without ways to gauge whether rate comparability has been achieved, the HCF will continue to be perceived as a "black hole" for support because regulators will lack a way to measure "success."
- *The increasingly indispensable characteristic of high-speed access to the Internet means that affordable access to broadband service is essential for all.* As Rate Counsel has stated in numerous previous pleadings, Commission leadership and regulatory intervention are critically important to narrow the "digital divide" and to ensure that all Americans can partake in mainstream, Internet-based society.

Summary of recommendations

Rate Counsel reiterates its major recommendations to the Commission regarding the reform of existing high cost programs and the design of new universal service support.

- The Joint Board recommends a transition of five years, consisting of the gradual reduction of identical support funding to provide the source for

^{8/} In 2005, the FCC sought comment on "how reasonably to define the statutory terms 'sufficient' and 'reasonably comparable' in light of the Court's holding in *Qwest II*." *In the Matter of Federal-State Joint Board on Universal Service*, FCC CC Docket No. 96-45; *High-Cost Universal Service Support*, FCC WC Docket No. 05-337, *Notice of Proposed Rulemaking*, Rel. December 9, 2005, at para. 1, citing *Qwest Corp. v. FCC*, 398 F.3d 1222 (10th Cir. 2005) ("Qwest II"). Rate Counsel submitted initial and reply comments on March 27, 2006 and May 26, 2006, respectively, in the Commission's *Qwest II* proceeding.

Broadband and Mobility Funds.⁹ Rate Counsel supports such a transition, but recommends a three-year transition.

- High cost support should be discontinued for Bell operating companies and other price cap carriers, and should be phased out for other non-rural carriers and for rural carriers over a three-year period.
- Consistent with the Congressional directive in Section 706 of the 1996 Act, the Commission should assess broadband services a USF charge to support broadband deployment in unserved regions of the country and to subsidize broadband rates for underserved populations such as Lifeline participants.
- Using funds generated from an assessment on broadband revenues, ILECs and cable companies should provide subsidized broadband rates for participants in Lifeline/Link Up programs.
- Reverse auctions, if pursued at all, should be used on a trial basis to subsidize the one-time construction costs of broadband deployment in unserved areas, and then evaluated carefully, with all aspects of the program made public. The Commission should reinforce the obligation of all providers (cable and telecommunications companies) to provide detailed data to state regulators about their broadband deployment so that assistance can be targeted to areas that private investors would neglect.
- Broadband support for subsidized broadband Lifeline rates and for construction to unserved areas should be distributed to states, proportionally, based on population.
- The fundamental aspects of the Lifeline/Link-Up program should not be modified, but the Commission should require ILECs to demonstrate their efforts to publicize the program's availability.
- High cost support should not be a vehicle for protecting ILECs from the impact of competition. High cost support should not be available for any regions of the country in which ILECs' rates have been deregulated.
- States that receive federal high cost support should be required to provide matching funds, or have their high cost support halved.
- The Commission should reject proposals to award high cost support on a wire center level.
- The Commission should reject Sprint Nextel's proposal to "solve" the USF challenge by shifting the burden to the subscriber line charge.
- The Commission should respond to the Court's *Qwest II* directive regarding the determination of reasonably comparable rates.

⁹ / *In the Matter of High-Cost Universal Service Support*, FCC WC Docket No. 05-337; *Federal-State Joint Board on Universal Service*, FCC CC Docket No. 96-45, *Recommended Decision*, Rel. November 20, 2007 ("Recommended Decision"), at para. 27.

II. CONSUMER IMPACT

A. USF FEES

The Commission should consider the impact of the existing high cost fund and any reform to the existing high cost fund on consumers.

As stated in initial comments, Rate Counsel urges the Commission to consider the impact of any USF programs on consumers.¹⁰ As the Indiana Utility Regulatory Commission (“IURC”) states, “the current growth rate of the fund will jeopardize the future viability of all universal service programs, thereby affecting the future of affordable and ubiquitous access to telecommunications services for consumers.”¹¹ The increasing fund (and thus increasing 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.¹² 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).”¹³ While universal service funds (and thus fees) have been increasing (purportedly to make implicit support explicit), rates that provided implicit support have not experienced a corresponding decline.¹⁴

Rate Counsel concurs with Verizon and Verizon Wireless that USF “burden[s] consumers with large surcharges, inefficiently distributing support, and failing to create

¹⁰ / Rate Counsel, at 14, citing Recommended Decision, Statement of Commissioner Deborah Taylor Tate, at 30.

¹¹ / IURC, at 14.

¹² / Rate Counsel, at 14.

¹³ / *Qwest II*, at 1234, citing *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2001) (“Qwest I”), at 1200.

¹⁴ / Rate Counsel, at 16-17.

the proper incentives for companies to serve rural America.”¹⁵ Rate Counsel also echoes the concern raised by the New Jersey Board of Public Utilities (“New Jersey Board”):

New Jersey ratepayers have paid more than \$722 million in excess of what they have received from the Fund in just four years (2003-2006), *NEARLY THREE QUARTERS OF A BILLION DOLLARS!!* ... It is time to reduce the burden on urban states such as New Jersey and its ratepayers, many of whom struggle to pay for their own services from having to subsidize telephone service (and as proposed in the Recommended Decision, broadband services) of rural consumers.¹⁶

Rate Counsel also concurs with the New Jersey Board that “[b]efore the FCC considers a new high-cost structure, it *must* revise the currently flawed allocation of funds to make it more equitable to states like New Jersey”¹⁷ and similarly concurs with the MACRUC States that the proposed cap “does nothing to reduce the already overburdened ratepayers in donor states.”¹⁸ The California Public Utilities Commission (“CPUC”) similarly recommends that the Commission “guard against unlimited and untargeted funding” of the USF.¹⁹ As Verizon and Verizon Wireless stated: “[u]nder the current system, many providers receive support at levels far in excess of what is necessary to ensure affordable universal service to consumers.”²⁰

Rate Counsel acknowledges that the 1996 Act requires reasonably comparable rates, but reminds the Commission that, in fulfilling that goal, it must not thwart the equally compelling goal of affordable service for all by requiring consumers to pay

¹⁵ / Verizon and Verizon Wireless, at 1.

¹⁶ / New Jersey Board, at 4 (emphasis in original).

¹⁷ / *Id.*, at 13 (emphasis in original). See also MACRUC States, at 2-3 (stating that “MACRUC ratepayers have paid more than **\$2 Billion** in excess of what we have received from the federal Universal Fund (FUSF) in just four years (2003 – 2006)” (emphasis in original)).

¹⁸ / MACRUC States, at 3.

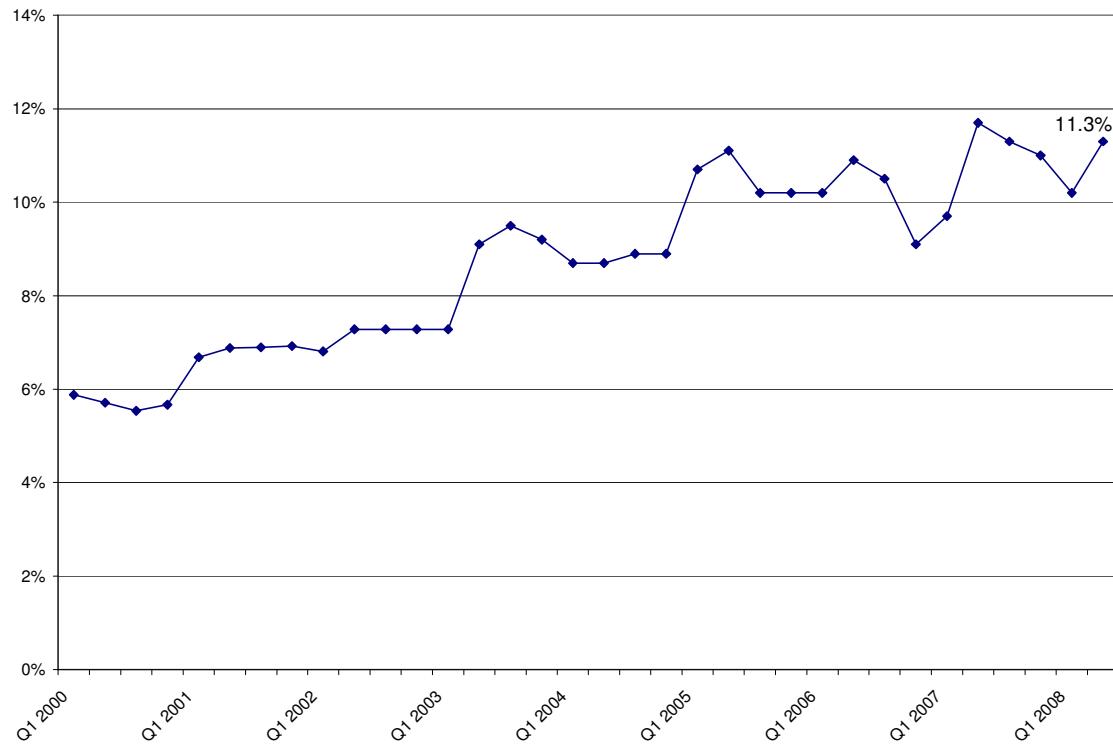
¹⁹ / CPUC, at 17.

²⁰ / Verizon and Verizon Wireless, at 1.

excessive USF contribution fees. The following graph shows that the USF contribution fee almost doubled between 2000 and 2008.

Figure 1

USF Contribution Fee Nearly Doubles Between 2000 and 2008²¹



B. LIFELINE/LINK UP PROGRAM

The Lifeline/Link Up program is working effectively, and, therefore, should not be disrupted by high cost reform, but rather should be expanded to encompass broadband access.

Rate Counsel concurs with the New Jersey Board that reform of the high-cost fund should not harm the Lifeline/Link Up program.²² Instead reform should occur in

²¹ / FCC, Wireline Competition Bureau, Industry Analysis and Technology Division, *Trends in Telephone Service*, February 2007 (“Trends – 2007”), Table 19.17.

²² / New Jersey Board, at 14. See, also, MACRUC States, at 7.

two areas to ensure that all Americans have access to the telecommunications infrastructure at affordable rates:

1. The Commission should encourage state regulators and telecommunications providers to enhance their outreach efforts to increase Lifeline/Link Up participation. Programs such as the Lifeline/Link Up program are critically important to achieve and maintain universal service goals.
2. Rate Counsel supports broadband subsidies for Lifeline/Link Up participants. In its initial comments, Rate Counsel quoted an earlier filing, which proposed use of Lifeline subsidies and support for funds in the hands of consumers.²³ Rate Counsel also stated: “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 supply. To this end, Rate Counsel encourages the Commission to move forward with enabling financial incentives for build-out to unserved and underserved areas.”²⁴ Rate Counsel does not advocate the use of “broadband vouchers” *per se* (because this would entail substantial administrative costs), but does support fully the expansion of the existing Lifeline/Link Up program to subsidize broadband service for income-eligible customers (because using the existing program as a platform would minimize administrative overhead and also would target support to

²³ / Rate Counsel at 32, citing *In the Matter of Federal-State Joint Board on Universal Service, High-Cost Universal Service Support*, CC Docket No. 96-45, WC Docket No. 05-337, Comments of the New Jersey Division of the Ratepayer Advocate, March 27, 2006 (“Rate Counsel 2006 USF Initial Comments”), at 22-23.

²⁴ / *Id.*, at 30.

consumers). As Section IV discusses, an assessment on broadband revenues could be used to finance part of these broadband subsidies.

C. ACCOUNTABILITY

Establishing guidelines for assessing “reasonably comparable” rates is essential to measuring the nation’s success in achieving universal service.

Resolving the thorny issue of determining “reasonably comparable” urban and rural rates is a threshold requirement for establishing USF accountability.²⁵ Until states and the Commission have a yardstick by which to measure whether rural rates are reasonably comparable to urban rates, the success of the USF cannot be gauged. As a consequence, the high cost fund could be higher than is necessary, with the excess support burdening consumers unduly. As Rate Counsel has said previously, numerous factors influence rate comparability, stating for example that “[s]tate rate designs are inherently complex and difficult to compare, which means that the Commission should establish broad ranges for assessing ‘reasonable comparability.’”²⁶ Without ways to gauge whether reasonable urban/rural rate comparability has been achieved, consumers are at risk of subsidizing an inflated HCF.

Qwest and others express concern about the Commission’s inaction with respect to addressing the *Qwest II* remand. Qwest asserts that the Commission’s focus on wireless and overall reform has delayed Commission focus on the remand: “After a dozen years and two court reversals, the Commission still lacks lawful rules ensuring that

²⁵ / See National Cable & Telecommunications Association (“NCTA”), at 14.

²⁶ / *In the Matter of Federal-State Joint Board on Universal Service*, FCC CC Docket No. 96-45; *High-Cost Universal Service Support*, FCC WC Docket No. 05-337, *Notice of Proposed Rulemaking*, Rel. December 9, 2005, at para. 1, citing *Qwest II*. Rate Counsel 2006 USF Comments, at 29. See, also *id.*, stating “Because of these countless factors, which state regulators address, [Rate Counsel] is wary of any federal mechanism that places undue emphasis on precision in rate comparisons. See Rate Counsel’s initial and reply comments for further discussion of “reasonable comparability.”

rural rates for non-rural carriers are ‘reasonably comparable’ to urban rates, as required by the 1996 Act.”²⁷

The National Association of State Utility Consumer Advocates (“NASUCA”) reminds the Commission that it has not dealt with the *Qwest II* decision by determining how to define “reasonably comparable” and “affordable,” stating: “Absent that definition, it is literally impossible for the Commission to determine that any configuration of the high-cost fund – either the new pieces or the remainder that will become the POLR Fund – is sufficient to meet the requirements of 47 U.S.C. § 254.”²⁸

The Commission should examine the HCF carefully and comprehensively.

Rate Counsel concurs with NCTA’s concern about the adverse consequences of the open-ended, unexamined continuation of high cost support. NCTA states:

While these programs have enabled companies to build networks to serve areas that otherwise might have been uneconomic to serve, there is a significant concern that they tend to provide far more support, for a far longer time than is necessary to make it economic for the carrier to serve the supported area. This concern arises from the fact that the program contains no mechanism for reassessing whether the need for support to a carrier has changed due to conditions in the marketplace.²⁹

Rate Counsel urges the Commission to establish periodic examinations of the need for high cost support.³⁰

²⁷ / Qwest, at 5.

²⁸ / NASUCA (re Recommended Decision), at 5-6. *See, also*, IURC, at 3.

²⁹ / NCTA, at 7.

³⁰ / The Commission’s recent decision in which it grants AT&T’s petition for forbearance from cost accounting requirements unfortunately establishes an ill-advised precedent that thwarts access to cost data. In the Matter of Petition of AT&T Inc. For Forbearance Under 47 U.S.C. § 160 From Enforcement of Certain of the Commission’s Cost Assignment Rules, Petition of BellSouth Telecommunications, Inc. For Forbearance Under 47 U.S.C. § 160 From Enforcement of Certain of the Commission’s Cost Assignment Rules, WC Docket No. 07-21, WC Docket No. 05-342, Memorandum Opinion and Order, rel. April 24, 2008.

Rate Counsel also echoes NCTA’s concern that Commission rules that average all costs across the number of lines that an ILEC serves shelter ILECS inappropriately from the impact of competition: as competitors enter markets, ILECs’ per-line subsidies increase.³¹

A fundamental flaw in the HCF is that it does not include mechanisms whereby, based on changing market conditions, support is phased out or eliminated.³² As networks become more efficient, the need for high cost support should be declining. NCTA proposes:

- In those markets where a state has deregulated local exchange service, that HCF be phased out and eventually eliminated.
- An ILEC’s introduction of multichannel video service should cause the FCC to reassess the need for HCF, and, as NCTA observes, “is fully consistent with the Joint Board’s proposal to consider unregulated revenues in determining the need for, and level, of support that a company receives.”³³
- Where multiple CETCs serve a geographic area, USF support is no longer necessary.

Rate Counsel supports NCTA’s proposal that when any of these three triggers is identified, competitive providers should be able to seek a review of the need for continuing support,³⁴ and further urges the Commission to undertake immediately a proceeding whereby it undertakes such a review, and also commits to an annual review of the need for high cost support.

NASUCA similarly expresses concern that in some instances in which carriers’ rates have been deregulated, purportedly in the face of competition (and their rates are asserted to be “market based”), states continue to certify that universal service support is

³¹ / NCTA, at 7.

³² / *Id.*, at 8.

³³ / *Id.*, at 9, citing Joint Board Recommended Decision, at para. 31.

³⁴ / *Id.*, at 10.

required to ensure reasonably comparable rates.³⁵ Rate Counsel agrees with NASUCA’s recommendation that: “it would be reasonable for the Commission to determine that a state, having relinquished control over its retail basic service rates, can have no control over whether those rates are reasonable or reasonably comparable, and thus should not receive any high-cost support.”³⁶ In addition, it is difficult to justify high cost support (that is purportedly granted because no carrier would otherwise serve the area) to a carrier when its rates have been deregulated in the face of purported competition. In the alternative, the Commission should consider NASUCA’s recommendation that if a carrier with deregulated rates receives POLR funding it must use the fund to provide direct credits to customer bills.³⁷

The high cost fund should not subsidize carriers’ entry into unregulated markets.

Rate Counsel concurs with NCTA that “[t]here is no reason whatsoever that consumers should be subsidizing ILEC video services through the high cost mechanism or in any other manner” and that “[a]t the very least, the Commission should ensure that ILECs allocate an appropriate portion of their costs to non-regulated services.”³⁸ The CPUC alternatively proposes that the FCC assess carriers’ unregulated revenues when collecting USF fees.³⁹ Universal service support for broadband services should be

³⁵ / NASUCA (re Recommended Decision), at 32-33.

³⁶ / *Id.*, at 33.

³⁷ / *Id.*

³⁸ / NCTA, at 9-10. Rate Counsel has been raising concerns for several years in pleadings before the Commission regarding ILECs’ regulated telephone service customers’ improper subsidization of ILECs’ pursuit of video and other unregulated services. Rate Counsel, at footnote 58, citing 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.

³⁹ / CPUC, at 12.

limited to support for the deployment of broadband services in areas that otherwise would not occur and for subsidized rates for Lifeline participants.

The USF contribution fee has been increasing, but retail rates have not been declining, resulting in a “double whammy” for consumers.

One metric of a successful USF would be evidence of retail rate reductions. High cost support purportedly enables carriers to translate implicit support (i.e., above cost urban rates) into explicit support (i.e., HCF support). This shift should yield cost-based, *lower* retail rates in urban areas and reasonably comparable, subsidized rates in rural areas. However, as Rate Counsel stated in its initial comments, ILECs have been *increasing* retail rates, which has resulted in the double whammy for consumers of higher telephone service prices *and* higher USF fees.

Rate Counsel reiterates its concern, stated in initial comments:

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.⁴⁰

Subtracting the approximate one billion dollars associated with the identical support rule⁴¹ from the \$4.5 billion high cost fund⁴² yields \$3.5 billion, an amount that should be declining. Competitive pressures, mergers, and technological advancements combined

⁴⁰ / Rate Counsel, at 43.

⁴¹ / CETC Cap Order, at para. 6.

⁴² / Recommended Decision, at para. 26.

with the fact that facilities already have been deployed to provide dial tone to the vast majority of Americans should lead to a declining need for high cost funds.⁴³

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.⁴⁴ Rate Counsel has previously advocated and continues to support the sunset, and indeed, the outright elimination of the non-rural high cost fund. It seems unlikely that Congress, with the 1996 Act, intended the high cost fund to become an unwarranted and unending revenue windfall for ILECs. Unless it adopts provisions for ending the non-rural and rural high cost funds, the Commission will be implicitly endorsing a program whereby, with non-existent accountability (and despite purported competition), ILECs receive an open-ended subsidy from consumers.

States that receive federal high cost support should be required to provide matching funds.

Rate Counsel concurs with the New Jersey Board that states that receive high cost support should be required to provide matching funds.⁴⁵ The New Jersey Board observes that four of the nine states that were the highest net support recipients in 2006 apparently do not have intrastate universal service funds.⁴⁶ A requirement for matching funds would add an important element of accountability on the part of recipient states.

⁴³ / *See, also,* Rate Counsel, at 43-44.

⁴⁴ / *Id.*, at 46, citing Rate Counsel 2006 USF Initial Comments, at 4-5.

⁴⁵ / New Jersey Board, at 12. *See, also,* MACRUC States, at 6-7.

⁴⁶ / *Id.*

III. SUPPORTED SERVICES

The Joint Board recommends that the Commission add broadband Internet service to the definition of supported services.⁴⁷ Rate Counsel and others support the inclusion of “affordable broadband” in the list of supported services.⁴⁸ Rate Counsel disagrees with those who argue that broadband should not be included in the list of services eligible for universal service support. According to Section 706 of the Act, the Commission “shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans . . . by utilizing, in a manner consistent with the public interest, convenience, and necessity, price cap regulation, regulatory forbearance, measures that promote competition in the local telecommunications market, or other regulating methods that *remove barriers to infrastructure investment.*”⁴⁹ Because low population density and complex geography limit the potential revenues a carrier might earn from a given investment, they are impediments to infrastructure investment. Adding broadband to the list of services eligible for high-cost support is a reasonable and appropriate way to remove these “barriers to infrastructure investment” because high-cost support can transform an uneconomic business scenario into an economic possibility.

Broadband services are clearly named as an advanced telecommunications capability. Section 706 states that the term “advanced telecommunications capability” is defined “without regard to any transmission media or technology, as high-speed,

⁴⁷ / Recommended Decision, at para. 56. See, also, *id.*, at para. 57 describing several “beneficial results” of inclusion.

⁴⁸ / Rate Counsel, at 5; IURC, at 5-6 (noting Congress’ intent for universal service to evolve because telecommunications services evolve); NASUCA (re Recommended Decision), at 16; AT&T, at 4.

⁴⁹ / Section 706, paragraph (a) (emphasis added).

switched, *broadband telecommunications capability* that enables users to originate and receive high-quality voice, data, graphics, and video telecommunications using any technology.”⁵⁰ It is clear from the words “high-quality voice, data, graphics, and video” that the Act does not limit “advanced telecommunications capability” to voice service alone. “Advanced telecommunications capability” includes all the features that make broadband access valuable to consumers. It is clear that broadband access should be a supported service.

Some commenters question the Commission’s authority to add broadband to the supported services list. According to Verizon and Verizon Wireless, the Commission’s authority to use federal high cost subsidies to promote universal service is limited to telecommunications services, and the Commission has determined that broadband Internet access is an information service, not a telecommunications service.⁵¹ However, the Commission possesses the requisite authority to support broadband service because, as the Joint Board points out, broadband Internet services have become essential for education, public health, and public safety.⁵² The Joint Board’s assessment that because more than half of all U.S. households already subscribe to broadband access, it is appropriate to view broadband as an “important component of modern life”⁵³ is correct. NASUCA agrees that broadband meets the statutory qualification of a supported service

⁵⁰ / *Id.*, paragraph (c) (emphasis added).

⁵¹ / Verizon and Verizon Wireless, at 31, citing (among others) 47 U.S.C. § 254(c) and *Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities*, Report and Order and Notice of Proposed Rulemaking, 20 FCC Rcd 14853 (2005), para. 17. See also Wyoming Office of Consumer Advocate re Recommended Decision (“Wyoming OCA (re Recommended Decision)”), at 10.

⁵² / Recommended Decision, at para. 58.

⁵³ / *Id.*, at para. 59.

and supports inclusion in the list of supported services.⁵⁴ However, NASUCA includes the caveat that wireless broadband should not be supported.⁵⁵ Rate Counsel agrees.

Others oppose adding broadband to the list of supported services.⁵⁶ Verizon and Verizon Wireless oppose the addition of mobility and broadband to the list of supported services.⁵⁷ Instead, Verizon and Verizon Wireless asserts that the Commission can award one-time wireless construction mobility grants and also encourage public-private partnerships to promote broadband availability and subscribership without changing the list of supported services.⁵⁸

Rate Counsel disagrees with NCTA that the market is already meeting consumers' broadband needs adequately.⁵⁹ NCTA relies on a Commission Press Release regarding its yet to be released Fifth Report to Congress under Section 706 of the 1996 Act ("Fifth Report") to support its assertion that "broadband service is being made available to all Americans on a reasonable and timely basis."⁶⁰ Contrary to the Commission's apparent conclusions in its forthcoming Fifth Report,⁶¹ many Americans continue to lack affordable access to broadband service.⁶²

⁵⁴ / NASUCA (re Recommended Decision), at 16.

⁵⁵ / *Id.*, at 16-17.

⁵⁶ / CPUC, at 2 (asserting that the addition of broadband to the statutory definition of universal service likely would increase the USF substantially).

⁵⁷ / Verizon and Verizon Wireless, at 4, 24-31.

⁵⁸ / *Id.*, at 25.

⁵⁹ / NCTA, at 19.

⁶⁰ / *Id.*, at 19-20.

⁶¹ / Federal Communications Commission Press Release, "FCC Expands, Improves Broadband Data Collection," March 19, 2008. In that press release, the Commission indicates that it adopted a report "showing that broadband services are currently being deployed to all Americans in a reasonable and timely fashion" and finding that "there have been considerable changes and advances in the delivery of broadband-based services and applications since the Fourth Report." Rate Counsel concurs with the dissenting statement of Commissioner Michael J. Copps, instead, that "[w]e can write reports that conclude that Americans are receiving broadband in a reasonable and timely fashion. But the facts are always there,

AT&T is in favor of including broadband as a supported service, and submitted a proposal to fund greater broadband deployment. According to AT&T, “[u]nder the new Broadband Incentive Fund, the Commission would immediately begin providing project-based funding for investment in infrastructure necessary to provide fixed location broadband internet access services in unserved areas.”⁶³

US Telecom opposes the addition of broadband services to the list of supported services.⁶⁴ Nonetheless, US Telecom states that if the Commission does add broadband to the list of supported services, it should do so on a “project-oriented” basis and as a mechanism “entirely separate from current universal service high-cost support mechanisms.”⁶⁵ Rate Counsel concurs. Furthermore, Rate Counsel agrees with US Telecom that “[i]deally the realization of the important social goal of ubiquitous broadband deployment would be funded through the use of general government revenues.”⁶⁶ However, consumers cannot afford to wait for designation of general government revenues for this purpose. Furthermore, Rate Counsel strongly disagrees with US Telecom’s proposed Commission and Congressional steps to promote

glaring and staring us in the faces, showing us where we really stand.” Statement of Commissioner Michael J. Copps, Dissenting, Re: 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, GN Docket No. 07-45, Fifth Report (Mar. 19, 2008). As conceded by Chairman Martin: “But there is certainly more work to be done. That is why I am pleased the Commission today adopts an Order to collect dramatically improved data on broadband services. This improved data will enable us to better identify and analyze the deployment of broadband throughout the nation.” Statement of Chairman Kevin J. Martin, Re: 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.

⁶² / See, e.g., Rate Counsel, at 18-19, 22.

⁶³ / AT&T, at 4.

⁶⁴ / US Telecom, at 32.

⁶⁵ / *Id.*, at 33.

⁶⁶ / *Id.*

deployment, including a “continued light regulatory touch” and “avoidance of new net regulation.”⁶⁷

CPUC opposes adding broadband service to the definition of universal service, and, because it has a pending proceeding regarding the possibility of expanding the California Universal Lifeline Telephone Service Program to include wireless voice service, it does not comment on the possible inclusion of wireless voice to the definition of universal service.⁶⁸

The New Jersey Board asserts that adding broadband to the list of supported services would exacerbate the problems with the size of the high cost fund and that “the possibility of adding broadband without sufficient data on the impact of such added support, would worsen an already critical problem.”⁶⁹ Rate Counsel concurs that additional broadband data is essential to identify unserved areas,⁷⁰ and further concurs that it is essential that relevant federal agencies collaborate to avoid duplicative funding.⁷¹

While Rate Counsel strongly supports the widespread deployment of affordable broadband, at reasonable speed, to all Americans, it also shares the New Jersey Board’s concern about the potential for uncontrolled escalation in the HCF should broadband become a supported service. Nonetheless, in light of the importance of broadband service to mainstream society, Rate Counsel recommends that the definition of universal

⁶⁷ / *Id.*, at 34, stating that net regulation “will kill investment.”

⁶⁸ / CPUC, at 14.

⁶⁹ / New Jersey Board, at 9.

⁷⁰ / *Id.*

⁷¹ / *Id.*, at 9-10 (referring to the Department of Agriculture, Department of Commerce, Department of Health and Human Services, Department of Education, and Appalachian Regional Commission).

service be expanded to include broadband service. The Commission, furthermore, should assume that urban and rural broadband rates are reasonably comparable.⁷² Therefore, the purpose of any broadband support should be to: (1) subsidize one-time construction in unserved areas and (2) subsidize broadband rates for Lifeline customers.⁷³ Furthermore, the total broadband support provided to any state should be distributed proportionally, based on states' population.

As Section IV demonstrates, annual broadband revenues in the United States may be as high as \$40 billion. Assuming a 1 percent assessment, a broadband USF fee would yield \$400 million per year, which, together with the Broadband Fund monies derived from elimination of the Identical Support Rule as recommended by the Joint Board, could support one-time construction grants and subsidize rates for Lifeline participants. While construction grants to expand broadband deployment ideally would be implemented over a short period (*e.g.*, only a few years), support for Lifeline customers would be an ongoing requirement. According to USAC data filed with its Q3 2008 Fund Size Projection, approximately 6,950,000 consumers received Lifeline support in 2007.⁷⁴ Assuming, for example, an illustrative basic broadband service rate of \$20, subsidizing half the rate for broadband access for Lifeline customers would require a subsidy of

⁷² / “Looking at what people reported paying for service, respondents with more than one home high-speed service provider said they paid \$36 monthly for service. Those who said they did not have more than one provider reported a monthly bill of \$38 ... Rural areas are the places with the highest incidence of having one high-speed service available to them. Among rural respondents, 35% said they did not have more than one high-speed provider available to them versus 24% of non-rural respondents who said this.” Pew Internet & American Life Project, “Home Broadband Adoption 2006,” at 8.

⁷³ / NASUCA supports Lifeline subsidies for broadband. NASUCA argues that if broadband Internet service is included as a supported service then Lifeline customers would be eligible for discounts. NASUCA (re Recommended Decision), at 16 and footnote 45.

⁷⁴ / Universal Service Administrative Company, Federal Universal Service Support Mechanisms Fund Size Projections for the Third Quarter 2008, May 2, 2008, Appendix L01 – Lifeline Subscribership by State or Jurisdiction.

approximately \$800 million per year.⁷⁵ The \$400 million derived from a 1% broadband user fee, matched by state subsidies of the same magnitude would yield approximately half of the required subsidy. AT&T recommends that the Commission “establish a Lifeline-only ETC designation to ensure that, as support becomes targeted to provide broadband and advanced mobility services to unserved areas, low-income consumers continue to have access to affordable voice service regardless of where they live.”⁷⁶ Rate Counsel recommends that the Commission determine the requisite funds for ongoing Lifeline support for broadband services and for the one-time costs necessary for the build-out of infrastructure to unserved areas.

NASUCA supports the inclusion of wireless service as a supported service based on the growth of wireless subscriptions since the 1996 Act, stating: “Americans now have a reasonable expectation that quality mobility services should be available in all populated areas of the country, including along state and federal highways.”⁷⁷ However, similar to Rate Counsel, NASUCA notes that support does not recognize wireless service as a complete substitute, but rather, as a complement to wireline service.⁷⁸ NASUCA reasons that “mobility services with their own unique capabilities are increasingly important to a mobile American society” and that wireless services should be “defined based on wireless (not wireline) standards, with funding to qualifying carriers based on a

⁷⁵ / 6.95 million Lifeline subscribers * \$20 per month *12 months * ½ subsidy = \$834 million. Of course, the precise cost would depend on the level of broadband Lifeline participation.

⁷⁶ / AT&T, at 9.

⁷⁷ / NASUCA (re Recommended Decision), at 21.

⁷⁸ / *Id.*, at 21, citing Identical Support NPRM, at para. 9.

set of reasonable customer service expectations that will need to be developed and approved by the FCC.”⁷⁹

With some reservations, Rate Counsel supports the inclusion of wireless as a supported service, but recommends that any USF support be limited to the one-time construction costs for serving unserved areas.

IV. BROADBAND

A. INTRODUCTION

Initial comments address many aspects of broadband support.

Rate Counsel has been a long-time advocate of ubiquitous access to affordable broadband service,⁸⁰ and therefore welcomes the Joint Board’s proposed inclusion of broadband as a supported service.⁸¹ This goal should be achieved in a way that is economically efficient, builds on states’ familiarity with their unserved markets, does not duplicate investment that would occur otherwise, and ensures that all Americans, regardless of their region of the country and their income, have access to an affordable broadband link to the Internet.

Comments on the link between USF and broadband fall into several categories: (1) the need to map unserved areas to inform state and federal decisions regarding the appropriate levels of, and locations for, broadband support; (2) concern that adding broadband to the list of supported services would exacerbate USF growth and may not be permitted because broadband has been declared an information service; (3) recommendations that support be limited to the one-time construction costs of deploying

⁷⁹ / *Id.*, at 22.

⁸⁰ / See e.g., Rate Counsel, at 21, citing Rate Counsel 2006 USF Initial Comments, at 25.

⁸¹ / Recommended Decision, at para. 56-58.

broadband to unserved areas, and furthermore not support the entire construction but rather subsidize only that portion necessary to make a business case profitable; (4) recommendations that if the Commission intends to pursue reverse auctions, it do so on a pilot basis, such as to support the construction costs of broadband (or mobile towers) (see discussion on reverse auctions below); (5) interest in making broadband affordable to Lifeline/Link-Up participants (see discussion regarding Lifeline program in Section III); (6) concerns about the evolving nature of broadband, which in turn lead to recommendations for requirements for minimum download and upload speeds for any supported broadband services; (7) recommendations that broadband revenues be assessed for the specific purpose of subsidizing broadband in unserved areas; and (8) assertions that the rural high cost fund furthers the Commission’s broadband deployment goal.

As stated by Consumers Union, Consumer Federation, and Free Press (“CU et al.”), the Commission, the Joint Board and interested parties have come to an understanding that promotion of broadband should be supported by universal service funds.⁸² However, “large gaps remain between parties when the discussion shifts to implementation. The roots of the debate lie in the phenomenon of convergence itself, and the path dependent nature of this massive multi-billion dollar program.”⁸³

B. MAPPING

The Commission should direct providers to submit detailed information to state regulators to enable them to identify the regions that lack broadband service.

Rate Counsel urges the Commission to require supply-side reporting of broadband availability. As stated in initial comments: “The first task in extending broadband

⁸² / Others support the proposed Broadband Fund. *See, e.g.*, IURC, at 5.

⁸³ / CU et al., at 3.

facilities to all Americans is to determine what areas currently lack broadband.”⁸⁴ If the Commission adds broadband to the list of services supported by universal service, consistent with the recommendation of Rate Counsel and others, then policymakers require greater deployment detail from broadband suppliers. Broadband service providers already have the data necessary to determine where service is available on an address-by-address basis.⁸⁵ These data should be incorporated into a geographic information system (“GIS”) application that allows for neighborhood-by-neighborhood mapping of service availability.⁸⁶ Also, broadband availability mapping data should be segmented into residential and business components.

Rate Counsel also 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 support term, the grantees should be required to compare actual deployment with planned deployment.

Rate Counsel concurs with the comments that stress the need for mapping to ascertain the location of unserved and underserved broadband areas,⁸⁷ an effort that lends

⁸⁴ / Rate Counsel, at 21.

⁸⁵ / *Id.*, at 22, citing 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.

⁸⁶ / The mapping efforts conducted by the ConnectKentucky (now ConnectedNation) have received mixed reviews, 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. *See* Rate Counsel, at 22-24.

⁸⁷ / *See, e.g.*, Verizon and Verizon Wireless, at 27-28; NCTA, at 20 (stating that “no financial support should be provided under such a program until the Commission is able to identify such unserved areas”); CPUC, at 7-8 (recommending that states be charged with collecting relevant information, and citing to the California Digital Infrastructure and Video Competition Act of 2006, under which the CPUC collects annual data from state video franchise holders and their affiliates, as well as to the California Broadband Task Force, which conducted a mapping project using a third party to collect confidentially relevant data,

itself most logically to states, which typically oversee geographic information system (“GIS”) endeavors. As Rate Counsel described in its initial comments,⁸⁸ and as others observed, many states have already begun efforts to identify and to address broadband gaps.⁸⁹ State GIS, regulatory, and economic development agencies are better positioned than is the FCC to design and implement broadband programs. Rate Counsel concurs in part with the MACRUC States’ recommendation that the Commission “determine broadband availability before any determination...that support for broadband is even necessary.”⁹⁰ Comprehensive data and information are essential to target support where needed.⁹¹

CPUC raises a recommendation similar to that raised in Rate Counsel’s initial comments⁹² stating that the Commission should explicitly authorize California (and presumably other states) to collect relevant data “from all broadband providers (not just

then analyzed through GIS mapping techniques); US Telecom, at 36 (stating that an essential first step to broadband support (in any form) should be the identification of unserved areas); NASUCA (re Recommended Decision), at 20-21, stating that “[f]uture broadband goals will be difficult to establish until such time as the total number of unserved customers is quantified, along with available funding and estimated costs.”

⁸⁸ / Rate Counsel, at footnote 52.

⁸⁹ / See, e.g., Verizon and Verizon Wireless, at 29-30 (discussing California, Kentucky, Massachusetts, Ohio, and West Virginia).

⁹⁰ / MACRUC States, at 5.

⁹¹ / The FCC is examining ways to improve broadband data collection, in a separate but related docket. In March 2008, the FCC announced a notice of proposed rulemaking and order that it adopted but has not yet released. *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, Federal Communications News Release, “FCC Expands, Improves Broadband Data Collection,” March 19, 2008. Rate Counsel submitted initial and reply comments on June 15, 2007 and July 16, 2007, respectively, in WC Docket No. 07-38 and incorporates herein those comments by reference. Among other things, Rate Counsel urged “the Commission to share routinely with state public utility commissions and state consumer advocates any information that the Commission may collect and may deem confidential, subject to appropriate proprietary treatment” and further stated that [r]egular access to detailed data is critically important to states’ ability to fulfill their share of the dual responsibility of broadband oversight and achieving widespread broadband deployment.” WC Docket No. 07-38, Rate Counsel Initial Comments, at 6.

⁹² / Rate Counsel, at 22-23; 49.

those broadband providers subject to [its] regulatory authority.”⁹³ States’ access to detailed data regarding the location and speed of broadband deployment is essential to inform the efficient use of any broadband funds.

Qwest acknowledges that the zip code level of analysis for measuring broadband deployment is flawed but nonetheless proposes that it be used for the “first round” of grants given that it “might be the simplest administrative measure to use.”⁹⁴ Rate Counsel disagrees and urges the Commission to obtain data at a more granular level from the outset of the program. Experience thus far with universal service demonstrates that “second best” choices become entrenched in the regulatory apparatus, making rational implementation of an efficient system of support difficult, if not impossible. Rate Counsel urges the Commission to take the time now to work out important details of a broadband mapping program, rather than leaving them to the future.

Qwest also reasons that broadband providers will have an incentive to provide mapping data “to avoid the possibility of competing against a subsidized carrier,”⁹⁵ *i.e.*, a provider does not want its service area labeled as “unserved” because this would allow the entrance of subsidized competitors. Yet the Commission may lose valuable data if it simply relies upon the threat that a provider cannot compete for subsidies, the incentive identified by Qwest. The incentive identified by Qwest means that once one provider reports in an area, thus marking the area as “not unserved,” no other providers will provide data, which is vital to the task of determining the status of competition. Rather,

⁹³ / CPUC, at 8.

⁹⁴ / Ex Parte Letter from Ms. Melissa E. Newman, Qwest, to Ms. Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 96-45, July 7, 2007, Attachment: “Qwest Proposal for Broadband Deployment to Unserved Areas” (“Qwest Broadband Proposal”), at 15. Qwest cites its Broadband Proposal throughout its April 17, 2008 comments. *See, e.g.*, Qwest, at 3.

⁹⁵ / Qwest Broadband Proposal, at 16.

the Commission should compel *all* providers to furnish information regarding broadband build-out. Furthermore, the Commission should obtain information about the rates, types of consumers served, and the speed of service available in areas across the nation.

C. CONSTRUCTION IN UNSERVED AREAS

Broadband support should be limited to one-time costs and any broadband fund should have a sunset date that would require explicit FCC renewal to continue.

One of the fundamental flaws in the existing high cost fund is that it contains no roadmap for “declaring victory,” no test of success, and no method to discontinue support once success is achieved. Rate Counsel concurs with those recommending that broadband funds targeting unserved areas be used for one-time construction costs, and not for ongoing operation and maintenance expenses. NCTA recommends that if the Commission determines that additional funding for broadband is necessary, the additional support should be limited the construction of broadband networks in areas that today lack terrestrial broadband service,⁹⁶ and also that the Commission should establish safeguards for any new broadband (or mobility) funding.⁹⁷

Rate Counsel concurs with Verizon and Verizon Wireless that if the Commission decides to use USF subsidies to fund broadband deployment that “it should do so on a basis that limits the scope of the subsidy and avoids expectations of permanent government funding.”⁹⁸ However, Rate Counsel disagrees with Verizon and Verizon Wireless that the Commission and not the states should decide which companies receive

⁹⁶ / NCTA, at 3. See also TWTC, at 3, stating that subsidies for broadband and wireless should be limited to one-time construction costs.

⁹⁷ / NCTA, at 6.

⁹⁸ / Verizon and Verizon Wireless, at 34.

the grants.⁹⁹ Rate Counsel’s recommendation to distribute any broadband funding in proportion to states’ population¹⁰⁰ should address the concern that Verizon and Verizon Wireless raises about creating incentives for states to over-designate unserved areas. Rate Counsel also disagrees with Verizon and Verizon Wireless that any broadband funding should be capped at \$300 million.¹⁰¹ Instead, the amount of Commission-established funding should correspond with criteria such as the gaps that states document through mapping efforts and the magnitude of the subsidy that is necessary to render broadband profitable (that is, rather than subsidizing the entire cost of deployment, USF subsidies should only be used to support what is necessary to yield a positive business case). Rate Counsel joins CPUC in supporting the Joint Board’s recommendation that would allow states to administer the new Broadband Fund, based on state-specific guidelines and criteria on matters such as the determination of what constitutes “unserved” and “underserved” areas.¹⁰²

AT&T offers a plan to encourage further deployment of broadband.¹⁰³ As described by AT&T:

Under the new Broadband Incentive Fund, the Commission would immediately begin providing project-based funding for investment in infrastructure necessary to provide fixed location broadband internet access services in unserved areas. Using an auction-like application process, states and the Commission would combine their expertise to select a fixed location provider (wireline and fixed wireless) to deploy and offer the supported broadband Internet access service (e.g., up to 1.5 mbps downstream) for a specified period (e.g., seven years) . . . This new money would be

⁹⁹ / *Id.*

¹⁰⁰ / Rate Counsel, at 18, 30.

¹⁰¹ / Verizon and Verizon Wireless, at 34.

¹⁰² / CPUC, at 5-6.

¹⁰³ / AT&T, at 3.

supplemented by transitioning funding from the current high-cost mechanisms to the Broadband Incentive Fund.¹⁰⁴

AT&T predicts that demand for switched access will decline to close to zero, and that, therefore, it makes little sense to require or support stand-alone, fixed-location voice service: “The risk is that the growing subsidy needed to maintain narrowband voice networks will drain funds that might otherwise be available to promote broadband investment and deployment. The opportunity is that the declining viability of the POTS business model makes it feasible to provide a measured transition to the broadband business model.”¹⁰⁵ However, if the Commission, consistent with Rate Counsel’s recommendations, reforms the high cost fund, funds will be available to support broadband service.

CPUC supports a new and limited Broadband Fund to provide grants for constructing facilities in unserved areas, and further indicates that such an approach would be consistent with the California Advanced Services Fund, which the CPUC established in December 2007.¹⁰⁶ Rate Counsel urges the Commission to learn from programs such as the one that the CPUC has recently established.¹⁰⁷ Rate Counsel concurs with CPUC that federal funding for the operation and maintenance of broadband networks should be limited or non-existent,¹⁰⁸ with the important exception that *ongoing* support subsidize broadband rates for Lifeline participants.

¹⁰⁴ / *Id.*, at 4.

¹⁰⁵ / AT&T, at 8.

¹⁰⁶ / CPUC, at 4-5, citing CPUC Decision 07-12-054.

¹⁰⁷ / CPUC indicates that it anticipates initial proposals to be submitted in early June 2008. CPUC, at 5.

¹⁰⁸ / *Id.*, at 7.

Rate Counsel also supports NCTA’s recommendation that where an ILEC has already promised to deploy broadband service in high cost areas as part of regulatory approval of a transaction or deregulation, the federal HCF should not subsidize the ILEC’s broadband deployment. In initial comments, Rate Counsel discusses various examples of regulatory bartering that have occurred in state proceedings in which ILECs have obtained regulatory approval conditioned on broadband promises.¹⁰⁹

Aside from questioning whether broadband qualifies for support based on its designation as an information service, the Wyoming Office of Consumer Advocate (“Wyoming OCA”) also questions whether \$300 million per year is enough to close the broadband gap, or only “widen the chasm between the haves and the have-nots.” Furthermore, Wyoming OCA questions whether the unserved and underserved would be forced to contribute to a USF that covers broadband while they still wait for broadband service,¹¹⁰ a concern that Rate Counsel’s proposal should minimize. Rate Counsel reiterates its positions, however, that broadband can and should be included as a supported service, the recommended funding level is completely inadequate, and the timetable for ubiquitous deployment must be accelerated in order to prevent the “chasm” to which Wyoming OCA refers.

Other commenters echo Rate Counsel’s assertion that states are in the best position to understand their markets.¹¹¹ As Rate Counsel previously stated, its support for the Broadband Fund is contingent upon the fact that the fund is “carefully structured, has a clear sunset date, and is distributed proportionally to all states and jurisdictions

¹⁰⁹ / Rate Counsel, at footnote 23.

¹¹⁰ / Wyoming OCA (re Recommended Decision), at 11.

¹¹¹ / Rate Counsel, at 49; IURC, at 6-7 (indicating that states “can effectively target support to the areas that need it most”).

(based on population or households).¹¹² Furthermore, the Broadband Fund should only support one broadband service provider in a given geographic area.¹¹³

D. MINIMUM DOWNLOAD AND UPLOAD SPEEDS

The Commission should establish minimum download and upload speeds for any supported broadband service.

The term “broadband” has, until now, escaped several attempts to define its limits, and continues to be used to describe a wide range of connection speeds. Rate Counsel concurs with Independent Telephone & Telecommunications Alliance (“ITTA”) that the substantial increase in broadband subscription needs to be “tempered by the low speed at which ‘broadband’ is measured under current Commission standards”¹¹⁴ - subscription data overstates the status of broadband deployment because it captures all lines that exceed 200 kbps in at least one direction.¹¹⁵ CPUC indicates that it adopted a “3/1” standard, *i.e.*, a standard of 3 Mbps for download and 1 Mbps for upload, for evaluating proposals for the state’s broadband funding, and explained further that it “found compelling the arguments that a minimum upload speed of 1 Mbps is necessary for effective telecommuting.”¹¹⁶ In initial comments, Rate Counsel reiterated its “support for an updated definition of broadband (*e.g.*, a minimum of 1 Mbps downstream), as well as periodic revisions to the definition to correspond with evolving technology and

¹¹² / Rate Counsel, at 30.

¹¹³ / *Id.*, at 31.

¹¹⁴ / ITTA, at 24.

¹¹⁵ / See, *e.g.*, Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, *High-Speed Services for Internet Access: Status as of June 30, 2007*, March 2008, at footnote 4 and 2.

¹¹⁶ / CPUC, at 16. Proposals with higher speeds than the “3/1” are weighted more favorably and those with slower speeds could be funded, but are weighted less favorably. *Id.*, at 17.

consumer demand.”¹¹⁷ This recommendation was based on the Rate Counsel’s filing submitted in Docket No. 07-38, regarding the FCC’s broadband data collection.¹¹⁸ However, in light of numerous other commenters seeking an updated definition of “broadband,” and, in particular, CPUC’s analysis of the minimum requirements for effective telecommuting, Rate Counsel recommends that the Commission adopt the CPUC’s “3/1” minimum standards, and further recommends that the Commission periodically revisit these standards based on further innovation and advancements. Rate Counsel concurs with NASUCA that “[i]t is virtually impossible to move forward to quantify existing broadband availability until the FCC defines precisely the bandwidth and transmission speed that qualify as ‘broadband’ service.”¹¹⁹ Similarly, funds cannot be disbursed for broadband deployment until the FCC arrives at a definition of broadband.

E. BROADBAND ASSESSMENT

The Commission should assess broadband services a USF charge to support broadband deployment in unserved areas and to subsidize broadband rates for Lifeline participants.

In initial comments, Rate Counsel estimated that the three BOCs generate as much as \$18 billion annually in DSL revenues.¹²⁰ Because this preliminary analysis was limited to only the three BOCs, it significantly underestimated industry-wide broadband

¹¹⁷ / Rate Counsel, at 35-36.

¹¹⁸ / 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, Reply Comments of the New Jersey Division of Rate Counsel, July 16, 2007.

¹¹⁹ / NASUCA (re Recommended Decision), at 18. NASUCA does not make a specific recommendation for a defined speed but recommends that the Commission should establish minimums and ensure that the networks deployed have “the capability of meeting higher standards based on future needs.” *Id.*

¹²⁰ / Rate Counsel, at 30. See Table 5 showing an estimated range spanning \$5 billion to \$18 billion.

revenues. For example, based on the FCC's most recent high speed Internet access report, there are more cable modem service subscribers than DSL subscribers in the United States.¹²¹ Extending the analysis presented in intial comments to include those non-RBOCs providing DSL services, as well as companies providing cable-based access, Rate Counsel estimates that the industry-wide revenue from broadband was between \$12 billion and \$44 billion in 2007.¹²²

¹²¹ / See Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, *High-Speed Services for Internet Access: Status as of June 30, 2007*, March 2008, at Table 1, which shows approximately 27.5 million DSL subscribers and 34.4 million cable modem subscribers as of June 2007.

¹²² / The estimates span a wide range because consumers may pay a wide range of prices, which, in turn, affects the calculation of the total revenues. In Table 1, the "low" estimate corresponds with a range of monthly rates between \$12.99 and \$26.99, and the "high" estimate corresponds with a range of monthly rates between \$54.99 and \$64.99.

Table 1
Estimate of Broadband Revenues – 2007

| | Number of Connections | Estimated 2007 Revenues | |
|--------------|-----------------------|-------------------------|------------------|
| | | Low Estimate | High Estimate |
| RBOC DSL | 25,432,000 | \$4,897,088,160 | \$18,000,245,040 |
| Non-RBOC DSL | 2,084,171 | \$401,319,956 | \$1,475,133,246 |
| Cable | 34,408,553 | \$6,625,578,700 | \$24,353,664,103 |
| Total | 61,924,724 | \$11,923,986,816 | \$43,829,042,389 |

Note: This estimate of revenues from broadband extends earlier analysis of RBOC (AT&T, Verizon, and Qwest) broadband revenues. (See Rate Counsel Initial Comments at Table 5.) Using the results of the earlier analysis, the revenue per connection is applied to the non-RBOC DSL connections and the cable-modem connections, neither of which were included in the previous analysis. Total DSL and cable-modem connections are as reported by the FCC.

Sources: 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; FCC, High Speed Services for Internet Access: Status as of June 30, 2007, Table 1.

CPUC recommends that the Commission require all broadband service providers to contribute to the Broadband Fund, and further recommends that if the Commission requires states to provide matching funds, the Commission delegate authority to states to seek contributions.¹²³ NASUCA also proposes that broadband services be assessed, stating that “it is only reasonable that if broadband is to become a supported service, broadband should itself contribute to the fund.”¹²⁴

Rate Counsel recommends that the FCC assess a broadband USF surcharge on broadband providers for the specific and limited purposes of subsidizing (1) one-time

¹²³ / CPUC, at 9.

¹²⁴ / NASUCA (re Recommended Decision), at 12.

construction charges for deploying broadband in unserved areas and (2) broadband Lifeline support. A small surcharge, applied to such a large base of revenues, would assist the Commission in ensuring that all Americans have access to affordable broadband service. States should be required to provide matching funds.

F. RURAL HIGH COST SUPPORT AND BROADBAND

Explicit broadband support should be provided to urban and rural regions of the country where there is a demonstrated need, and implicit broadband support should be discontinued.

Another theme implicit in several carriers' comments is the link between the rural HCF and broadband deployment. ITTA asserts that a re-basing of the cap to "reflect current actual costs" is appropriate to accommodate growing "interest in broadband and advanced services that rely upon underlying incumbent networks."¹²⁵ Although Rate Counsel supports a ubiquitous nationwide broadband network, urban consumers should not subsidize rural carriers' broadband deployment while rural carriers' shareholders alone benefit from the broadband revenues. For those ILECs that are rate-of-return regulated, in computing the rate of return on their investment, the cost of the common network is included, but the broadband revenues (made possible by those costs) are excluded. The overall effect of the rural high cost program would appear to be to encourage investment supporting unregulated products, the cost of which is borne disproportionately by urban consumers.

Embarq considers a fund aimed at supporting providers of last resort as a priority over supporting broadband build-out.¹²⁶ Embarq asserts:

¹²⁵ / ITTA, at 20.

¹²⁶ / Embarq, at 4.

It is only through ILECs fulfilling their POLR obligations that broadband services and mobility services are (or can be made) available in high-cost, rural areas. The best way to promote broadband deployment in extreme rural areas is to adequately support the only underlying network that is ubiquitous in those areas, the POLR network.¹²⁷

While Embarq supports a broad-based program to encourage broadband deployment, it does not support an “unfunded mandate” that would result from the reverse auction process.¹²⁸

Contrary to Rate Counsel’s argument that \$300 million per year is insufficient for deploying broadband ubiquitously,¹²⁹ Embarq indicates that it “supports such an estimate, but takes exception with the suggestion made by the Joint Board that these funds ‘could be reassigned to the Broadband fund from legacy POLR programs’” and further states that “[t]he notion of reducing the existing POLR dollars to fund additional services is a clear step in the wrong direction.”¹³⁰

Windstream also appears to support “traditional” high cost support as a way to achieve broadband deployment. Windstream opposes a broadband fund, noting that the recommended support level is meager, the costs of provisioning broadband in rural areas are large, and basic voice service is a higher priority than broadband.¹³¹ However, Windstream’s purported need for high cost support is undermined, at least in part, by its

¹²⁷ / *Id.*, at 19.

¹²⁸ / *Id.*, at 5.

¹²⁹ / Rate Counsel, at 32-33.

¹³⁰ / Embarq, at 25-26.

¹³¹ / Windstream states: “Windstream – a company with approximately two percent of the nation’s ILEC access lines – alone could require more than \$300 million to deploy broadband to the rest of its customers.” Windstream estimates that the cost of reaching its 450,000 remaining access lines that now lack broadband would be between \$250 and \$400 million. Windstream, at 13. Windstream also projects that transport costs alone could reach \$20 per customer served per month in rural areas and that shortening loops to move DSLAMs closer to homes is another major cost of rural carriers such as Windstream. *Id.*, at 15-16.

recent financial performance. Windstream most recently had a 29% profit margin (defined as net income divided by operating revenue), and its most recent net income increased by 24% relative to the previous year.¹³² Rate Counsel is not persuaded by Windstream's assertion that reforming allocation of traditional support will make broadband more economic to provision in high-cost areas because dual-use plant will receive additional funding.¹³³ Reforming traditional high cost funding is indeed essential, but support for broadband should be limited to those situations where neither private investment nor other state initiatives will leave consumers without broadband access.

NASUCA states that a substantial amount of high cost support currently funds broadband investment and that the providers acknowledge this support.¹³⁴ Rate Counsel concurs with NASUCA's proposal, in opposition to Embarq and Windstream, that “[a]t the very least, those dollars should be cut from the high-cost herd and be allocated to the Broadband Fund.”¹³⁵

G. SUMMARY OF RECOMMENDATIONS

Rate Counsel reiterates its agreement with the Joint Board's recommendation that the nation's universal service goals should include the universal availability of broadband

¹³² / Windstream 2007 10-K, page F-5. In a recent press release, Windstream reported: “Net income was \$124 million, a 24 percent increase from a year ago. Average revenue per customer was \$82.52, an increase of 6 percent from a year ago. Windstream added almost 40,000 broadband customers during the quarter, bringing its total broadband customer base to approximately 911,000 – an increase of 22 percent year-over-year and a 29 percent penetration rate of total access lines. ‘We recently doubled broadband download speeds to offer 3-Mbps service to virtually all of our broadband customers and up to 12-Mbps service in certain areas. This upgrade increases our competitiveness and provides a platform to sell faster speeds and additional products and services, which is an important part of our strategy to transform this business to a broadband-centric model,’ Gardner said.” “Windstream reports higher revenue, cash flow in first quarter,” May 9, 2008 <http://www.windstream.com/about/NewsDetail.aspx?NewsID=81>

¹³³ / Windstream, at 3.

¹³⁴ / NASUCA (re Recommended Decision), at 19. *See, also,* US Telecom, at 35; Qwest Wire Center Proposal, at 3.

¹³⁵ / *Id.*

services.¹³⁶ 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. As these comments discuss above, there is broad support that the Commission:

- support the deployment of broadband service;
- implement detailed mapping to ensure that support is targeted where private investment would not otherwise occur;
- learn from mis-steps with the High Cost Fund in constructing the Broadband Fund; and
- explore, on a pilot basis, reverse auctions for the allocation of construction funds for broadband service.

Rate Counsel also continues to support audits and enforcement mechanisms to ensure that suppliers receiving broadband support are accountable for their use of funds,¹³⁷ and a fixed sunset date (subject to Commission extension if circumstances so warrant) to prevent any Broadband Fund from becoming an open-ended subsidy. Finally, assessing the billions of dollars in broadband revenues that industry generates to support broadband deployment to unserved areas and to subsidize broadband rates for Lifeline participants would address both the "distribution and contribution side of the ledger."¹³⁸

¹³⁶ / Rate Counsel, at 18, citing Recommended Decision, at para. 56.

¹³⁷ / *Id.*, at 31.

¹³⁸ / *Id.*, at 27, citing 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. *See, also*, detailed discussion of DSL revenues in Rate Counsel's initial comments, at 27-29.

V. MOBILITY

A mobility fund should be limited in scope, and should be focused on unserved areas.

Rate Counsel reiterates its position that any universal service support for mobility should be defined carefully, mobility support should be limited to a single carrier, and mobility funds should be used first to serve regions of the country that may lack any telephone service.¹³⁹ As stated in initial comments, the vast majority of households continue to rely on wireline service despite the explosive growth in demand for wireless service, suggesting that most consumers subscribe to wireless service *in addition to* and *not instead of* wireline service.

It is not evident that wireless deployment is slowing or that there is a significant problem with wireless supply. As noted in initial comments, 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.¹⁴⁰ Rate Counsel continues to believe that the Commission should not subsidize deployment that might occur *without* the subsidy. If the Commission decides to use USF monies to subsidize wireless deployment, it should 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.

Although access to at least one carrier is desirable, Rate Counsel recommends that the Commission define more explicitly how one would assess whether a "plausible economic case" can be made. For example, the wireless industry should be encouraged

¹³⁹ / Rate Counsel, at 36.

¹⁴⁰ / Smaller Towns Gaining The Attention Of Wireless Carriers Monday, February 11, 2008, <http://deadcellzones.blogspot.com/>

to submit specific recommended parameters that the Commission and states could use to assess the economic plausibility of serving areas. The Commission should work with states and funds should only be disbursed to one wireless carrier in any geographic area. As with the broadband fund, Rate Counsel agrees with the Joint Board recommendation that states prepare detailed maps (and wireless carriers provide necessary data) of wireless deployment.

Some oppose outright the establishment of a new separate Mobility Fund,¹⁴¹ while others support a limited Mobility Fund to support grants for the construction of wireless service in unserved areas.¹⁴² If the Commission establishes a separate mobility fund, Rate Counsel concurs with NCTA that the Commission should “implement mechanisms to ensure that support is provided only to the extent that it is absolutely necessary to provide services in areas where it otherwise would not be economical to provide affordable service.”¹⁴³

AT&T supports a separate wireless fund: “Recognizing the unique characteristics of wireless technologies, AT&T proposes a separate and distinct Advanced Mobility Fund that would immediately make project-based funding available for the deployment of wireless broadband and voice capabilities in unserved areas. Utilizing an application process similar to the Broadband Incentive Fund, wireless providers would be selected to provide the supported service for a specified period.”¹⁴⁴ Funding for AT&T’s Mobility

¹⁴¹ / See e.g., New Jersey Board, at 3; MACRUC States, at 8.

¹⁴² / CPUC at 10-11 (see page 11 for recommended parameters of such a fund); Verizon and Verizon Wireless at 3.

¹⁴³ / NCTA, at 19.

¹⁴⁴ / AT&T, at 5.

Fund would come from high cost support currently going to wireless CETCs, transitioning over a five year period.¹⁴⁵

Wireless support should be targeted to those few regions in the country where the cost of deploying wireless service is so high as to prevent private investment.¹⁴⁶ Rate Counsel further concurs with Verizon and Verizon Wireless that “the Commission should not seek to fully fund infrastructure build-out but should provide one-time grants that are sufficient to make building infrastructure in these unserved areas an attractive proposition.”¹⁴⁷ Rate Counsel recommends that the Commission consider the Verizon and Verizon Wireless proposal for a reverse auction¹⁴⁸ on a pilot basis. Furthermore, any pilot program should be scrutinized based on well-established criteria.

If the Commission adopts Rate Counsel’s recommendation to distribute any mobility funds proportionally, based on states’ population, states will not have an incentive to overstate their needs, thereby addressing Verizon and Verizon Wireless’ concern that states have the incentive to identify areas as unserved in an effort to obtain additional funding.¹⁴⁹ States and the Commission should collaborate to determine any unserved areas that may merit subsidy. Also, Verizon and Verizon Wireless’ opposition to the use of wireless subsidies to support “underserved” areas because it is difficult to

¹⁴⁵ / *Id.*, at 23.

¹⁴⁶ / See Verizon and Verizon Wireless at 9-10, citing to Commission data that shows that approximately 99.8 percent of the U.S. population has one or more different options for mobile service and that 95 percent of the U.S. population lives in areas with at least three wireless operators. *See, also*, New Jersey Board at 8.

¹⁴⁷ / Verizon and Verizon Wireless, at 10.

¹⁴⁸ / *Id.*, at 10-17.

¹⁴⁹ / *Id.*, at 14-15.

define or establish a test for determining underserved areas (*e.g.*, where reception may be poor) has merit.¹⁵⁰

Wyoming OCA asserts that the Mobility Fund should be used primarily for construction and only secondarily for on-going operation and maintenance costs.¹⁵¹

Wyoming OCA points out, however, that towers along isolated highways (a public safety consideration) may need subsidies for operational expenses, as there may not be enough calls to support fully the towers' costs.¹⁵² USFon emphatically rejects the permissibility of a separate Mobility Fund, arguing that a separate fund for mobility violates the technological neutrality principle of universal service.¹⁵³

While supporting reverse auctions, US Telecom also proposes that the Commission earmark a portion of the savings that accrue from capping identical support and eliminating the portion of support related to access, to be put toward “project-based support to extend mobile service to unserved areas.”¹⁵⁴ Tellingly, US Telecom suggests in a footnote that a “significant portion” of those same savings should be directed to support for ILECs serving high cost wire centers,¹⁵⁵ a proposal that would bolster ILECs’ position inappropriately at the expense of its competitors and consumers. It is unclear whether US Telecom envisions the project-oriented funding to be instead of, or in addition to, reverse auctions or how such a transition would occur. However, US

¹⁵⁰ / *Id.*, at 15-16.

¹⁵¹ / Wyoming OCA (re Recommended Decision), at 8.

¹⁵² / *Id.*

¹⁵³ / USFon, at 4.

¹⁵⁴ / US Telecom, at 23.

¹⁵⁵ / *Id.*, at footnote 36.

Telecom proposes the “vast bulk” of high cost funding to mobile wireless carriers should “eventually” be in the form of project-based support.¹⁵⁶

Rate Counsel reiterates the concerns it expressed in initial comments:

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.¹⁵⁷

VI. OTHER HIGH-COST REFORM ISSUES AND PROPOSALS

A. PHASING OUT HIGH COST SUPPORT

High cost reform should begin with immediate elimination of high-cost support to price cap carriers and a gradual phasing out of support to non price cap and rural carriers over a five-year period.

Rate Counsel concurs with Verizon and Verizon Wireless that the Commission should cap high cost support to ILECs and take steps to reduce existing subsidy levels.¹⁵⁸ Also, the Commission should reject proposals such as those submitted by Sprint Nextel, which would, rather than tackling the root cause of HCF growth, simply shift the fund to higher subscriber line charges.¹⁵⁹ Rate Counsel also concurs with the MACRUC States that “[b]efore the FCC considers a new high-cost structure, it *must* revise the fatally

¹⁵⁶ / *Id.*, at 23-24.

¹⁵⁷ / Rate Counsel, at 41.

¹⁵⁸ / Verizon and Verizon Wireless, at 4-8. *See, also*, New Jersey Board at 4 (asserting that the fund “must be reduced”).

¹⁵⁹ / *See* discussion of the Sprint Nextel proposal in Section IX, *infra*.

flawed allocation of funds to make it more equitable to states like those in the MACRUC region.”¹⁶⁰ Rate Counsel urges the Commission to consider carefully the need for high cost support – although it may seem easier to subsidize ILECs indefinitely than to phase out such subsidies, consumers ultimately pay for USF support. ILECs should be required to demonstrate that support is necessary and states should be required to demonstrate that they have not only provided matching subsidies, but also have addressed rate design issues where rates are regulated.¹⁶¹

The Commission should discontinue high cost support for price cap carriers.

In its filing opposing AT&T’s acquisition of BellSouth, Rate Counsel recommended that any Commission approval of the merger be conditioned on, among other things, the sunset of high cost funds for AT&T.¹⁶² Consistent with this recommendation, and with its initial comments in this proceeding, Rate Counsel recommends that the Commission eliminate any high cost support to AT&T, Qwest, and Verizon and to other large price cap carriers.

¹⁶⁰ / MACRUC States, at 7 (emphasis in original).

¹⁶¹ / In its oversight of the state’s high cost fund, the Public Utilities Commission of Texas in 2007 opened a proceeding reexamining which lines are eligible for high cost support and the appropriate benchmarks for determining monthly support per line in the service areas of Texas’ four Texas High Cost Universal Service Plan (“THCUSP”) ILECs. This investigation came in response to claims from competitive carriers and cable companies that Texas’ large incumbents were claiming excessive high cost support. On April 25, 2008, the Commission approved a settlement agreement supported by all participating parties. The settlement reduces, over a four-year phase-in period, the THCUSP by \$144.35 million per year, a reduction of 36.5%. This represents a 25% reduction of the total Texas USF. The stipulation also specifies that after January 1, 2009, exchanges with population greater than 30,000 will no longer be eligible for high cost support if they have been deregulated. Petition for Review of Monthly per Line Support Amounts from the Texas High Cost Universal Service Plan Pursuant to PURA § 56.031 and PUC. Subst. R. 26.403, TX PUC Docket No. 34723, Order, April 25, 2008.

¹⁶² / *In the Matter of AT&T Inc. and BellSouth Corporation Applications for Approval of Transfer of Control*, FCC WC Docket No. 06-74, Comments on behalf of the New Jersey Division of the Ratepayer Advocate, June 5, 2006, at 22; Declaration of Susan M. Baldwin and Sarah M. Bosley on behalf of the New Jersey Division of the Ratepayer Advocate, June 5, 2006, at para. 195. See, also, *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, Reply Comments of the New Jersey Division of the Ratepayer Advocate, May 26, 2006 Reply Comments, at 3.

Rate Counsel recognizes that Qwest's size and territory differs from those of AT&T and Verizon. In support of its targeted wire center-based proposal for support for non-rural carriers, Qwest proposed that Verizon and AT&T need not be included in the plan and therefore would not qualify for additional support (thus reducing the estimated price tag for Qwest's proposal from \$1.2 billion to \$322 million).¹⁶³ Qwest defends such an approach in the following manner:

By any measure, each of the medium-size ILECs is only a fraction the size of AT&T and Verizon, and lacks the economies of scale of the larger companies. The medium-size ILECs also lack the access to capital enjoyed by AT&T and Verizon. Indeed, both of the larger companies have invested billions of dollars in aggressive roll-outs of new fiber networks designed to compete with cable companies and retain customers, and recently committed billions more on new wireless spectrum. These investments, coupled with their ownership of the largest wireless providers, provide AT&T and Verizon a scope unlike that enjoyed by any of the medium-size ILECs.¹⁶⁴

Qwest uses market capitalization as a measure of comparison and states that Qwest is only 8 percent the size of Verizon and less than 4 percent the size of AT&T.¹⁶⁵ Although acknowledging Qwest's small size relative to the other two BOCs, Rate Counsel opposes Qwest's proposal for a wire center-based assessment for high cost support, as is discussed in Section VI. Furthermore, unless Qwest provides compelling information to demonstrate otherwise, the Commission should assume that Qwest does not require high cost support in order to maintain reasonably comparable urban and rural rates.

The telecommunications industry has evolved significantly since Congress passed the 1996 Act. BOCs' mergers (from which the BOCs predicted substantial synergies), their use of consumer-funded common networks for unregulated services (which, in turn,

¹⁶³ / Qwest Wire Center Proposal, at 4-5.

¹⁶⁴ / *Id.*, at 5.

¹⁶⁵ / *Id.*, at footnote 16.

yield billions of dollars for shareholders),¹⁶⁶ and their successful pursuit of deregulation in numerous state proceedings provide ample evidence that high cost subsidies are no longer needed. As these and other comments demonstrate, it is no longer necessary (indeed, if it was ever necessary) to bolster BOC revenues with high cost support in order to translate implicit support into explicit support, nor have the BOCs demonstrated that subsidies are necessary in order to achieve the goals of the 1996 Act.

Time Warner Telecom Inc. (“TWTC”) addressed only non-rural USF in its comments.¹⁶⁷ Among the diverse points raised in TWTC’s comments are the following:

- Subsidies should not be provided to services that have been rate deregulated because carriers will set the rates for such services based on factors such as demand elasticity, and carriers’ profit-maximizing incentives: therefore subsidies would not affect affordability.¹⁶⁸
- Legacy networks are largely depreciated and paid for; as carriers replace them they are deploying next-generation broadband networks which offer new higher revenue opportunities.¹⁶⁹
- The FCC should discontinue its use of “its outdated cost model” and instead provide “targeted support for modern facilities.”¹⁷⁰

Rate Counsel concurs with TWTC’s observation that when all of a non-rural ILEC’s revenues are considered, it is unlikely that the ILEC requires support to offer affordable service.¹⁷¹

¹⁶⁶ / TWTC echoes Rate Counsel’s concern about the fact that Internet access relies on common loop and generates substantial revenues. TWTC, at 7; Rate Counsel, at footnote 58, citing 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.

¹⁶⁷ / TWTC, at 1, fn 2.

¹⁶⁸ / *Id.*, at 2, 5.

¹⁶⁹ / *Id.*, at 2.

¹⁷⁰ / *Id.*, at 3.

¹⁷¹ / *Id.*, at 4. See Rate Counsel, at 30, Table 5 (regarding estimates of broadband revenues).

As Rate Counsel indicated in its initial comments, \$347 million in non-rural high cost loop payments were made in 2007.¹⁷² This amount does not include other forms of high cost, which Table 2 summarizes below, and which also should be phased out for price cap ILECs.

Table 2¹⁷³

High Cost Support to BOCs Should Be Eliminated: 2007 Support

| Rural Support | AT&T | Qwest | Verizon | BOC Total |
|--------------------------------|----------------------|---------------------|----------------------|----------------------|
| Interstate Common Line Support | \$0 | \$0 | \$0 | \$0 |
| High Cost Loop Support | \$0 | \$0 | \$2,279,442 | \$2,279,442 |
| Local Switching Support | \$0 | \$541,296 | \$6,149,076 | \$6,690,372 |
| Total | \$0 | \$541,296 | \$8,428,518 | \$8,969,814 |
| Non-Rural Support | AT&T | Qwest | Verizon | BOC Total |
| Interstate Access Support | \$97,756,500 | \$50,525,844 | \$206,879,607 | \$355,161,951 |
| High Cost Model Support | \$119,197,010 | \$27,136,004 | \$31,303,101 | \$177,636,115 |
| Total | \$216,953,510 | \$77,661,848 | \$238,182,708 | \$532,798,066 |
| Total High Cost Support | \$216,953,510 | \$78,203,144 | \$246,611,226 | \$541,767,880 |

Rate Counsel's analysis above focuses primarily on the BOCs, but Rate Counsel also questions the ongoing need for high cost support to other price cap ILECs.

The Commission should begin a five-year phase-out of high cost support for rural carriers.

ITTA, which includes as members mid-size local exchange carriers that serve 26 million customers in 44 states,¹⁷⁴ contends that "every effort should be made to avoid

¹⁷² / Rate Counsel, at 7, 43-44, citing Federal-State Joint Board on Universal Service, Universal Service Monitoring Report 2007 (Data Received through June 2007) (2007 Monitoring Report), at Table 3.9.

¹⁷³ / Federal-State Joint Board on Universal Service, Universal Service Monitoring Report, 2007, Data Received through June 2007, Tables 22-29. High Cost Loop and Local Switching Support are targeted to rural carriers; Interstate Common Line Support is geared to "mostly rural and some non-rural carriers." High Cost Model Support is for non-rural carrier, while Interstate Access Support is for "mostly non-rural and some rural carriers." See <http://www.usac.org/hc/competitive-carriers/step01/>.

disruption of sound policy programs.”¹⁷⁵ According to ITTA, “[c]ost-based programs have enabled successful investment and network deployment.”¹⁷⁶ ITTA contends:

- The “existing Federal regulatory framework has generally functioned well for many rural ILECs to ensure that reasonable rates can be maintained for consumers in areas with high costs and low population density;”¹⁷⁷ and
- “[T]he infusion of external, *i.e.*, non-customer-derived, support is necessary to ensure network deployment and maintenance.”¹⁷⁸

ITTA further asserts that “USF is a remarkably cost-efficient program,” stating:

USF for incumbent rural wireline carriers supports only costs that have been incurred and accounted for under regulatory scrutiny. The program boasts built-in accountability, as costs must be supported by the audited financials of the entity incurring the costs and are reconciled to all other regulatory reported costs through the elaborate and effective control mechanisms implemented by the National Exchange Carrier Association (NECA), the Universal Service Administration Company (USAC), and often state commissions.¹⁷⁹

Rate Counsel disagrees with ITTA’s recommendation that the Commission reject the Joint Board’s proposed imposition of an overall cap on high-cost funding.¹⁸⁰ ITTA opposes a cap because it would be “a ‘top down’ approach that does not accommodate actual needs or costs,”¹⁸¹ “would eviscerate rate-of-return regulation by failing to assure

¹⁷⁴ / ITTA, at 1.

¹⁷⁵ / *Id.*, at 3.

¹⁷⁶ / *Id.*

¹⁷⁷ / *Id.*, at 5.

¹⁷⁸ / *Id.*, citing Robert Cohen, Mark W. McNulty, Robert F. Wescott, “Consumers at Risk: The Impact of Reduced Universal Service Fund Support on Telephone Service Affordability in Rural America,” Keybridge Research LLC, Washington, DC, October 2007.

¹⁷⁹ / *Id.*, at 6; see also pages 10-11 (discussing regulatory and accounting safeguards).

¹⁸⁰ / *Id.*, at 18, citing Joint Board NPRM, at para. 26.

¹⁸¹ / *Id.*, at 18.

carriers their authorized rate of return,”¹⁸² and would “fail to contemplate evolving needs in a dynamic environment.”¹⁸³ Rate Counsel is not persuaded by ITTA’s reasoning. The “evolving needs” typically concern carriers’ costs for deploying advanced (and therefore unregulated) services, the cost of which should not be transferred to consumers.¹⁸⁴

Rate Counsel recommends that the Commission begin a five-year phase-out of rural high cost support because the open-ended subsidy has not been demonstrated to be essential to achieve national universal service goals. At a minimum, any carrier that receives federal high cost should be disqualified unless states provide matching funds for such support. It is far easier to over-subsidize carriers in the name of universal service than it is to subject the subsidies to scrutiny to ensure that they are indeed essential.

ITTA also raises a concern about the way in which rural high cost loop support is computed that merits attention:

The current caps on incumbent high-cost support cause unintended consequences. Currently, high-cost loop support (HCLS) for incumbent rural carriers is provided where the average line costs in a study area are more than 115 percent of the National average cost per loop (NACPL). The total amount of HCLS available to all carriers is capped, and adjusted annually by the Rural Growth Factor. Upward adjustment in the NACPL however, can have the effect of eliminating some carriers from eligibility for support, since the threshold of “greater than 115 percent of the NACPL” consequently increases. From 2002 to 2006, the “115 percent of NACPL” threshold rose from \$295.08 to \$407.59. Accordingly, if a carrier’s cost-per-line did not increase nine and one-half percent annually during those years (or 38 percent over the five years), it lost support. Moreover, since the Rural Growth Factor can take the form of a negative number, the total amount of HCLS to rural LECs can decrease. This is particularly potentially damaging since not all carrier costs are directly proportional to the number of loops

¹⁸² / *Id.*

¹⁸³ / *Id.*, at 20.

¹⁸⁴ / Except in the case of an explicit and separate broadband deployment program.

served.¹⁸⁵

Rate Counsel questions the efficiency of a system that appears to “reward” high costs – that is, the higher a carrier’s costs, the greater chance it is above the national average. In this sense, Rate Counsel echoes ITTA’s concern that the current method could exclude carriers from support,¹⁸⁶ but does not necessarily concur that the solution is to re-base the cap. Re-basing the cap could result in the inclusion of carriers that more successfully and prudently limit their costs (which, all else being equal, would appear to give the proper economic signal), but would not address the need to stem support for unbridled growth in costs by other carriers.

Also, as competitors enter new areas, competitive pressures should drive down the cost of service, and therefore reduce the need for high cost support.¹⁸⁷ As NCTA explains, “[m]arket forces are not static”¹⁸⁸ and, for example, the transition to IP-based equipment and services has enabled competitive entry by cable operators where it had not previously been profitable.¹⁸⁹ As facilities-based competitors enter local voice and non-voice markets, high-cost support should become less necessary.¹⁹⁰ The USF should not shield rural ILECs from the effect of competition.¹⁹¹ NCTA recommends that the Commission cap per-line support for all providers that serve a particular geographic area to recognize that technological advances reduce the cost of providing service and that the

¹⁸⁵ / ITTA, at 19.

¹⁸⁶ / *Id.*, at 20.

¹⁸⁷ / National Cable & Telecommunications Association (“NCTA”), at 2-3.

¹⁸⁸ / NCTA, at 4.

¹⁸⁹ / *Id.*

¹⁹⁰ / *Id.*

¹⁹¹ / *Id.*, at 13.

USF should not shield rural ILECs from the effect of competition.¹⁹² The Commission's recent order aptly states, "We are not persuaded ... that the Act requires the promotion of competition in high-cost areas through the provision of equal per-line support amounts to all carriers. Rather than requiring the use of universal service support to subsidize competition, the court in Alenco was concerned with the sustainability of universal service in a competitive environment."¹⁹³

Verizon and Verizon Wireless proposes that (1) carriers consolidate all study areas commonly owned within a state; (2) all carriers serving rural areas with 100,000 lines or more within a state receive universal service support under the non-rural support mechanism; and (3) the FCC freeze per-line support for all carriers at current levels.¹⁹⁴ This proposal merits consideration by the Commission. Verizon and Verizon Wireless opposes the implementation of a new POLR because it would require substantial resources and costs associated with the time necessary to create new rules.¹⁹⁵

ITTA cites to a report which purportedly demonstrates the importance of the rural high cost fund to keep "America connected."¹⁹⁶ Rate Counsel, of course, supports

¹⁹² / *Id.*

¹⁹³ / CETC Cap Order, at para. 15.

¹⁹⁴ / Verizon and Verizon Wireless, at 4.

¹⁹⁵ / *Id.*, at 22.

¹⁹⁶ / See, e.g., ITTA, at 5, citing "Consumers At Risk: The Impact of Reduced Universal Service Fund Support on Telephone Service Affordability in Rural America, An Analysis for the Coalition to Keep America Connected," Dr. Robert F. Wescott, Dr. Robert Cohen, and Mark McNulty, Keybridge Research LLC, October 1 2007 ("Keybridge Report"). The Coalition to Keep America Connected is touted as a "broad coalition of school teachers, doctors, entrepreneurs, farmers, small business owners, grandmothers, communications and high-tech industry leaders, civic groups and organizations, and many others." However, the organization's website notes that: "The Coalition to Keep America Connected effort is organized by The Independent Telephone & Telecommunications Alliance, National Telecommunications Cooperative Association, Organization for the Promotion and Advancement of Small Telecommunications Companies and the Western Telecommunications Alliance, whose memberships include more than 700 small and midsize communications companies." See <http://www.keepamericaconnected.org/page.cfm/id/3>. The "founding members" of the organization are The Independent Telephone & Telecommunications Alliance, National Telecommunications Cooperative Association, Organization for the Promotion and

reasonable efforts to ensure that all Americans are connected to the telephone network, but urges the Commission to recognize that, ultimately, consumers pay the price for universal service support.

In some ways, the report that ITTA cites illustrates the possible inefficiency of the existing rural high cost fund. The report analyzes USF data in 1,311 rural regional program study areas and estimates that 2.7 million households “might be at risk of losing access to affordable telephone service if HCP [high cost fund] support to telephone service providers is eliminated.”¹⁹⁷ The report further breaks down the households at risk into three categories: 45.4% at “moderate risk”; 18.1% at “high risk”; and 36.5% at “severe risk.” Setting aside the households at “moderate risk,” this classification of households, which is based on their estimated elasticity of demand for telephone service (that is, an assessment of whether, in the face of a rate increase, the consumers will terminate their telephone service) and their household incomes,¹⁹⁸ translates into approximately 1.5 million households purportedly at high or severe risk of losing access if high cost support is eliminated.

The report asserts that the purpose of the 1996 Act was to ensure that prices charged and services available to high-cost areas “would be comparable” to the prices charged and the services available in urban areas.¹⁹⁹ The Act requires that rates be “reasonably comparable.”²⁰⁰ Reasonable comparability does not require rates to be

Advancement of Small Telecommunications Companies and the Western Telecommunications Alliance. See <http://www.keepamericaconnected.org/page.cfm/id/121>.

¹⁹⁷ / Keybridge Report, at i, 1.

¹⁹⁸ / *Id.*, at 1-2.

¹⁹⁹ / *Id.*, at 2.

²⁰⁰ / 47 U.S.C. §254(b)(3), emphasis added.

identical, and, indeed, as Rate Counsel has explained in other filings, a range of rates is inevitable.²⁰¹

The Keybridge Report asserts that if high cost support were eliminated, carriers' rates of return would not be sufficient to attract capital unless carriers raised their rates.²⁰²

As a consequence of losing high cost support, the report asserts, the rural carriers "would be expected to pass along the cost of lost USF support to consumers"²⁰³ through higher rates. However, the report lacks any discussion whatsoever of *existing* rates, nor does it include any comparison of existing rural rates with the corresponding urban rates in the relevant jurisdictions. It may be possible for carriers to raise rates some and still maintain reasonably comparable rates: the study is silent on this critically important detail. The report fails to address whether *less* high cost support would suffice, and therefore more efficiently achieve the goal of reasonable comparability among rural and urban regions.

The report is also silent on whether any of the states have established high cost funds; if states were concerned about rural carriers' ability to earn reasonable rates of return, high cost funds could be established to complement federal funds. In any event, surely there is a more efficient way to yield reasonably comparable rates for these 1.5 million households that are at "high" and "severe" risk of losing access to the network.

²⁰¹ / In the Matter of High-Cost Universal Service Support, FCC WC Docket No. 05-337; Federal-State Joint Board on Universal Service, FCC CC Docket No. 96-45, Comments of the New Jersey Division of the Ratepayer Advocate, March 27, 2006, at 15-16, stating, in part: "Variances in rates within states and among states are inevitable: the wide array of state decisions about rate design necessarily will yield rate variations within state boundaries and across state boundaries. Where, for reasons beyond their control (mountains, sparsely populated areas, rocky terrain, etc.), states experience above-average costs, the non-rural high cost fund can contribute to the goal of reasonably comparable rates. However, as long as intrastate rates are set by state public utility commissions, and not by the FCC, it would be unfair to the net contributors to any high cost fund to support (or second-guess) the specific rate-making decisions of other states."

²⁰² / Keybridge Report, at 1-2.

²⁰³ / *Id.*, at 2.

By way of illustration, the \$2.7 billion provided in high cost support that the Keybridge Report examines, divided among the 1.5 million households purportedly at high or severe risk of being disconnected would yield a *monthly* subsidy of \$150 per household, presumably far in excess of what would be needed to yield reasonably comparable rates.

Furthermore, affordability should be examined separately from “reasonable comparability.” If, and as necessary, the Commission could consider a rural Lifeline program with the specific purpose of subsidizing rural rates for low income households, setting an income threshold that is more inclusive than that now used for Lifeline, and where state commissions certify that rural rates exceed urban ones by a pre-determined ratio. Rate Counsel supports subsidizing consumers’ rates, particularly where income constraints and/or high rates so warrant. Endlessly subsidizing carriers, however, is not an efficient way to achieve affordable and reasonably comparable rates. As Rate Counsel has stated previously²⁰⁴, the increasing fund (and thus USF fees on consumer bills) can indeed impact affordability of basic services.²⁰⁵ 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).”²⁰⁶

Recognizing the importance of affordable access throughout the country at comparable rates, Rate Counsel nonetheless urges the Commission to:

- Consider whether the goal of comparable rates can be achieved more efficiently and with a lower HCF.
- Address the issue of “comparability,” as is required by the *Qwest II* remand.

²⁰⁴ / Rate Counsel 2006 USF Initial Comments, at 12-13.

²⁰⁵ / 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 fees.

²⁰⁶ / *Qwest II*, at 1234, citing *Qwest I*, 259 F.3d, at 1200.

- Address the continuing need for rural HCF: is there a point at which sufficient support has been provided to deploy networks in rural areas that funding can be reduced. Since the lion's share of providing basic loop service is attributable to high fixed costs, the need for rural HCF should gradually diminish.²⁰⁷

B. WIRE CENTER PROPOSAL

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

The ILECs' proposals and Joint Board consideration of distributing high cost support on a wire center basis would, as the Joint Board acknowledges, "neglect the economies of scale and scope inherent in non-rural LEC networks."²⁰⁸ Such an approach would increase high-cost support significantly and unnecessarily. 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, as shown in Rate Counsel's initial comments.²⁰⁹

US Telecom and others continue to campaign for high-cost support targeted at (or even below) the wire center level.²¹⁰ The arguments cited for such support (including the Joint Board's observation that competitors compete in densely populated areas that are lower cost to serve) have been widely panned by ILECs in federal and state proceedings examining competition. Indeed, the ILECs have argued that statewide analyses are

²⁰⁷ / See ITTA, at 15, stating: The fixed costs associated with the deploying [of] telecommunications are generally high in comparison to the incremental (marginal) costs" and also referring to the construction of facilities. See also TWTC, at 14 stating that "the vast majority of costs incurred by telecommunications carriers are the one-time, sunk costs associated with network deployment and the incremental costs of providing services are relatively low."

²⁰⁸ / Recommended Decision, at para. 41.

²⁰⁹ / See Rate Counsel, at 47-48.

²¹⁰ / US Telecom, at 29.

adequate. In seeming contradiction to the concern it expresses about the time and burden for wireless carriers to prepare cost studies,²¹¹ US Telecom supports an initiative by the Commission to: “commence a study to collect population density data from companies choosing to submit such data for study purposes, select a suitable model for estimating the cost of service, and then identify the high cost areas in need of additional support.”²¹²

The ILECs’ assertions that the fund currently does not provide “adequate” support in high cost wire centers is unsubstantiated and therefore should be dismissed.²¹³ US Telecom argues that “excessive levels of funds are being provided to competitive ETCs,” yet asserts that “[h]igh cost wire centers within large study areas may receive an insufficient amount of support due to study area averaging.”²¹⁴ ITTA asserts that serving low-cost areas does not help to cover a carrier’s cost of deploying services in high-cost areas because, according to ITTA, the competition in the low-cost areas forces prices to cover these lower costs, and, “[t]herefore, there is no margin with which to cover the higher costs in other areas.”²¹⁵ Rate Counsel disagrees that the ILECs need additional support for high-cost areas. The ILECs consistently overstate the level of competition that exist, and provide no evidence that rates “just cover costs” in low cost areas.²¹⁶

Qwest submitted an *ex parte* filing on May 5, 2008 that purports to provide a plan to revise the high-cost universal support funding mechanism for non-rural carriers in a

²¹¹ / *Id.*, at 18.

²¹² / *Id.*, at 30-31. US Telecom is proposing that any duplicative funding to mobile CETCs and funding currently used to support the identical support rule can simply be redirected to the coffers of ILECs in high cost areas. In addition, those redirected funds may need supplementation, but according to US Telecom, the additional needs would be “modest.” *Id.*, at 7.

²¹³ / See, e.g., US Telecom, at 5; ITTA, at 17; Qwest Wire Center Proposal, at 3.

²¹⁴ / US Telecom, at 3.

²¹⁵ / ITTA, at 17.

²¹⁶ / See, e.g., NASUCA (re Recommended Decision), at 46 (providing evidence regarding statewide costs).

manner that complies with *Qwest II*.²¹⁷ Qwest contends that “vigorous competition throughout the country, and particularly in rural areas, has substantially eliminated the implicit subsidies that underlie the Commission’s current high-cost support rules for non-rural ILECs.”²¹⁸ Thus, Qwest further asserts, non-rural ILECs are unable to provide services in rural areas at reasonably comparable rates (as those in urban areas).²¹⁹ Finally, Qwest suggests that it cannot possibly deploy broadband to its rural areas without “additional federal assistance.”²²⁰ Qwest proposes to solve these problems by having the FCC provide even more high-cost funds to non-rural carriers (to be targeted to rural areas).²²¹ To that end, the Qwest proposal would replace the current non-rural high-cost support mechanism with “support targeted to the high cost wire centers served by the non-rural ILECs.” The targeted support would be calculated by reducing the current Commission “rate comparability” benchmark to 125 percent of the national average urban rate.²²² Qwest estimates that its proposal would increase non-rural high cost support by \$1.2 billion (assuming that CETC support is frozen in those areas).²²³ Qwest, in an apparent effort to soften the financial impact of its proposal, suggests that the Commission could “on an interim basis” just target support to smaller non-rural ILECs

²¹⁷ / Qwest Wire Center Proposal.

²¹⁸ / *Id.*, at 3.

²¹⁹ / *Id.*

²²⁰ / *Id.*

²²¹ / *Id.*

²²² / *Id.*, at 4.

²²³ / *Id.* Furthermore, Qwest’s proposal is that this particular support would not be subject to any cap that the Commission ultimately adopts. *Id.*

(or medium-size ILECs) because, purportedly, they have been the most affected by competition.²²⁴

Rate Counsel opposes Qwest's Wire Center Proposal for several reasons. First, as discussed in initial comments and above, "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."²²⁵ Despite Qwest's assertions to the contrary, "vigorous competition throughout the country"²²⁶ has not materialized and the non-rural ILECs are benefiting from a high cost windfall (created to replace 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 Qwest or other ILECs lowering local exchange rates as a result of receiving high cost support. Qwest's arguments for additional support make no sense if the competition is as "geographically ubiquitous and long-lived" as Qwest suggests.²²⁷ Presumably, if competition existed everywhere, the nation would not need to provide high-cost funds at all!

As the Joint Board observes, the Commission has not acted on the remand that it received in 2005.²²⁸ Rate Counsel has addressed the determination of comparable urban and rural rates in other pleadings. This unresolved issue bears directly on the issues

²²⁴ / Qwest Wire Center Proposal, at 4. Qwest calculates that, by excluding AT&T and Verizon (the large ILECs), the cost of the new targeting would be \$322 million of which \$200 million would go to Qwest. *Id.*, at 5.

²²⁵ / Rate Counsel, at 43.

²²⁶ / Letter from R. Steven Davis, Senior Vice President – Public Policy and Shirley Bloomfield, Senior Vice President- Federal Relations, Qwest, to Ms. Marlene H. Dortch, Secretary, Federal Communications Commission, May 5, 2008, at 2.

²²⁷ / Qwest Wire Center Proposal, at 13.

²²⁸ / Recommended Decision, at para. 33.

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.²²⁹

The Commission should reject ILEC attempts to increase the amount of funds they receive and their attempt to justify high-cost funding to non-rural carriers as a means of expanding broadband deployment.²³⁰ US Telecom suggests that all of the necessary reforms to the Universal Service program “should require not greater than a modest increase over today’s amount.”²³¹ US Telecom would have the Commission rely on the “enhanced targeting” of support at the wire center (or even more granular) level to “encourage investment in joint use facilities.”²³² The ILECs arguments are not persuasive, and Rate Counsel reiterates its observation that:

The result [of determining non-rural support on a wire center or sub-wire center basis] 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 the ILECs, 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

²²⁹ / Rate Counsel, at 46, citing Rate Counsel USF 2006 Initial Comments, at 36.

²³⁰ / Rate Counsel recognizes, as does AARP, that broadband and voice services are often provided by the same carrier and over the same loop. However, carriers must be accountable for the funds they receive. AARP interestingly suggests that if universal service monies have been given to carriers and those carriers have not yet deployed broadband “it is incumbent upon the FCC to determine why that is.” AARP – Joint Board Recommended Decision, at 50. Rate Counsel agrees with AARP that broadband support should be made explicit. *Id.*, at 52. Rate Counsel does not endorse AARP’s proposal, at this time, however. Further review is required.

²³¹ / US Telecom, at 7. US Telecom’s support for limiting the size of the fund seems particularly self-serving when US Telecom states that “[a]ny limitations in the size of the high cost fund should allow for increases in fund size if necessary as a result of intercarrier compensation reform.” *Id.*, at 8.

²³² / US Telecom, at 35; Qwest Wire Center Proposal, at 3.

of the high cost fund would be substantial, and is not necessary to achieve universal service goals.²³³

NASUCA similarly expresses support for the continuation of statewide cost-averaging for large non-rural carriers.²³⁴ In summary, Rate Counsel urges the Commission to reject industry proposals to distribute high cost support at a wire center level because such proposals would inflate unnecessarily the USF burden on consumers and because carriers have not demonstrated that the proposal are necessary to enable ILECs to compete efficiently.

C. 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.”²³⁵ Rate Counsel reiterates its support for periodic audits of universal service funds.²³⁶

The Mobility and Broadband Funds should sunset.

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.”²³⁷

²³³ / Rate Counsel, at 48.

²³⁴ / NASUCA (re Recommended Decision), at 41.

²³⁵ / Recommended Decision, at para. 49.

²³⁶ / Rate Counsel, at 50-51.

²³⁷ / Recommended Decision, at para. 38.

However, the Joint Board does not offer any specific sunset date. Rate Counsel urges the Commission to establish clear sunset dates.

Implementation, Transition and Review.

Initial comments address implementation and transition matters. For example, CPUC recommends that reforms to the high cost program occur within a three-year to five-year time frame.²³⁸ IURC recommends that “ample transition time be accorded to all providers” that would be affected by high cost reform to enable them to revise their businesses, as necessary.²³⁹ Rate Counsel recognizes the need for carriers to have time to revise their businesses to accommodate high cost reform, but cautions the Commission against unduly delaying high cost reform, which would penalize consumers.

Rate Counsel urges the Commission to adopt the Joint Board’s recommendation for an overall cap on high cost funding.²⁴⁰ As stated in initial comments:

ILECs’ ability to achieve a fair rate of return on their investment in the public switched network is not at risk. 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 ILECs’ ability to earn supra-competitive profits on their special access services). 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.²⁴¹

²³⁸ / CPUC, at 13.

²³⁹ / IURC, at 2.

²⁴⁰ / Recommended Decision, at para. 26.

²⁴¹ / Rate Counsel, at 52-53.

The Commission should, consistent with the Joint Board’s recommendation, cap the total amount of high cost funding at \$4.5 billion.²⁴² Rate Counsel also concurs with the proposed elimination of support from the identical support rule, over a three-year period, which will, as the Joint Board states, provide a source of monies for the Mobility and Broadband funds.²⁴³

Rate Counsel also supports the Joint Board’s recommendation that each of 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),²⁴⁴ and, as explained in these reply comments, recommends that high cost support for the three BOCs and the other price cap ILECs be discontinued, and that high cost support for the non-rural carriers be phased out over a five year period.

VII. REVERSE AUCTIONS

The Commission has tentatively concluded that reverse auctions offer several potential advantages over current high-cost support distribution mechanisms, and that the Commission should develop an auction mechanism to determine high-cost universal service support.”²⁴⁵ Rate Counsel reiterates its opposition to the widespread use of reverse auctions, which, although theoretically appealing, would entail undue implementation challenges.²⁴⁶ Several commenters express concerns related to reverse

²⁴² / Recommended Decision, at para. 26.

²⁴³ / See Rate Counsel, at 54; Recommended Decision, at para. 27.

²⁴⁴ / *Id.*, at para. 32.

²⁴⁵ / Reverse Auction NPRM, at para. 1.

²⁴⁶ / See Rate Counsel, at 54-59.

auction implementation and emphasize the drawbacks of reverse auctions.²⁴⁷ TWTC states that “[a]uctions are extremely complex and would be needlessly costly to conduct.”²⁴⁸ According to Embarq, the use of reverse auctions for ILECs would necessarily involve the Commission pre-empting state carrier-of-last-resort requirements and rate regulation for auction losers.²⁴⁹ There is nothing in the record to contradict the following observation put forth by NASUCA:

It is unreasonable to think that the FCC can orchestrate the auction of existing high-cost rural territories currently served by incumbents who have invested billions of dollars to provide quality services to their customers, and have carrier of last resort . . . responsibilities in those areas, without causing irreparable harm to the rural customers who were promised universal availability of quality communications services at affordable and reasonably comparable rates by the 1996 Telecommunications Act.²⁵⁰

Rate Counsel concurs with the Wyoming OCA that “the time is not right to implement reverse auctions as the overarching framework for currently needed high-cost funding reform.”²⁵¹ The Commission should not ignore the numerous difficult issues related to the implementation auctions and drawbacks of the Commission’s current proposals, including (but not limited to) the following issues:

- Carrier of Last Resort obligations;
- Stranded and/or duplicate network investment;

²⁴⁷ / See, e.g., Wyoming OCA (re Reverse Auctions), at 2; TWTC, at 3; ITTA, at 36; Qwest, at 8; RCA, at iv; NASUCA (re Reverse Auctions), at 5-7; Embarq, at 15; AT&T, at 34; US Telecom, at 20.

²⁴⁸ / TWTC, at 3.

²⁴⁹ / Embarq, at 15.

²⁵⁰ / NASUCA (re Reverse Auctions), at 2.

²⁵¹ / Wyoming OCA (re Reverse Auctions), at 2. Wyoming OCA expresses concern that explicit caps on support would impede the discovery of proper costs (and therefore appropriate bids) through the reverse auction mechanism. *Id.*, at 3.

- Reserve Prices; and
- Complexity and cost of the unresolved implementation details and regulations.²⁵²

AT&T supports the goals of reverse auctions, but not the auctions themselves.

AT&T notes that if an application process is used instead of a reverse auction, the Commission can award support based on factors other than cost alone, *e.g.* speed of build-out. AT&T also questions the obligations of an ILEC that loses an auction.²⁵³

US Telecom asserts that “[r]everse auctions are the most rational way to determine the appropriate single mobile provider in a geographic area with multiple wireless competitive ETCs” and states that “[t]he Commission is correct that direct market signals are a far superior methodology to either historical or forward-looking cost models, particularly when applied to providers that operate relatively unconstrained by either price or profit regulation, as mobile competitive ETCs do.”²⁵⁴ However, US Telecom acknowledges that the mechanics of reverse auctions and the requirements placed on successful bidders are unclear and may be difficult to resolve. US Telecom concedes this and states, “a statement that would define the winning bidder’s obligation would have to be developed and this obligation would serve as the basis for bidding. In return for winning the action, the provider would be required to offer service in the entire area and to meet *any other terms upon which the bidding process was conditioned.*”²⁵⁵ Ultimately, while US Telecom acknowledges that reverse auctions should be

²⁵² / See, *e.g.*, Wyoming OCA (re Reverse Auctions), at 3 6; Qwest, at 8; Embarq, at 17; RCA, at 68.

²⁵³ / AT&T, at 34.

²⁵⁴ / US Telecom, at 19-20.

²⁵⁵ / *Id.*, at 20 (emphasis added).

implemented “with deliberation” and in a “measured and sequential way,” US Telecom provides no specific implementation strategies.²⁵⁶ Notably, US Telecom’s support for reverse auctions does not extend to wireline carriers. US Telecom opposes competitive bidding to reduce ETCs in an area to just one regardless of technology: “Potential legal and practical constraints would make application of reverse auctions to wireline providers highly problematic and far more troublesome than the savings which they yield.”²⁵⁷ US Telecom’s argument comes back to the fact that wireline ILECs and CLECs receive far less support in study areas where there are multiple ETCs than the wireless ETCs do, and thus the total wireline support is “negligible in the overall context of high cost support.”²⁵⁸ Yet, this type of reasoning is troubling and would, at a minimum, attract a legal challenge. US Telecom also bases its opposition on the purported fact that wireless carriers have market-based rates, yet “wireline carriers are subject to pervasive price or profit regulation.”²⁵⁹

Verizon and Verizon Wireless submitted a proposal for a competitive bidding process to be used to fulfill universal service obligations.²⁶⁰ Verizon and Verizon Wireless’ plan is detailed and builds off of the Commission’s spectrum allocation experience, but ultimately, the proposal is unnecessarily unwieldy as a wholesale replacement of existing HCF. Instead the proposed plan has some merit for adoption on a

²⁵⁶ / *Id.*, at 23.

²⁵⁷ / *Id.*, at 24.

²⁵⁸ / *Id.* US Telecom supports allowing wireline CETCs to continue to draw funds based on identical support (with the exception of the IAS and ICLS portions). *Id.*, at 31.

²⁵⁹ / *Id.*, at 25. US Telecom questions how reverse auctions would conform with rate of return regulation. *Id.*, at 26.

²⁶⁰ / Verizon and Verizon Wireless, at 18-22. Verizon and Verizon Wireless, Appendix, “Modernizing Universal Service: a Design for Competitive Bidding” (“Verizon Reform Plan”). (Verizon and Verizon Wireless submitted an earlier version of this plan last year. Comments of Verizon and Verizon Wireless, WC Docket No. 05-337, CC Docket 96-45, May 31, 2007, Attachment.)

pilot basis to distribute broadband support, and, should the Commission decide to support mobility in unserved areas, for that purpose as well.

Rate Counsel agrees with the Wyoming OCA that “regulation may need to become more heavy-handed under a regulatory scheme that only allows for one provider to receive high-cost support in a geographic area in order to ensure compliance with the reverse auction requirements.”²⁶¹ The concerns raised in this proceeding make implementation of a reverse auction scheme an ill-advised, costly, and complicated factor in USF administration. Just as the identical support rule had negative unintended consequences, which are only now being ameliorated, reverse auctions likely would create new problems for the future. Rate Counsel recognizes the theoretical appeal of reverse auctions but reiterates its opposition to using reverse auctions as a way to distribute existing high cost support: the cost and burden of the administrative infrastructure necessary to design and implement such a mechanism outweigh the benefit. The Commission should not ignore the real drawbacks simply because the solution is theoretically (or politically) appealing.

Indeed, ITTA states that the “Commission’s Reverse Auctions NPRM appears to steamroll over filed oppositions to reverse auctions” and identifies numerous concerns that have been raised by many commenters opposing the use of reverse auctions.²⁶² Also, NASUCA questions the Commission’s apparent failure to heed the “significant and

²⁶¹ / Wyoming OCA, at 4. *See, also*, Rate Counsel, at 55 quoting Commissioner Copp’s observation that the reverse auction approach may, in fact, be “hyper-regulatory.”

²⁶² / ITTA, at 36. *See id.*, generally at 36-42.

substantive record that shows the lack of merit” of reverse auctions in areas already served by a carrier.²⁶³

Qwest, like Rate Counsel, questions the use of reverse auctions on a broader basis, stating that to distribute high-cost support where existing providers already serve consumers “raises significant concerns surrounding the existing network in the event the existing provider is not the successful bidder in the auction.”²⁶⁴ The solution may be to use reverse auctions in specific cases in an unserved geographic area. To use reverse auctions only in unserved areas would eliminate many of the concerns related to the existing carrier’s network. If, despite the drawbacks entailed, the Commission concludes that reverse auctions are desirable, Rate Counsel recommends that the Commission start small. Initial comments show substantial support for exploring reverse auctions on a pilot basis.²⁶⁵ Rate Counsel reiterates its support for the use of a reverse auction on a limited pilot basis to distribute support for broadband service and, if the Commission decides to subsidize wireless service, on a pilot basis to subsidize wireless service deployment in unserved areas.

²⁶³ / NASUCA (re Reverse Auctions), at 3. *See, also id.*, at footnote 9 (citing previous comments of numerous parties).

²⁶⁴ / Qwest, at 8.

²⁶⁵ / Many echo Rate Counsel’s recommendation (at 10) that a reverse auction be used on a pilot basis (MACRUC, at 2; NCTA at 15 (indicating “[b]ecause the Commission has no experience with using reverse auctions to distribute high-cost support, it will take some time before they can be used extensively” and also supporting, for that reason, the use of a pilot program); ITTA, at 38; Qwest, at 7; NASUCA (re Reverse Auctions), at 2, 7. Also, IURC “tentatively and cautiously supports the selective deployment of reverse auctions initially as a transition tool for migrating from the current competitive eligible telecommunications carrier (CETC) scheme to the proposed ‘cap-ex focused’ model for the Mobility Fund.” IURC, at 2.)

Similar to Rate Counsel, both Qwest and NASUCA express support for reverse auctions in only limited circumstances.²⁶⁶ NASUCA supports the use of reverse auctions only in unserved areas and states that the use of auctions would be “particularly appropriate as pilot programs for broadband or mobility service in [unserved] areas.”²⁶⁷ Qwest’s broadband proposal includes competitive bidding as a way for states to distribute block grants.²⁶⁸ It is clear that, for most commenters, any support that does exist for reverse auctions is limited to narrowly defined conditions (unserved areas, broadband and mobility funds).²⁶⁹

If the Commission nonetheless concludes that it will implement reverse auctions, whether on a pilot or wholesale basis, there is widespread support for the requirement that there should be only a single winner of an auction in any defined area.²⁷⁰ In contrast to most commenters, USFon welcomes the use of reverse auctions – even auctions that allow for multiple winners. According to USFon’s proposal, multiple winners would not raise the level of the High Cost Fund because geographic areas would be subject to an

²⁶⁶ / Qwest, at 7; NASUCA (re Reverse Auctions), at 2, 7. *See, also*, IURC, at 11-12 (supporting pilot program for reverse auctions).

²⁶⁷ / NASUCA (re Reverse Auctions), at 2.

²⁶⁸ / Qwest, at 7.

²⁶⁹ / *See, e.g.*, NASUCA (re Reverse Auctions), at 2; MACRUC, at 2; NCTA at 15; ITTA, at 38; Qwest, at 7; IURC, at 2, 11-12.

²⁷⁰ / Qwest, at 7; NASUCA, (re Reverse Auctions), at 9-10. The Reverse Auctions NPRM is in opposition to the Joint Board Recommended Decision in that it seeks input on whether wireless and wireline ETCs should have separate auctions for high cost support. Of course, wireless funding would be completely separate if the Commission adopted the Joint Board’s idea for a mobility fund. See, also US Telecom, at 18 highlighting the apparent contradiction or tension in the Commission’s methods for reform: the Reverse Auctions NPRM considers competitive bidding while the Identical Support Rule NPRM considers a requirement that CETCs file cost studies; CU et al. at 4-5, stating: “These three NPRMs, while broad in nature, do not deal with the problem of universal service reform in a comprehensive manner . . . Indeed, if all of the ‘tentative conclusions’ contained within these three NPRMs were implemented, the result would be a Fund in more need of reform than the one we have now – and one no closer to realizing the goal of universal, affordable and competitive advanced communications marketplace.”

aggregate cap which would be shared by multiple winners in that area.²⁷¹ However, although geographic capping might be effective in limiting growth of high cost support, multiple winners would dilute support on a per-line basis, and therefore, may decrease the effectiveness of the High Cost Fund. Rate Counsel agrees with Qwest that to the extent that reverse auctions could reduce the cost of support, “the inefficiencies of providing explicit high-cost support to multiple providers in a previously unserved high cost area would eclipse any consumer welfare gain introduced by multiple supported providers.”²⁷² Proponents of a multiple winner auction system contend that consumers benefit from competition.²⁷³ Yet, this reasoning completely ignores the consumer harm related to the growing and bloated subsidies that result from high cost support for multiple providers currently (and that the Commission has attempted to address partially in its May 1st Order capping CETC subsidies). Finally, Rate Counsel repeats its analysis that in unserved areas, “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.”²⁷⁴ NASUCA’s position that “a multiple winner auction, in any form, would not be reform, but would represent preservation of the status quo,”²⁷⁵ should not be ignored.

Rate Counsel urges the Commission to reject reverse auctions as a way of distributing high cost support because of the numerous implementation challenges that would thwart its purported goal of achieving an efficient high cost distribution system.

²⁷¹ / Comments and Proposals of USFon (“USFon”), at 5.

²⁷² / Qwest, at 8.

²⁷³ / See, e.g., Reverse Auction NPRM, at 16, citing CTIA.

²⁷⁴ / Rate Counsel, at 55.

²⁷⁵ / NASUCA (re Reverse Auctions), at 11.

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.²⁷⁶ 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 already is being provided. Initial comments show broad support for the position that if the Commission does decide to move forward with reverse auctions, that those auctions should be utilized only in unserved or as limited, pilot programs for the broadband and mobility funds.²⁷⁷ Additionally, Qwest’s recommendation that the Commission open a rulemaking to develop the auction rules and a “model contract for states to adopt and enforce” vis-à-vis the winning bidder of its proposed broadband provider auction has merit in many circumstances.²⁷⁸ Certainly, Qwest’s proposal that the Commission require “performance bonds” and adopt clear performance triggers are important components of any funding, an idea that may well merit consideration in all aspect of the universal service programs.²⁷⁹

VIII. IDENTICAL SUPPORT RULE

Initial comments address the Commission’s Identical Support NPRM, which primarily concerns how one might compute the costs for competitive ETCs (if the identical support rule is abolished). Embarq asserts that the identical support rule should

²⁷⁶ / Reverse Auctions NPRM, at paras. 50-51.

²⁷⁷ / *See, e.g.*, NASUCA (re Reverse Auctions), at 2, and discussion *supra*.

²⁷⁸ / Qwest Broadband Proposal, at 24-25.

²⁷⁹ / *Id.*, at 25.

be eliminated,²⁸⁰ stating that it is illogical to give CETCs support without requiring any cost justification.²⁸¹ Windstream finds that the rule “irrationally allows multiple CETCs to receive support as a function of other carriers’ costs, which are unrelated to the CETCs’ costs and are often based on different technologies.”²⁸²

In sharp contrast, Rural Cellular Association and the Alliance of Rural CMRS Carriers (“RCA”) asserts that the Commission *cannot* eliminate the identical support rule, stating: “Repeal of [the] identical support rule would turn the Commission’s core principle of competitive neutrality into a hollow promise by further entrenching incumbent LECs in rural and other high-cost markets and would hinder the delivery of competitive services in these markets.”²⁸³ According to RCA, the Commission has an obligation “to ensure that consumers in rural and high-cost areas have affordable access to wireless services, and elimination of the identical support rule would have the effect of reducing the likelihood that this obligation could be met.”²⁸⁴ However, contrary to RCA’s position, a Mobility Fund – targeted solely to areas that otherwise would be unserved – would subsidize wireless deployment in unserved areas and benefit consumers more efficiently than would the approximate \$1.18-billion now spent to subsidize duplicative networks under the identical support rule.²⁸⁵

²⁸⁰ / Embarq, at 3. *See also* ITTA, at 25-28 (supporting elimination of identical support rule).

²⁸¹ / Embarq, at 10.

²⁸² / Windstream, at 22. Wyoming OCA also agrees that the rule should be eliminated. Wyoming OCA (re Identical Support Rule), at 2.

²⁸³ / RCA, at iv.

²⁸⁴ / *Id.*, at 5.

²⁸⁵ / CETC Cap Order, at para. 6.

While Wyoming OCA agrees that the lack of cost data underlying the high cost mechanism is a major problem,²⁸⁶ it does not see cost-based support for CETCs (primarily wireless carriers) as the best way forward in an overall plan of comprehensive reform. Wyoming OCA argues that because wireless carriers are essentially unregulated, there is no record of costs: In order to account for their costs, a new uniform system of accounts would need to be created, studies conducted to separate expenses and assets based on supported vs. non-supported services, and systems of verification established. Wyoming OCA states: “It would be the equivalent of starting a mini-regulatory system for wireless carriers in an era when there is little regulation of wireline carriers.”²⁸⁷ Furthermore, Wyoming OCA asserts that basing support on carriers’ own costs would be difficult because the costs are difficult to verify.²⁸⁸ Wyoming OCA recommends that the Commission “transition to a new, comprehensive system of reform that is not grounded in formulaic inputs that are hard to verify.”²⁸⁹ Rate Counsel concurs

RCA argues that the Commission *cannot* use costs as basis for support for multiple reasons. First, RCA argues that using embedded costs as the basis for high-cost support violates the tenet of competitive neutrality. According to RCA, “any independent examination of wireless competitive ETC costs, for the purpose of allocating high-cost support, would violate the competitive neutrality principle”²⁹⁰ because basing support on costs gives some carriers an unfair advantage over others. Rate Counsel disagrees with RCA’s position. Instead, the Commission should refrain from providing high cost support

²⁸⁶ / Wyoming OCA (re Recommended Decision), at 3.

²⁸⁷ / Wyoming OCA (re Identical Support Rule), at 3-4.

²⁸⁸ / *Id.*, at 2.

²⁸⁹ / *Id.*

²⁹⁰ / RCA, at 15 and 53.

at an amount that is *greater* than that provided to the ILEC.²⁹¹ To do so would force consumers to fund inefficient entry.²⁹²

RCA also refers to the ways that wireline economics differ from wireless economics, and concludes that instead of the Commission facing head-on the challenge of constructing fair rules that take account of these differences, “the simplest (and most equitable) solution to this dilemma is to avoid it altogether by retaining the identical support rule.”²⁹³ Rather than continue to support costly, inefficient, and duplicative support systems, As RCA’s proposal would seem to do, Rate Counsel encourages the Commission to use a well-defined, Mobility Fund of limited duration and with adequate accountability.

Verizon and Verizon Wireless contends that eliminating the identical support rule and replacing it with the option for CETCs to obtain support based on cost data “is a misguided ‘quick-fix.’”²⁹⁴ Instead, according to Verizon and Verizon Wireless, the Commission should take immediate steps to transition wireless support so that it is either sunset or used for the specific purpose of deploying wireless where it would not otherwise occur. Rate Counsel concurs with Verizon and Verizon Wireless’ recommendation. Rate Counsel also concurs with the New Jersey Board that “[t]here is no economic basis for funding more than one network when one network is not sustainable without support.”²⁹⁵ The Commission should eliminate the identical support

²⁹¹ / Rate Counsel, at 61.

²⁹² / *Id.*, at 61-62. See, also, Identical Support NPRM, at para. 25.

²⁹³ / *Id.*, at 54.

²⁹⁴ / Verizon and Verizon Wireless, at 4.

²⁹⁵ / New Jersey Board, at 3. The MACRUC states also support the elimination of the identical support rule. MACRUC States, at 2.

rule because, for the most part, it is subsidizing the construction of duplicative networks rather than subsidizing carriers' entry into unserved areas. US Telecom asserts that when wireline CETCs do compete with incumbent ETCs, they compete directly with incumbent ETCs for a "relatively fixed number of subscriber lines."²⁹⁶

Rate Counsel reiterates its support for the Joint Board's conclusion 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,"²⁹⁷ and agrees that the Commission should eliminate the identical support rule.²⁹⁸ Rate Counsel stated in initial comments:

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." 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." The Commission should immediately cap the competitive ETC fund and eliminate the identical support rule.²⁹⁹

Rate Counsel, therefore, commends the Commission for its decision last month to cap the CETC fund, and urges the Commission now to eliminate the identical support rule. Toward that end, Rate Counsel continues to support the Joint Board's recommended transition consisting of the reduction of identical support funding to provide the source

²⁹⁶ / US Telecom, at 32.

²⁹⁷ / Recommended Decision, at para. 35.

²⁹⁸ / Identical Support NPRM, at para. 1.

²⁹⁹ / Rate Counsel, at 62, cites omitted.

for Broadband and Mobility Funds, but recommends a three-year transition rather than the five-year transition proposed by the Joint Board.³⁰⁰

As stated in Rate Counsel's initial comments, the expectation when adopting a CETC policy was that CETCs would "capture" the lines that ILECs had previously served.³⁰¹ As explained 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.³⁰²

Thus, the identical support rule has increased the number of lines served but, for the most part, has not subsidized deployment to underserved or unserved areas. US Telecom emphasizes the importance of wireline networks.³⁰³ In fact, because the support of

³⁰⁰ / Recommended Decision, at para. 27.

³⁰¹ / Rate Counsel, at 59.

³⁰² / Identical Support NPRM, at para. 9, cites omitted.

³⁰³ / US Telecom states: "Currently operation of wireless networks almost always requires dependence on wireline networks for functions such as backhaul. It is thus impractical to create a structure in which the wireline carrier serving a high cost area could lose universal service support and have rural consumers solely rely on a mobile solution. Not only is maintenance of the wireline network required for wireless carriers to operate efficiently, most broadband service is and will continue to be provided over wireline networks, at least in the near to mid-term future." US Telecom, at 25.

competitors is based upon the incumbent's costs, the CRTC does not have an incentive to deploy facilities to areas that are more costly to serve.³⁰⁴

The Commission should eliminate interstate access support and interstate common line support not only for CLECs, but also for BOCs.

Embarq,³⁰⁵ ITTA,³⁰⁶ Qwest,³⁰⁷ and US Telecom³⁰⁸ are among those that recommend that the Commission eliminate Interstate Access Support (IAS) and Interstate Common Line Support (ICLS) for wireless carriers. ITTA estimates that the elimination of access replacement support that is paid to mobile carriers would reduce the USF by a half-billion dollars.³⁰⁹ US Telecom argues that access reform lowered the access rates paid by wireless ETCs to ILECs and identical support to wireless ETCs is thus “unnecessary and redundant.”³¹⁰ US Telecom argues that IAS and ICLS funds should be diverted to LEC high cost wire centers to “increase the money available for needed investment in network facilities, including joint use facilities that can be used to provide

³⁰⁴ / Rate Counsel, at 60, citing Identical Support NPRM, at para. 10.

³⁰⁵ / Embarq, at 12. According to Embarq: “Wireless C-ETCs have never relied on access charges to cover their costs; therefore they have never demonstrated a legitimate need for the revenues produced by access charges.” *Id.* Windstream Communications, Inc. (“Windstream”), at 23. Windstream also opposes wireless carriers receiving Local Switching Support (LSS).

³⁰⁶ / ITTA states that access replacement support corresponds with access revenues which mobile carriers would not have received. ITTA, at 30.

³⁰⁷ / Qwest agrees with the Commission’s tentative conclusion that CETCs not receive IAS and ICLS support noting that “the purposes underlying IAS and ICLS support to ILECs are not served in providing this support to CETCs.” Qwest, at 7, citing Identical Support Rule NPRM, at para. 23.

³⁰⁸ / US Telecom supports the use of competitive bidding and auctions for determining support for mobile competitive ETCs but asks the Commission to phase out the portion of identical support which relates to access replacement mechanisms. US Telecom, at 11. See, also, US Telecom, at 12 supporting the Commission’s tentative conclusion that competitive ETCs should not receive IAS or ICLS support. US Telecom states that IAS And ICLS “were created to replace access revenue lost through the reduction of interstate access charges in the Commission CALLS and MAG proceedings” and were “specifically designated for incumbent LECs which were, and continue to be, subject to pervasive Commission regulation as to either their interstate access prices or earnings.”

³⁰⁹ / ITTA, at 31.

³¹⁰ / US Telecom, at 13.

broadband service.”³¹¹ Rate Counsel concurs that because wireless ETCS were never entitled to tariffed access charges and because CETCs (whether wireline or wireless) have not traditionally relied upon access charges to support universal service, the Commission should eliminate those subsidies to CETCs immediately.³¹² However, Rate Counsel opposes US Telecom’s proposal to divert these funds to ILECs. Instead of shifting monies from CETCs to ILECs, the goal of the Commission should be to implement high cost reform that gradually reduces the USF overall, and to improve the overall efficiency of the way in which subsidies are distributed to the industry. The consequence of an unnecessarily high USF is a higher telephone bill for consumers.

High cost support should not be used to subsidize competition; competition instead should drive down the need for high cost support.

Commenters concur with the Joint Board’s observation that it is not “in the public interest to use federal [high cost] support to subsidize competition and build duplicative networks.”³¹³ Rate Counsel reiterates its recommendation that the Commission avoid allowing high cost funds to increase as a result of subsidizing inappropriately the development of competition. Competition should lower rates for consumers and not increase the burden on consumers.

Numerous comments raise the well-founded concerns that the approximate one billion dollars that is being spent on wireless subsidies contributes only minimally to the

³¹¹ / *Id.*, at 13. US Telecom proposes a four-step phase-out of access replacement, which would include a 25 percent reduction per year. *Id.* See also ITTA, at 25; 28-31.

³¹² / Verizon and Verizon Wireless, at 5.

³¹³ / Recommended Decision, at para. 35. See e.g., comments of Verizon and Verizon Wireless, at 8.

goal of expanding wireless coverage.³¹⁴ A recent study conducted by Kenneth W. Caves, Ph.D. and Jeffery A. Eisenach, Ph.D. of Criterion Economics, LLC found that USF support to wireless carriers does not achieve the goals of the program. Noting that wireless CETCs received \$771 million in high cost support in 2006,³¹⁵ Caves and Eisenach used regression analysis to test the relationship between subsidies to wireless CETCs, and increases in wireless availability and choice of providers. Caves and Eisenach found that USF support neither expands the geographic area covered by wireless networks, nor increases the choice of wireless providers.³¹⁶ Rate Counsel opposes Windstream's recommendation that the Commission limit ETC designations to one wireline and one wireless carrier in each supported area³¹⁷ and instead recommends that any mobility subsidies be limited to the purpose of deploying wireless in unserved areas.

IX. OTHER PROPOSALS FOR USF REFORM

The Commission should reject the Sprint Nextel proposal.

On May 12, 2008, Sprint Nextel submitted a new proposal, which, essentially, would shift the recovery of approximately \$3 billion from USF assessments to subscriber line charge ("SLC") increases.³¹⁸ Sprint Nextel estimates that its proposed HCF reduction would translate into a reduction from 11.3% to 6.0% in the contribution

³¹⁴ / Verizon and Verizon Wireless, at 8-9, citing Criterion studies (Caves, Kenneth W. and Jeffery A. Eisenach, "The Effects of Providing Universal Service Subsidies to Wireless Carriers," June 13, 2007 ("Criterion Study"); ITTA, at 34 citing Criterion Study).

³¹⁵ / Caves, Kenneth W. and Jeffery A. Eisenach, "The Effects of Providing Universal Service Subsidies to Wireless Carriers," June 13, 2007, at 1.

³¹⁶ / *Id.*, at 42.

³¹⁷ / Windstream, at 3.

³¹⁸ / Sprint Nextel Proposal.

factor³¹⁹ and an increase of \$3.50 in the subscriber line charge.³²⁰ According to Sprint Nextel, “the effects on consumers from an increased SLC should be offset by reductions on consumer bills of pass-through federal universal service charges resulting from fund contributions and by additional protection for low-income consumers.”³²¹

Rate Counsel urges the Commission to reject Sprint-Nextel’s deeply flawed proposal. The proposal clearly would penalize low-volume consumers, as can be illustrated with a simple example. Assume a customer’s monthly bill is \$30. The USF reduction from 11.3% to 6.0% (assuming that carriers *do* flow through the savings) translates into a lowering by approximately five percentage points of the USF assessment. This lower USF fee translates into a “savings” of approximately \$1.50 for our illustrative customer with a \$30 bill.³²² This same customer would face an *increase* of \$3.50, and therefore, the net impact for this low-volume customer would be an overall increase in monthly rates of \$2.00. This proposal may benefit carriers, but would harm all customers with below-average expenditures.

Sprint Nextel’s proposal is also flawed because it assumes implicitly that the entirety of the HCF is efficient and necessary. As Rate Counsel demonstrates in these comments, the HCF is not warranted, as a result of factors such as changes in technology, ILECs’ opportunities to generate unregulated revenues, and deregulation in many markets.

In summary, Sprint Nextel’s proposal is flawed in at least two ways:

³¹⁹ / *Id.*, at 7.

³²⁰ / *Id.*, at 4.

³²¹ / *Id.*, at 7.

³²² / Put differently, instead of an 11.3% fee equal to \$3.39, the customer would see a 6% fee equal to \$1.80, for a monthly savings of \$1.59.

- Low volume customers would bear disproportionately the brunt of the change.
- The HCF should be declining; rather than “moving the problem around,” the Commission should eliminate non-rural high cost support and phase out rural high cost support over a five-year period.

X. CONCLUSION

Rate Counsel commends the Commission for undertaking long overdue reform of the high cost fund and seeking ways to deploy broadband and mobile services to unserved areas. Rate Counsel urges the Commission to implement timely reform to the high cost fund so that consumers are not burdened by inefficient subsidies for carriers including ILECs. A federal USF should be sufficient, but not excessive, and, therefore, the Commission should not only resist pressure from some carriers to increase high-cost support, but also should examine critically the need for existing levels of support. Ultimately, universal service is jeopardized if the fund renders services unaffordable for consumers.

Rate Counsel is in favor of the Joint Board’s proposed transitional elimination of support from the identical support rule to provide funding for the Mobility and Broadband Funds, and recommends that such transition occur over a three-year period. Rate Counsel further urges the Commission to eliminate high cost support for price cap ILECs and to begin a gradual phase-out of support for non-price cap ILECs and rural ILECs. Rate Counsel recommends that the Commission allocate broadband funds to states, based proportionally on their population, to subsidize broadband service for Lifeline participants and construction of facilities to unserved areas. An assessment on all broadband revenues and the transition of funds from identical support, matched by state funds, would finance these broadband subsidies, which are critically important so

that all Americans have access to affordable broadband service. Rate Counsel opposes the use of reverse auctions except on a pilot basis to distribute broadband or mobility support. Finally, Rate Counsel urges the Commission to establish clear measures for ensuring accountability by USF recipients, assessing reasonably comparable urban and rural rates, and sunset of various USF programs.

Respectfully submitted,

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