

**Before the  
FEDERAL COMMUNICATIONS COMMISSION  
Washington, D.C. 20554**

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

**COMMENTS OF THE**  
  
**NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION**

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April 17, 2008

## SUMMARY

The preservation and promotion of universal service is one of the Commission's most important jobs. As the Federal-State Joint Board on Universal Service recently found, however, the funding mechanisms the Commission established pursuant to the Telecommunications Act of 1996 are "dated and need to be modernized."<sup>1</sup> Without significant changes, the Joint Board observed, "the federal universal service fund [is] in dire jeopardy of becoming unsustainable."<sup>2</sup>

In the three *Notices* on which it now seeks comment,<sup>3</sup> the Commission proposes a variety of steps to get the Universal Service Fund back on a sustainable track. In the *Identical Support Notice*, the Commission tentatively concludes that it should eliminate the "identical support" rule and solicits comment on how support for competitive eligible telecommunications carriers (CETCs) should be calculated if the rule is eliminated.<sup>4</sup> In the *Reverse Auctions Notice*, the Commission seeks comment on when reverse auctions should be used to distribute universal service support and what rules should apply for such auctions when they are used.<sup>5</sup> Finally, in the *Comprehensive Reform Notice*, the Commission solicits comment on a recommendation from the Joint Board to restructure the current high cost funding mechanisms into three new funds – a

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<sup>1</sup> *High-Cost Universal Service Support*, WC Docket No. 05-337, Recommended Decision, 22 FCC Rcd 20477, 20483 ¶ 22 (2007) (*Joint Board Recommended Decision*).

<sup>2</sup> *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Recommended Decision, 22 FCC Rcd 9023 (2007).

<sup>3</sup> *Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-4 (rel. Jan. 29, 2008) (*Identical Support Rule Notice*); *Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-5 (rel. Jan. 29, 2008) (*Reverse Auctions Notice*); *Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-22 (rel. Jan. 29, 2008) (*Comprehensive Reform Notice*).

<sup>4</sup> *Identical Support Notice* at ¶ 12. As explained below, the identical support rule provides that a CETC is entitled to receive the same amount of support for serving a customer that the incumbent would receive if it served that customer and its support was calculated on a per-line basis.

<sup>5</sup> *Reverse Auctions Notice* at ¶ 1.

Provider of Last Resort (POLR) Fund, a Mobility Fund, and a Broadband Fund – and to cap the entire federal high-cost program at current funding levels.<sup>6</sup>

NCTA supports the general direction of the Commission’s proposals. It is long past time for the Commission to better align these legacy mechanisms with today’s marketplace realities. The Commission’s proposals do not go far enough, however, in reflecting the benefits of existing competition in high-cost areas and encouraging additional competition in the future. In these comments, NCTA proposes a number of steps the Commission can take to curtail the growth of the fund, and eventually reduce the total amount of government funding that is needed, including the following:

- Impose a cap on the total amount of federal high-cost support:
- Establish a procedure for reassessing support levels where market conditions have changed;
- Cap per-line support at current levels for *all* providers serving a particular area;
- Limit support for each provider to two lines per residential household;
- Establish safeguards for any new Mobility or Broadband funding mechanisms.

Each of these steps is designed to stem the escalating growth in federal support and ensure that the Universal Service Fund works *with* the marketplace, rather than working *against* it. NCTA encourages the Commission to move forward with these proposals expeditiously.

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<sup>6</sup> *Comprehensive Reform Notice* at ¶ 1, citing *Joint Board Recommended Decision* at ¶¶ 1-3.

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**COMMENTS OF THE  
NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION**

The National Cable & Telecommunications Association (“NCTA”) hereby submits its comments in response to the three Notices of Proposed Rulemaking issued by the Commission in the above-captioned proceedings.<sup>1</sup>

**INTRODUCTION**

NCTA is the principal trade association for the U.S. cable industry, representing cable operators serving more than 90 percent of the nation's cable television households and more than 200 cable program networks. The cable industry is the nation’s largest broadband provider of high-speed Internet access after investing over \$100 billion since 1996 to build a two-way interactive network with fiber optic technology. Cable companies also provide state-of-the-art voice service to millions of American homes and are rapidly making these services available nationwide.

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<sup>1</sup> *Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-4 (rel. Jan. 29, 2008) (*Identical Support Rule Notice*); *Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-5 (rel. Jan. 29, 2008) (*Reverse Auctions Notice*); *Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Notice of Proposed Rulemaking, FCC 08-22 (rel. Jan. 29, 2008) (*Comprehensive Reform Notice*).

Cable operators increasingly are bringing the benefits of their competitive voice services to rural areas. With appropriate changes in how funding is distributed, the presence of cable operators and other facilities-based competitors in high-cost areas ultimately should reduce the need for, and challenge the assumption of reliance on, federal universal service support.

In the three *Notices* on which it now seeks comment, the Commission continues its ongoing efforts to reform the high-cost fund and halt the staggering growth that has occurred over the last few years.<sup>2</sup> In the *Identical Support Notice*, the Commission tentatively concludes that it should eliminate the “identical support” rule and solicits comment on how support for competitive eligible telecommunications carriers (CETCs) should be calculated if the rule is eliminated.<sup>3</sup> In the *Reverse Auctions Notice*, the Commission seeks comment on when reverse auctions should be used to distribute universal service support and what rules should apply for such auctions when they are used.<sup>4</sup> Finally, in the *Comprehensive Reform Notice*, the Commission solicits comment on a recommendation from the Joint Board to restructure the current high cost funding mechanisms into three new funds – a Provider of Last Resort (POLR) Fund, a Mobility Fund, and a Broadband Fund.<sup>5</sup> As part of its proposal, the Joint Board also recommends capping the entire federal high-cost program at current funding levels and providing states with a more active role in deciding how federal funds should be distributed.<sup>6</sup>

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<sup>2</sup> In addition to these three *Notices*, the Commission also has a pending Notice of Proposed Rulemaking in which it is considering a cap on the funding provided to CETCs. *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Notice of Proposed Rulemaking, 22 FCC Rcd 9705 (2007).

<sup>3</sup> *Identical Support Notice* at ¶ 12. As explained below, the identical support rule provides that a CETC is entitled to receive the same amount of per-line support for serving a customer that the incumbent would receive if it served that customer.

<sup>4</sup> *Reverse Auctions Notice* at ¶ 1.

<sup>5</sup> *Comprehensive Reform Notice* at ¶ 1, citing *High-Cost Universal Service Support*, WC Docket No. 05-337, Recommended Decision, 22 FCC Rcd 20477 (2007) (*Joint Board Recommended Decision*).

<sup>6</sup> *Joint Board Recommended Decision* at ¶¶ 2, 3.

The three *Notices* include a number of constructive proposals for reform of the current USF distribution mechanisms. NCTA generally is supportive of each of the reform concepts underlying the *Notices* – structural reforms, reverse auctions, and new methods of calculating support – although in each case they do not go far enough in reflecting the benefits of competition or acknowledging the role of competition in meeting universal service goals. For example, the proposal to establish a POLR Fund that is available only to incumbents assumes, incorrectly, that markets that were uneconomic for competitive entry in the past will remain that way indefinitely. The Commission should not have any mechanism that is available only to ILECs, nor should it lock itself into subsidizing an ILEC indefinitely, which would discourage facilities-based alternatives from developing. Instead, as proposed below, the Commission should take a more market-oriented approach and establish a mechanism to reassess the amount of support provided to all providers serving a particular geographic area when certain triggers are met.

The Commission also should adopt a market-oriented approach with respect to support for broadband services. As the Commission recently concluded in its Fifth Report to Congress under Section 706 of the Telecommunications Act of 1996, broadband services are being deployed to all Americans on a reasonable and timely basis.<sup>7</sup> To the extent the Commission finds that additional funding for broadband is warranted, that funding generally should be directed to the construction of broadband networks in areas that have no terrestrial broadband service today. Moreover, given that most current recipients of high-cost funding have found a way to meet the consumer demand for broadband services, the Commission should establish a

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<sup>7</sup> See News Release, *FCC Expands, Improves Broadband Data Collection* (Mar. 19, 2008) (“Separately, the FCC today adopted a report showing that broadband services are currently being deployed to all Americans in a reasonable and timely fashion. The Fifth Report to Congress on broadband deployment under Section 706 of the Telecommunications Act of 1996 finds that there have been considerable changes and advances in the delivery of broadband-based services and applications since the Fourth Report.”).

presumption that companies are not eligible for additional broadband funding if they already are receiving high-cost support for a particular geographic area.

**I. TO PROTECT CONSUMERS, THE HIGH-COST FUND SHOULD BE CAPPED AT CURRENT LEVELS UNTIL COMPREHENSIVE REFORMS CAN BE IMPLEMENTED**

The preservation and promotion of universal service is one of the Commission's most important jobs. The federal high-cost support program provides funding to companies that serve geographic areas or individual customers where market forces alone might not result in the availability of affordable voice service. Market forces, however, are not static. Improvements in technology, particularly the transition to IP-based equipment and services, have made it possible for cable operators and other facilities-based competitors to serve areas that previously might not have supported competitive entry. Similarly, incumbent LECs increasingly are able to provide multiple services (including DSL and video) over infrastructure previously used solely to provide telephone service. This transition to markets in which there is facilities-based competition for voice and non-voice services calls into question the need for continued government funding at historical levels, and may eventually permit the total elimination of high cost support in at least some markets.

While these advancements in technology and competition should have the effect of reducing the overall amount of federal support that is needed, that has not happened. Instead, the overall size of the federal Universal Service Fund, and the burden on American consumers, has grown significantly in recent years.<sup>8</sup> The contribution factor has almost doubled from 5.7

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<sup>8</sup> See *Factors That May Increase Future Spending from the Universal Service Fund: A CBO Paper* at 1 (Congressional Budget Office, June 2006) (“Outlays from the Universal Service Fund have grown more than 50 percent in the past six years and now total about \$7 billion annually.”) (*CBO Report*).

percent for the second quarter of 2000 to 11.3 percent for the second quarter of 2008.<sup>9</sup> Absent changes to the program, this trend shows no signs of abating, as a report from the Congressional Budget Office concluded almost two years ago.<sup>10</sup>

The continued growth in the size of the fund is a matter of significant concern to the cable industry. Cable operators providing voice services are required to contribute to the Universal Service Fund,<sup>11</sup> and, as with other providers that pay into the fund, these costs ultimately are borne by consumers. To spare cable customers, as well as customers of other providers, from bearing excessive costs, it is critical that the Commission reduce the burden of federal support programs by more efficiently distributing support.<sup>12</sup>

The Commission's ongoing review of the high cost program in these three *Notices* is an opportunity to align these legacy mechanisms with today's marketplace realities. As we explain below, there are a number of steps the Commission can take to curtail the growth of the fund, and eventually reduce the total amount of government funding that is needed, including the following:

- Establish a procedure for reassessing support levels where market conditions have changed;
- Cap per-line support at current levels for *all* providers serving a particular area;
- Limit support for each provider to two lines per residential household;

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<sup>9</sup> Contribution factors are available on the Commission's web site at <http://www.fcc.gov/omd/contribution-factor.html>.

<sup>10</sup> *CBO Report* at 1 ("Spending for that program could double again in the next few years.").

<sup>11</sup> Cable operators that provide VoIP services have been contributing to the Universal Service Fund since 2006, *see Universal Service Contribution Methodology*, WC Docket No. 06-122, Report and Order and Notice of Proposed Rulemaking, 21 FCC Rcd 7518 (2006), and cable operators that provide circuit-switched services started contributing even earlier.

<sup>12</sup> *Joint Board Recommended Decision* at ¶ 2 ("We are mindful that it is consumers who must pay universal service contributions . . . we also want to avoid significantly increasing the burden on those consumers.").

- Establish safeguards for any new Mobility or Broadband funding mechanisms.

Because any comprehensive reform of the high-cost fund will take time to implement, the Commission also should impose a cap on the total amount of federal high-cost support, as recommended by the Joint Board. As the Joint Board explains, “[m]any areas of government enterprise operate within a budget, and we think that high-cost funding can do likewise.”<sup>13</sup> A cap would be the first step in getting the current program on a sustainable track, which must happen before the Commission seriously can consider whether, and how, to expand the program to support broadband services.

## **II. THE COMMISSION MUST ESTABLISH A PROCEDURE TO REVIEW SUPPORT LEVELS AS MARKETPLACE CONDITIONS CHANGE**

The Commission’s various universal service mechanisms are based on two key assumptions. First, each program assumes that certain customers or locations would not have affordable service available but for the support provided by the program. Second, each program is based on the assumption that the Commission can somehow identify when, and how much, support is needed.

When the Commission has developed programs that provide support to individuals, like Lifeline and Linkup, these assumptions generally have been accurate. The Lifeline and Linkup programs identify particular individuals that would not be able to afford service absent a subsidy and provide enough support so that a company can provide discounted services to those individuals.<sup>14</sup>

Programs that provide support to geographic areas, rather than individuals, like the high-cost fund, while achieving some of their goals, have not always done so in an efficient manner.

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<sup>13</sup> *Joint Board Recommended Decision* at ¶ 26.

<sup>14</sup> See 47 C.F.R. §§ 54.407 (reimbursement for offering Lifeline); 54.409 (consumer qualification for Lifeline).

As the Joint Board recognized, the current support mechanisms need to be updated to reflect the significant marketplace changes that have occurred since the USF program first was established. 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 changing conditions in the marketplace. In other words, there is no mechanism for revisiting the Commission's initial determination that market forces are inadequate to support the provision of affordable voice service in a particular location or identifying whether technology developments allow that service to be delivered more efficiently, perhaps by multiple providers.

Not only does the current program not reassess whether support is still needed, or whether it is needed at current levels, it actually includes features that lead to ever-increasing growth in the amount of support once competitive entry occurs. As competitors enter a market and win customers from the incumbent, the amount of per-line support provided to a rural LEC increases because of Commission rules that average all costs across the number of lines served.<sup>15</sup> As the Joint Board explained, "most of the existing mechanisms were introduced before local exchange competition became a reality, and may not appropriately adjust support to reflect line losses due to competition."<sup>16</sup> The increased amount of per-line support serves to attract

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<sup>15</sup> See *In the Matter of Federal-State Joint Board on Universal Service; Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Fourteenth Report And Order, Twenty-Second Order On Reconsideration, and Further Notice Of Proposed Rulemaking In CC Docket No. 96-45, and Report And Order In CC Docket No. 00-256, 16 FCC Rcd 11244, 11294-95, ¶ 125 (*MAG Order*) ("If the incumbent's lines decreased while its fixed costs remained roughly the same, its per-line costs would increase. Consequently, the incumbent would be entitled to higher support per line.").

<sup>16</sup> *Joint Board Recommended Decision* at ¶ 22.

additional CETC applications, which in turn results in further increases in per-line support. In short, the rules operate so that a competitor's market-based decision to serve a particular area not only fails to reduce the amount of the subsidy provided to the incumbent, but it actually creates an incentive for other providers to seek support.

Providing increased government support to areas benefiting from private investment and competitive entry is exactly the opposite of what should occur under a well-structured program. When circumstances have changed to the point where competitive entry becomes economic (generally without subsidy, because new entrants must build networks before they are able to qualify for support), the appropriate question should be whether, and by how much, to *decrease* support. But the current regime never asks that question and has no procedure by which it can be raised.

To address these problems, NCTA proposes that the Commission develop a procedure to reassess the amount of support made available to a particular location where there is evidence the market is working to make service available. Specifically, NCTA proposes three events that should, upon the request of a competitive provider, trigger a review of the amount of support that is distributed to a particular geographic area, including the possibility of eliminating support for all providers in the market.

**1. ILEC Deregulation.** As explained above, the premise underlying the high cost fund is that, absent financial support from the federal government, market forces would not be sufficient to ensure that affordable services are provided in the supported location. By contrast, when an ILEC seeks rate deregulation at the state level, a finding by a state commission that an ILEC's rates no longer need to be regulated is premised on the opposite conclusion, *i.e.*, that even in the absence of regulation, competitive market forces are sufficient to ensure that service

will be provided at reasonable rates. Where a state has made such a finding and deregulated local exchange service provided by the ILEC (whether provided on stand-alone basis or as part of a bundled offering), the fundamental premise for providing a government subsidy no longer exists and a process for reducing, and eventually eliminating, high cost support for all ETCs in the market (including the ILEC) should be initiated.

**2. ILEC Provision of Multichannel Video Service.** The Commission is not authorized to, nor does it, provide any financial support through the high-cost program (or any other program) for the provision of multichannel video service. Consequently, companies that receive USF support should not be able to use it to pay for facilities or equipment used in the provision of multichannel video service. But that is exactly what happens under the current rules when a LEC assigns the entire cost of fiber upgrades to subsidized voice service and then uses those facilities to provide video service at unregulated rates. As ILECs increasingly enter the multichannel video market, even in rural areas,<sup>17</sup> this should be an issue of significant concern to the Commission.

The introduction of multichannel video service by a LEC (or a LEC affiliate) is evidence that less support is needed by that provider to provide voice service and should trigger a reassessment of the amount of support a LEC receives. Such an approach 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.<sup>18</sup> There is no reason whatsoever that consumers should be subsidizing ILEC video services through the high-cost mechanism or in any other

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<sup>17</sup> For example, in reporting on a recent survey it conducted, the National Telecommunications Cooperative Association (NTCA) stated that 63 percent of respondents were providing video service by the end of 2006 and an additional 18 percent plan to do so by the end of 2008. NTCA 2007 Broadband/Internet Availability Survey Report (September 2007).

<sup>18</sup> *Joint Board Recommended Decision* at ¶ 31.

manner. At the very least, the Commission should ensure that ILECs allocate an appropriate portion of their costs to non-regulated services.

**3. Multiple CETCs.** The presence of multiple CETCs in a particular geographic area is evidence that the high cost program is not working as it should, or rather, that it is working harder than is necessary given marketplace developments. The *Notices* propose a variety of ways to potentially reduce the support that is provided to CETCs in this type of scenario. That certainly is a step in the right direction (if done in a competitively neutral manner, as we discuss below), but it fails to reflect fully the benefits of competition. Where multiple providers have invested in networks, the fundamental reason for providing USF support no longer exists and the Commission must look at how to reduce the total amount of government support that is made available, and eventually eliminate such support altogether for all providers in the area.

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As suggested above, when one of these three triggers is met, competitive providers should have the ability to request a review of the support situation in a given geographic area. Such a proceeding would give the agency conducting the review an opportunity to consider all the relevant facts as to how competition has developed in that area, the prices that competitors are charging for regulated and unregulated services, and the effect on all providers, and on consumers, if high-cost support were reduced or eliminated.

**III. THE COMMISSION SHOULD TAKE COMPETITIVELY NEUTRAL STEPS TO REDUCE SUPPORT IN AREAS SERVED BY MULTIPLE NETWORKS**

Under the Commission's current rules, a rural ILEC receives per-line support based on its embedded costs, and a CETC is entitled to receive per-line support based on the amount the ILEC would receive for serving the same customer if its support were calculated on a per-line

basis.<sup>19</sup> When it was adopted, the Commission found that this “identical support” rule was necessary to ensure that the high cost program would be competitively neutral.<sup>20</sup> Because the Commission’s rules do not distinguish between primary lines and secondary lines, CETCs are entitled to receive support for each line they serve, even in households with multiple lines.<sup>21</sup> At the same time, rural ILECs never experience support reductions for the loss of lines to competition.

In the *Identical Support Notice*, the Commission tentatively concludes that it “should eliminate the Commission’s current identical support rules” and that “a competitive ETC should receive high-cost support based on its own costs.”<sup>22</sup> NCTA agrees with the Commission that providing support to multiple carriers based on the ILEC’s embedded costs no longer makes sense. NCTA is concerned, however, with the myopic view the Commission takes as to the potential replacement mechanisms. Virtually every proposal advanced by the Commission consists of calculating support for CETCs based a CETC’s embedded costs.<sup>23</sup> And nowhere in the *Identical Support Notice* does the Commission even discuss the obvious question of whether it is time to move to a new methodology for calculating *ILEC* support.<sup>24</sup>

Where multiple carriers receive support, the amount of per-line support should be based on the *most efficient* provider, not the *least efficient* as it is today. In particular, in markets served by multiple networks, the Commission should move away from using ILEC embedded

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<sup>19</sup> *Identical Support Notice* at ¶ 3, citing 47 C.F.R. § 54.307(a).

<sup>20</sup> *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 8932, ¶ 287 (1997).

<sup>21</sup> *Id.* at 8828-30, ¶¶ 94-96.

<sup>22</sup> *Identical Support Notice* at ¶ 5.

<sup>23</sup> *Id.* at ¶¶ 13-25.

<sup>24</sup> In a footnote, the Commission notes that there are five open Joint Board referrals, some dating back as far as 2004, that address the issue of reform of the subsidy mechanisms for ILECs. *Id.* at ¶ 24 n. 58.

costs as the basis for calculating per-line support. As ILECs themselves acknowledge, rural ILEC networks are not the most efficient way to provide voice service in rural territories.<sup>25</sup>

There is no reason that the government should continue to provide funding at levels that exceed the amount that is absolutely necessary to ensure continued provision of service to any particular area.

To the extent the Commission's proposals in the *Identical Support Notice* continue to rely on embedded costs, they move in the wrong direction. As the Commission explained when it first established the USF program, "use of embedded cost to calculate universal service support would lead to subsidization of inefficient carriers at the expense of efficient carriers."<sup>26</sup> Moreover, in a market with multiple companies each providing supported and non-supported services, an embedded cost approach depends on totally arbitrary cost allocations among services. Finally, adopting an embedded cost approach for CETCs would be administratively burdensome, particularly if the Commission requires CETCs to comply with the Part 32 accounting rules that now apply only to ILECs. As the Commission recognized in a recent order addressing CLEC access charges, requiring competitive LECs to prepare cost studies would subject them to administratively burdensome legacy regulation.<sup>27</sup>

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<sup>25</sup> See, e.g., Comments of the Western Telecommunications Alliance at 24, WC Docket No. 05-337 (filed Oct. 12, 2006) (Rural ILECs "install and operate switches to serve study areas with relatively small numbers of access lines and are unable to generate significant economies of scale and scope with respect to their switching facilities. In contrast, many wireless CETCs employ a single switch (MTSO) to serve multiple urban and rural license areas in one or more states. They are not subject to the same inability to realize significant switching economies as are rural ILECs.").

<sup>26</sup> See, e.g., *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order, 12 FCC Rcd 8776, 8901, ¶ 228 (1997). Similarly, the Commission has found that "contrary to assertions by some incumbent LECs, regulation does not and should not guarantee full recovery of their embedded costs." *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, 11 FCC Rcd 15499, 15858, ¶ 706 (1996).

<sup>27</sup> *Access Charge Reform*, CC Docket No. 96-262, Order, 23 FCC Rcd 2556, 2561 ¶ 14 (2008).

Rather than expanding the use of embedded cost studies, the efforts of the Commission and the affected companies would be better spent considering alternative approaches. The proposals suggested below all move away from providing support to multiple providers based on the ILEC's embedded costs without abandoning the underlying principle of competitive neutrality that should be at the core of the federal USF program.

First and foremost, the Commission should cap per-line support at current levels for *all* providers serving a particular geographic area. Advances in technology continually have reduced the cost of providing voice service and there is no reason why any provider should receive an increasing amount of support for providing the same level of service. A cap would also control escalating per-line support in markets where ILECs are losing lines to CETCs. As noted above, the current regime insulates rural LECs from the effects of competition because they never experience support reductions when they lose lines. By the same token, because the ILEC's average support per-line rises, CETCs also experience per-line support increases as ILECs lose lines.

The Rural Task Force proposed such a cap for exactly the same reasons back in 2000, but the Commission did not adopt the proposal because it found that “the possibility of excess fund growth is speculative.”<sup>28</sup> Whatever merit that conclusion had when the Commission adopted it, seven years later there is nothing “speculative” about the explosive growth of the high-cost fund. It is long past time for the Commission to move to a more pro-competitive policy in which per-line support levels for all networks, regardless of technology, are capped.

The Commission also should limit support for any particular carrier to two lines per residential household. Presumably there are efficiencies associated with providing multiple lines

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<sup>28</sup> *MAG Order*, 16 FCC Rcd at 11295, ¶ 126.

to a single customer. Even if a provider can demonstrate that a subsidy is needed to provide affordable service to a customer in a high cost area, affordability cannot be much of a concern when it sells three or more lines to a single household. Like the cap on per-line support proposed above, this proposal is competitively neutral in that it applies the same rule to all providers, regardless of technology.

With these caps in place, growth of the fund would be constrained even if the Commission made no other changes in how the amount of support is calculated. But NCTA encourages the Commission to take a more aggressive approach by incorporating an assessment of affordability and reasonable comparability into its calculations as required by the statute.<sup>29</sup> Specifically, rather than basing its support calculations solely on an assessment of the carrier's costs for provisioning local service, the Commission should incorporate an assessment of what service rates the customer is charged.

In making such an assessment, the Commission would appropriately consider that customers rarely pay for standalone local service, but instead, pay a single rate for a bundle of services. In this changed marketplace, where wireline and wireless carriers routinely offer packages of unlimited local and long distance service, there is no reason the Commission should base its calculations on the assumption that a customer only is purchasing local exchange service. The Commission should assess whether revisiting the benchmark calculation to reflect the reality of the marketplace is an approach that would help bring the level of support to more efficient levels.

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<sup>29</sup> 47 U.S.C. §§ 254(b)(1), 254(b)(3).

#### **IV. PROPERLY STRUCTURED REVERSE AUCTIONS WOULD REDUCE SUPPORT TO MORE EFFICIENT LEVELS**

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In the *Reverse Auctions Notice*, the Commission again seeks comment on the use of reverse auctions as a mechanism for distributing high-cost support. In a reverse auction, the amount of support generally would be determined by the lowest bid to serve the auctioned area. The Commission tentatively concludes that reverse auctions “offer several potential advantages over the current high-cost support mechanisms” and it seeks comment on a number of issues regarding when auctions should be used and how they should be structured.<sup>30</sup>

NCTA consistently has supported the concept of using reverse auctions as a possible mechanism for distributing high-cost support.<sup>31</sup> If properly structured, auctions provide a mechanism through which the amount of support provided to competitive areas can be reduced to more efficient levels. In particular, a properly structured auction mechanism eliminates the need for the Commission to determine the cost of serving a particular area and the amount of support that is needed, and instead relies on the market to make such determinations.

While auctions appear to have many theoretical benefits over other distribution mechanisms, NCTA encourages the Commission to consider reverse auctions as a complement to, not a replacement for, other steps to control the size of the high cost fund, such as capping the amount of per-line support and the number of supported lines. Because 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.<sup>32</sup> In contrast, caps on per-line support and the number of

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<sup>30</sup> *Reverse Auctions Notice* at ¶ 1.

<sup>31</sup> See Comments of the National Cable & Telecommunications Association, WC Docket No. 05-337 (filed Oct. 10, 2006) (NCTA Comments).

<sup>32</sup> For that reason, the Commission’s proposal to conduct a pilot program is a sound one. *Reverse Auctions Notice* at ¶ 50.

supported lines can be implemented far more quickly and therefore they can provide a more direct and immediate response to the problems plaguing the existing high-cost support system.

As NCTA explained in its earlier comments, the structure of any auction system is critical if it is to achieve its intended goals. For example, it is important that the Commission use relatively small geographic areas, such as census block groups (CBGs), as the basis for distributing support. The use of a small service area is competitively and technologically neutral because it does not conform to the boundaries of any particular type of service provider, nor is it defined by the use of any particular technology.

The Commission should not use ILEC study areas as the basis for auctions as it has proposed in the *Reverse Auctions Notice*.<sup>33</sup> The Commission itself already has identified the fatal flaw in using ILEC study areas: “Basing the geographic area on any particular carrier’s service area would likely give that carrier an advantage in bidding because competing carriers are unlikely to have the same service footprint.”<sup>34</sup> Given this acknowledgement of the discriminatory effect of using ILEC study areas, the Commission must make a different choice.<sup>35</sup>

Some concerns have been raised that the winner of an auction might bid “too low” and be forced to raise retail rates and/or cut back on the quality of service.<sup>36</sup> To the extent that auctions are used to distribute money from the Broadband or Mobility Funds discussed below, that concern can be addressed by limiting funding to unserved areas. By definition there can be no diminution of service quality in an area that previously had no service. If necessary, rate

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<sup>33</sup> *Id.* at ¶ 21.

<sup>34</sup> *Id.* at ¶ 19.

<sup>35</sup> In previous comments, NCTA identified a number of other elements that should be part of an auction regime, including minimum service requirements, continued application of interconnection obligations, and elimination of any guaranteed support to incumbents. *See* NCTA Comments at 5-6.

<sup>36</sup> *Reverse Auctions Notice*, Statement of Commissioner Michael Copps, Approving in Part, Dissenting in Part.

concerns can be addressed by conditioning the grant of such funding on a requirement to offer service at or below a particular rate. Similar conditions on the receipt of funding also would address concerns about high rates or low service quality if auctions are used to distribute funding for voice services.

**V. STRUCTURAL CHANGES TO THE FUND ONLY SHOULD BE IMPLEMENTED AFTER THE COMMISSION TAKES STEPS TO CURB THE GROWTH OF THE FUND**

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**A. Summary of Joint Board Recommendation**

In addition to proposing to eliminate the identical support rule and implement reverse auctions, the Commission also seeks comment on a Joint Board recommendation to restructure the high cost fund into three separate funding mechanisms – a POLR Fund, a Mobility Fund, and a Broadband Fund. The Broadband Fund would be “tasked primarily with disseminating broadband Internet services to unserved areas, with the support being expended as grants for the construction of new facilities.”<sup>37</sup> Similarly, the Mobility Fund “would be tasked primarily with disseminating wireless voice services to unserved areas” and “support would be expended as subsidies for construction of new facilities.”<sup>38</sup> In both cases, funding would be made available on a “project-by-project basis” by the states pursuant to standards established by the Commission.<sup>39</sup> The Joint Board recommends that, at least on an interim basis, the new Mobility and Broadband mechanisms would be funded through “savings” that result from other changes that have been proposed, such as eliminating the identical support rule.<sup>40</sup>

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<sup>37</sup> *Joint Board Recommended Decision* at ¶ 12.

<sup>38</sup> *Id.* at ¶ 16.

<sup>39</sup> *Id.* at ¶¶ 14-15, 17-18.

<sup>40</sup> *Id.* at ¶ 27.

The POLR Fund would not be a new fund, but instead would be “comprised of the sum of all existing Incumbent LEC support mechanisms.” The Joint Board does not recommend any specific changes to these mechanisms, but it encourages the Commission to “establish a process and a timetable so that it will review and modernize the existing high-cost mechanisms for rural and non-rural carriers, with the objective of developing a coherent system that can be applied to all incumbent carriers.”<sup>41</sup>

**B. The Proposed POLR Fund Does Not Go Far Enough In Reflecting the Benefits of Competition**

The Joint Board appropriately recognizes that separating the current mechanism into three distinct funds will not, without more, solve the problems plaguing the current program.<sup>42</sup> Unfortunately, the Joint Board has not gone far enough in reflecting the benefits of competition in its proposal to establish a POLR Fund. In particular, NCTA cannot support a proposal that would indefinitely award support only to incumbent providers. In markets already served by multiple providers, such an approach patently violates the principle of competitive neutrality. If the Commission is going to subsidize a monopolist, which is essentially what the Joint Board has proposed, it cannot do so in markets where alternative providers already are operating or planning to operate.

Moreover, while there undoubtedly are areas where no competition exists today, advancements in technology and changes in demographics mean that no area should be consigned to a single provider on a permanent basis. This potential for material changes in marketplace conditions is the basis for NCTA’s proposal above that the Commission establish a mechanism to reassess support levels in a particular geographic area when such changes occur.

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<sup>41</sup> *Id.* at ¶ 23.

<sup>42</sup> *Id.* at ¶ 22 (“The current high-cost universal service mechanisms are dated and need to be modernized in several ways.”).

Such a mechanism would be especially critical if support only were made available to the incumbent provider.

**C. Broadband and Mobility Support Only Should Be Made Available For Construction of Networks In Unserved Areas**

As with its proposal to cap the overall size of the high-cost mechanism, the Joint Board's proposal to limit the size of the new Broadband and Mobility Funds to the savings produced from changing the existing fund is a welcome dose of fiscal responsibility. While the Commission ultimately should move to a regime in which increased competition and efficiency result in savings to consumers (in the form of reduced contributions), the use of any savings to support other universal service goals on an interim basis is not objectionable.

With respect to the Mobility Fund, for example, replacing support for multiple wireless providers in heavily served areas with support to unserved areas certainly is a step in the right direction. It is important, however, that the Commission not just redirect money from one set of pockets to another, but that it also implement mechanisms to ensure that support is provided only to the extent that it is absolutely necessary to provide service in areas where it otherwise would not be economic to provide affordable service. Thus, support from the Mobility Fund should be available only for the purpose of building facilities where none exist today and that support should be awarded through reverse auctions or some other bidding mechanism that will produce the most efficient approach to building those facilities.

With respect to the proposed Broadband Fund, NCTA generally opposes expansion of the high-cost fund to include broadband services because the market (supplemented by the existing high-cost mechanism) already is working to meet the needs of consumers. As the Commission

recently found in its Fifth Report to Congress under Section 706 of the 1996 Act, broadband service is being made available to all Americans on a reasonable and timely basis.<sup>43</sup>

Although the marketplace generally is working to meet the need for broadband, NCTA recognizes that there are still remote rural areas across the United States that lack access to terrestrial broadband service. Any future federal initiatives to promote ubiquitous broadband availability should carefully target these unserved areas of the country. Obviously no financial support should be provided under such a program until the Commission is able to identify such unserved areas. Its recent order adopting new broadband reporting requirements will help accomplish that objective.<sup>44</sup> Until reports based on that new data are available, however, no new broadband funding should be provided to any company.

In addition to making support available only to unserved areas, the Commission also should establish a presumption that rural LECs receiving support from the existing high-cost fund (or from the proposed POLR Fund, if adopted), would not be eligible to receive additional funding from the Broadband Fund for the same geographic area. Although broadband is not on the current list of supported services, federal high-cost support can be used to add fiber optics to LEC networks, which facilitates the provision of DSL service. As the Joint Board observed, “a significant portion of the High Cost Loop fund supports the capital costs of providing broadband-capable loop facilities for rural carriers.”<sup>45</sup>

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<sup>43</sup> See News Release, *FCC Expands, Improves Broadband Data Collection* (Mar. 19, 2008) (“Separately, the FCC today adopted a report showing that broadband services are currently being deployed to all Americans in a reasonable and timely fashion. The Fifth Report to Congress on broadband deployment under Section 706 of the Telecommunications Act of 1996 finds that there have been considerable changes and advances in the delivery of broadband-based services and applications since the Fourth Report.”).

<sup>44</sup> *Id.* (“An Order adopted by the Federal Communications Commission today will increase the precision and quality of broadband subscribership data collected every six months from broadband services providers. Improvements include collecting detailed subscribership information on a local level and more detailed information about the speed of broadband service.”).

<sup>45</sup> *Joint Board Recommended Decision* at ¶ 30.

Aided by a steady stream of government USF subsidies, most ILECs have been able to upgrade their networks to provide broadband services. For example, the National Telecommunications Cooperative Association (NTCA) reported that, in a 2007 survey of its members, 99 percent of respondents were providing broadband service to some portion of their service areas.<sup>46</sup> The rapid growth of broadband in rural areas under the current system makes clear that, in most areas, there is absolutely no need for additional government funding above and beyond the substantial amounts that ILECs already receive through the current high-cost support program.

Once areas are identified that are eligible for support from the Broadband Fund, funding should be made available on a project-by-project basis through reverse auctions or some other mechanism that would ensure that it is used efficiently and effectively. As proposed in the *Joint Board Recommended Decision*, support should consist of one-time grants for network construction, not ongoing funding for corporate overhead, except in extreme cases where the absence of ongoing support is essential to attract investment. Any entity using any technology should be able to bid. Allowing the widest possible pool of bidders will ensure that the service is provided through the most efficient technology, at the lowest cost to American consumers.

It may be appropriate for states to play a role in distributing any broadband funding, as suggested by the Joint Board. State commissions are more familiar with the situation on the ground and in many cases they have been actively involved in efforts to measure and promote the deployment of broadband networks. States also will be able to ensure that subsidies are not provided to companies for investments that they already have committed to provide in exchange

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<sup>46</sup> NTCA 2007 Broadband/Internet Availability Survey Report (September 2007). As noted above, the majority of these companies also are offering video services. *Id.* at 12 (63 percent of respondents were offering video services by the end of 2006 and an additional 18 percent plan to do so by the end of 2008).

for other regulatory benefits. If a LEC has promised to introduce broadband services in high cost areas of a state in exchange for approval of a corporate transaction or deregulation of its retail services, there is no reason those broadband services should be subsidized by the federal government. For example, as part of the recent transfer of assets from Verizon New England to FairPoint Communications, FairPoint agreed to expand DSL availability to reach 82% “addressability” of Maine access lines within two years of the closing of the transaction and 90% addressability in no more than six years.<sup>47</sup> In Vermont, as part of an amended Incentive Regulation Plan, Verizon agreed to yearly milestones for broadband availability; 65% of lines qualified, by year-end 2007, 75% by year-end 2008, 77% of lines qualified by year-end 2009, and 80% of lines qualified by year-end 2010.<sup>48</sup> In both cases, having the federal government provide support for these broadband services would be tantamount to double payment to the ILEC, which already has received a benefit from the state.<sup>49</sup>

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<sup>47</sup> See *Verizon New England Inc., et al, re: Joint Application for Approvals Related to Verizon’s Transfer of Property and Customer Relations to Company to be Merged with and into FairPoint Communications, Inc.*, Maine Public Utilities Commission, Docket No. 2007-67, at 17 (rel. Feb. 1, 2008).

<sup>48</sup> See *Investigation into a Successor Incentive Regulation Plan for Verizon New England Inc., d/b/a Verizon Vermont*, Vermont Public Service Board, Docket No. 6959, Order, Appendix A at 5 (rel. Apr. 27, 2006).

<sup>49</sup> The same is true for commitments made to the FCC. AT&T, for example, committed to provide broadband service to all its customers as a condition of receiving Commission approval for its acquisition of BellSouth, and it should not be able to collect federal support to help it comply with that obligation. *AT&T Inc. and BellSouth Corp. Application for Transfer of Control*, WC Docket No. 06-74, Memorandum Opinion and Order, 22 FCC Rcd 5662, Appendix F (2007) (committing to offer broadband Internet access to 100 percent of residential living units in AT&T/BellSouth in-region territory).

## CONCLUSION

For all the reasons explained above, NCTA encourages the Commission to take steps to reduce the size of the Universal Service Fund. In particular, the Commission should: (1) adopt a cap on the overall size of the high-cost fund; (2) establish procedures to reassess the need for support when marketplace conditions have changed; and (3) take competitively neutral steps to limit the amount of support in markets with multiple providers, such as capping the amount of per-line support and the number of supported lines for all providers.

Respectfully submitted,

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April 17, 2008