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Federal Communications Commission
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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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In the Matter of	)	
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Federal-State Joint Board on Universal Service	)	**CC Docket No. 96-45**
	)	

REPLY COMMENTS OF AT&T CORP.

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SUMMARY

As the comments indicate, there is nearly unanimous support for the Joint Board's efforts to reform fundamentally the universal service system, and the commenters endorse many of the key proposals contained in the Recommended Decision. These include measures suggested to ensure the competitive neutrality of universal service funding, the decision to base high cost support on forward-looking costs, and the recommendation that USF subsidies be fully portable, extending to those carriers providing service through unbundled network elements. By making only a few modifications to the Joint Board's specific proposals, the Commission can establish a sound, efficient, and competitively neutral universal service support system.

The comments likewise reflect general agreement about the proper operation of the high cost fund. First, strong support has emerged for basing USF contributions on both intrastate and interstate revenues. This broad base would not only reduce the size of any surcharge, but would also minimize the burden on high cost states that would otherwise be required to make up the difference through their own state USFs. Including intrastate revenues will also avoid the regulatory difficulties certain to arise as some carriers attempt improperly to shift revenues from interstate to intrastate offerings and thereby avoid federal USF contributions. The Commission, as many commenters demonstrate, clearly has statutory authority to base contributions to the USF on total revenues.

Second, commenters almost uniformly advocate an end-user, retail surcharge as the best means of collecting USF support. A retail surcharge will promote competitive neutrality by applying equally to customers of all carriers and preventing strategic cost

allocations to avoid USF contributions. Also, the public visibility and ease of administering this fee will aid in maintaining control of the fund's size. Because the Act permits a mandatory end user surcharge and customers will ultimately bear the universal service support costs regardless of how they are assessed, the Commission should follow the advice of almost every participant in this proceeding and specify the recovery of universal service support directly from end users in the form of a separate line-item on the end user bill. If the Commission decides, however, to adopt the Joint Board's recommendation to levy the surcharge on a carrier's gross revenues net of payments to other carriers, it should require carriers to recover their obligation equiproportionally from all services.

Third, there is little support in the comments for use of a competitive bidding system in lieu of a proxy model to determine support levels in high cost areas. Such a scheme undermines competition by unnecessarily restricting entry. Coupled with the administrative complexities inherent in conducting numerous auctions nationwide, any potential benefits of a competitive bidding system are far outweighed by its disadvantages.

Fourth, there is widespread consensus for rejecting the Joint Board's proposed benchmark methodology. Instead of nationwide average revenue per line, most comments endorse a system that includes in the benchmark only revenues or costs associated with providing universal service. This methodology would permit the Commission to manage the overall size of the fund and to eliminate impermissible implicit subsidies.

Fifth, there is general agreement with the Joint Board's conclusion that carriers providing service through UNEs qualify for full universal service support under Section

214(e)(1). Not only should the Commission affirm the Board's recommendation, it should also promulgate a rule requiring states to define carriers' service areas as coterminous with those areas where the carriers offer and price unbundled network elements. While state commissions have the ultimate authority to define USF areas, if they fail to define them in this manner they will contravene the prohibitions against barriers to entry in Section 253. To avoid uneconomic arbitrage or barriers to competition, it is also vital that the costs of universal service be calculated consistent with the cost of unbundled network elements. In addition, while a few commenters have suggested that eligibility for universal service subsidies should be predicated on assuming carrier of last resort obligations, Section 214(e) expressly sets forth the relevant statutory duties. Those obligations are quite clear and there is no reason for the Commission to impose additional requirements.

Almost every commenter also agrees that modifications to the SLC and CCLC should be referred to the Commission's access proceeding. The comments establish that there is no evidence or valid universal service objective which would justify reducing the SLC. Moreover, to the extent the Commission decides to modify the CCLC in this docket, it should be eliminated entirely because it constitutes an impermissible cross-subsidy and barrier to effective competition.

Finally, with respect to the appropriate method of determining costs for the high cost fund, there is broad support in the comments for use of a forward-looking cost proxy model. The Hatfield Model has already demonstrated its superiority for these purposes,

and despite premature attacks by some ILECs, the newest version of the Hatfield Model will continue to be the best forward-looking economic cost model.

In addition to the broad consensus regarding operation of the high cost fund, the comments also provide ample support for the Commission to take steps that would maintain control of the overall cost of the universal service system. These include rejecting the Joint Board's recommendation that the Lifeline and Link-Up programs' baseline support be increased to $5.25. The comments also unambiguously indicate that industry participants favor controlling the size of subsidies to schools, libraries, and rural health care providers. While AT&T and others support assistance to these institutions, they also widely agree that support should be limited to telecommunications services.

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REPLY COMMENTS OF AT&T CORP.

Pursuant to the Commission's November 18, 1996 Public Notice ("Public Notice"), AT&T Corp. ("AT&T") hereby submits these reply comments on the Federal-State Joint Board's Recommended Decision ("RD"), released November 8, 1996, regarding implementation of the universal service provisions of the Telecommunications Act of 1996 ("Act").[1]

INTRODUCTION

The comments filed with the Commission reflect broad approval of the Joint Board's recommendations for fundamental reform of the entire universal service system. AT&T generally agrees with these comments and with the Board's efforts to adopt a set of reforms that achieve the Act's objective of providing and funding universal service in a competitively neutral manner.

The commenters endorse many of the Board's key proposals. For example, the vast majority of commenters support the Board's explicit recognition of competitive neutrality

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[1] The Commission opened this proceeding with a notice of proposed rulemaking soliciting comments on how the universal service provisions of the Act should be implemented. Federal-State Joint Board on Universal Service, Notice of Proposed Rulemaking and Order Establishing Joint Board, CC Docket No. 96-45, FCC 96-93 (released March 8, 1996) ("NPRM").

as a fundamental principle of universal service policy pursuant to Section 254(b)(7). RD at ¶ 23. The comments also generally affirm the Board's decision to base high cost support on the forward-looking, economic cost of providing service. To that end, the Board recommended that costs be determined through a forward-looking proxy model and compared against a national benchmark "affordable rate." See RD at ¶¶ 268, 275. These aspects of the Joint Board's methodology have also met with widespread approval. Commenters also overwhelmingly agree that universal service subsidies must be fully portable, following the customer rather than the carrier. With few exceptions, the commenters agree that any carrier meeting the criteria set forth in Section 214(e) should be eligible to receive full universal service support including those providing the supported services using unbundled network elements. As the Board stated, this approach "best embodies the pro-competitive, de-regulatory spirit of the 1996 Act and ensures the preservation and advancement of universal service." RD at ¶ 155.

In light of the overwhelming support for the broad outlines of the Board's proposals, AT&T urges the Commission to adopt the Board's suggested framework and many of its specific recommendations. Indeed, by making only a few modifications -- all advocated by a broad range of participants in this proceeding -- the Commission will establish a sound, efficient, and competitively neutral universal service support system.

As explained in Section I, there is broad consensus on additional steps the Commission should take to ensure the competitive neutrality of the high cost fund. Most importantly, as most commenters urge, intrastate revenues should be included along with

interstate revenues in determining federal USF support obligations, and universal service contributions should be collected through an end-user retail surcharge. As explained in Section II, the Commission should also adopt certain widely endorsed measures to control the overall cost of the USF with respect to low-income support and aid to schools, libraries, and rural health care providers. Finally, Section III discusses the commenters' universal endorsement of a neutral administrator.

I. THE COMMENTS REFLECT GENERAL AGREEMENT ABOUT THE PROPER OPERATION OF THE HIGH COST FUND.

Like AT&T, the vast majority of commenters endorse the Joint Board's express recognition that the universal service system must be competitively neutral if it is to fulfill the objectives, and satisfy the requirements, of the 1996 Act. However, the comments also reveal widespread agreement that the Joint Board's proposals require certain modifications to ensure the competitive neutrality of high cost universal service support.

A. The Commenters Support Basing Contributions To The Federal USF On Interstate and Intrastate Revenues.

For example, there is widespread support among the commenters -- including many LECs -- for requiring contributions to the federal USF to be based on both interstate and intrastate revenues. Indeed, a number of commenters acknowledge that competitive neutrality demands that the contribution base be total revenues.

Most commenters echo the concerns AT&T raised in its Comments. For example, the commenters recognize that the statute permits the Commission to establish a "nonjurisdictional" USF, to be funded through an assessment on the total retail revenues

of interstate carriers. See U S WEST at 16-17; GTE at 66-67; Pacific at 23-24. Many commenters also note the importance of broadening the contribution base, so that the surcharge can be smaller. See U S WEST at 24; GTE at 67. In that regard, USTA (at 17-18) agrees that a smaller contribution base will merely require states with the most high cost areas -- i.e., the states in most need of help -- to make up the difference through their own state USFs. In addition, many commenters note that limiting the contribution base to interstate revenues would not be "practical" because of the resulting incentives to try to avoid federal universal service obligations by structuring service offerings as intrastate offerings. USTA at 17; see also BellSouth at 10-11; GTE at 68; U S WEST at 19-20.

A handful of state commissions, however, argue that the Commission has no statutory authority to establish total revenues as the contribution base.[2] Although AT&T (at 6-7) demonstrated in its Comments that the statute's language and structure clearly authorize a total revenue approach, two points bear mentioning.

First, the new universal service system that Congress established in Section 254 inherently transcends traditional jurisdictional distinctions. Contrary to the apparent belief of some commenters, federal universal service obligations are not analogous to interstate "charges" that are designed to recover the interstate "costs" of universal service.[3] Indeed,

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[2] See Ohio PUC at 20-25; Md. PSC at 10-18; California PUC at 16-19. The public utility commissions of Texas and Vermont, however, support total revenues as the contribution base. See Texas PUC at 12-13; Vermont Pub. Serv. Bd. at 1-11.

[3] See, e.g., Md. PSC at 17 ("Applying the federal surcharge to intrastate revenues will unfairly shift most of the burden of funding interstate universal service to local telephone rates."); Ameritech at 33 (federal fund should subsidize only interstate costs).

it is undisputed that the federal USF will subsidize primarily the costs of providing intrastate services. See RD, ¶ 822. Congress expressly required that contributions to the federal USF be "equitable and nondiscriminatory" and "sufficient" to "preserve and advance universal service," all of which belie any notion that Congress intended the federal fund to be limited to the interstate aspects of universal service. That is why Section 254 places no limitations on the revenues that can constitute the base of support for the federal USF.[4]

Second, assessing the federal obligations on total revenues would not impinge upon the authority of the states. Congress has maintained the states' role in preserving universal service in Section 254(f), which expressly permits the states to adopt complementary state USFs to ensure whatever level of universal service support a state deems appropriate. Indeed, most states are likely to establish such funds, which means that the states, not the FCC, will effectively be establishing policy concerning the services and affordability levels that are to be subsidized by the universal service system.[5] A broader base of support for the federal USF can only *help* the states in achieving their goals, by reducing the need for

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[4] That is also why AT&T Communications of the Mountain States, Inc. v. Pub. Serv. Comm., 625 F. Supp. 1204 (D. Wyo. 1985), cited by some commenters, is inapplicable. See, e.g., Ohio PUC at 22; Md. PSC at 16 n.24; see also Separate Statement of Commissioner McClure at 2-3. The AT&T case dealt with services provided by a LEC to IXCs, and therefore separating those services into their interstate and intrastate components, with a separate rate for each, was appropriate. Universal service support obligations are not rates for services, but rather constitute an inherently nonjurisdictional subsidy system. As such, the establishment of the USF is subject to the express standards of Section 254, and not to the quite different separations process outlined in Sections 221 and 152(b). See, e.g., NARUC v. FCC, 746 F.2d 1492 (D.C. Cir. 1984).

[5] Section 254(f) also allows states to support individual state USFs using total revenues, including interstate revenues, billed in the state. See, e.g., USTA at 18; U S WEST at 18; BellSouth at 14.

larger state USFs that must be funded solely by those states' own consumers. See USTA at 17-18.

B. There Is Nearly Unanimous Support For The Proposition That Universal Service Should Be Funded Through a Retail Surcharge On End Users' Bills.

The comments likewise reflect nearly unanimous support for the view that universal service should be funded through a retail surcharge on end users' bills. The Joint Board recommended against requiring universal service support to be reflected on the end user bill as a surcharge, though it did not prohibit carriers from separately stating the costs of universal service support on customer bills. RD at ¶ 812. Echoing the position of nearly every set of comments on the USF funding mechanism, however, BellSouth (at iii) correctly asserts that the "best approach to recovery [of Universal Service costs] is for the Commission to fix the recovery mechanism by establishing an end user surcharge to be applied in a similar manner by all contributing carriers."[6]

First, as U S WEST (at 45) points out, "[u]nless the USF assessment is specifically identified on the end user's bill, it would not comply with the Act and would not be competitively neutral." According to BellSouth (at iii), a "mandatory surcharge would be consistent with the principle of competitive neutrality because the contributions of all carriers would be recovered in precisely the same manner." And SBC (at 11) argues that "[a]t a minimum competitive neutrality and the need to make universal service funding

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[6] See also USTA at 22; U S WEST at 45; MFS at 12; NYNEX at 23 (carriers should be allowed to assess an end-user surcharge on interstate services); California at 13; Bell Atlantic at 8-9; Ameritech at 30-31.

explicit demand that the Commission mandate that all universal service funding. . . be passed-through by all providers to customers in the form of an explicit, mandatory surcharge." An explicit, visible retail surcharge best ensures that carriers recover the cost of universal service proportionately across all of their services; otherwise, a carrier could strategically allocate the cost of the subsidy among its various services to the disadvantage of consumers and competitors. See AT&T at 8-9.

Second, an explicit surcharge will have the added benefit of enabling regulators to prevent the subsidy from spinning out of control in the future (NPRM at ¶ 28) principally by creating public pressure to keep overall subsidy levels in check. In addition, a retail surcharge will further facilitate regulatory oversight because it is "simple to calculate and easy to administer." BellSouth at 16.

Finally, the commenters almost universally reject the Board's recommendation that contributions should be based on carriers' gross revenues net of payments to other carriers. See Bell Atlantic at 3; SBC at 14-15; BellSouth at 11; NYNEX at 4; U S WEST at 43; GTE at 33; USTA at 15-16; CBT at 4; Citizens Utilities at 29. By failing to address how carriers would recover their obligations from customers, the Board's approach could allow carriers improperly to recover their USF support obligations disproportionately from different customer segments. As a result, "[t]he recommended use of a carrier's gross telecommunications revenues net payments to other carriers as the basis for determining a carrier's funding contributions . . . will effectively discriminate against classes of carriers." SBC at 14-15. A retail revenue assessment, by contrast, will guarantee that all subscribers

make a fair and equitable contribution on exactly the same basis. AT&T at 9; see also USTA at 16; U S WEST at 46; CompTel at ii. High volume users will also bear their proportionate share of the universal service obligation.

In all events, the comments support the view that, even if the Commission adopts the Joint Board's recommendation that USF support be assessed against carriers' gross telecommunications revenues net of payments to other carriers (RD ¶¶ 807-12), the Commission should at a minimum require each carrier's obligation to be collected equiproportionally across all its services and reflected as a line-item on the services bill.[7]

C. There Is No Support In The Record For A Competitive Bidding System To Determine The Levels Of High Cost Support.

Another key issue addressed by the comments concerns the mechanism by which to determine the appropriate level of high cost support. The Joint Board properly recommended that universal service support levels for high cost areas be determined on the basis of forward-looking economic cost, and that a proxy model be developed to estimate those costs. RD, ¶¶ 268-69. While there is some debate about which proxy model is appropriate, the commenters broadly support that basic approach.

By contrast, there is virtually no support among the commenters for using a competitive bidding scheme, instead of a proxy model, to determine support levels in high cost areas for universal service purposes. Although the Joint Board recommended that the Commission "explore the possibility" of using a competitive bidding scheme (RD, ¶ 341),

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[7] Indeed, NYNEX (at 23) supports allowing carriers to assess an end-user surcharge when only interstate revenues are included in the basis for USF support.

and GTE and Citizens for a Sound Economy have each proposed such a scheme, they are almost alone in arguing for the adoption of competitive bidding. GTE at 59-66; Citizens for a Sound Economy at 8-10. Indeed, a competitive bidding system would harm the development of competition, and should be rejected for several reasons.

First, a competitive bidding scheme would necessarily act as a barrier to entry. In contrast to most auctions, in which the winner gains exclusive use of an asset or exclusive access to a particular market, the level of support determined in a universal service "auction" would have to be made available nonexclusively to all carriers operating in the market. This basic fact, which is inherent in all universal service auction proposals, means that no carrier has any incentive to participate or to win unless there is some "bonus" for participating and winning. Without such a bonus -- and none of the bidding schemes offer any -- the only carrier with any incentive to participate would be the incumbent.

Moreover, under GTE's proposal, carriers *must* participate in an auction to be eligible for support. This is an even more blatant barrier to entry, and would impose needless administrative burdens and costs on any carrier wishing to enter a market. Similarly, GTE's proposal to limit the subsidy to carriers that bid within a certain range of the winning bid would merely deny certain carriers any opportunity to enter that market. All of these proposals would confer an artificial competitive advantage on certain carriers. The proxy model approach has none of these defects.

Competitive bidding would also be an administrative nightmare. Conducting auctions for high cost areas throughout the nation would be a far more complex process

than the proxy model approach, and would be costly for both regulators and the participating carriers. For all of its administrative complexity and cost, moreover, a competitive bidding scheme would offer few benefits. Under the proxy model approach, any carrier would be free to enter the market at any time, receive the subsidy, and compete with existing carriers to provide service at lower cost and better quality. Customers would have unfettered choice of carriers, and could thus garner all the benefits of competition. A competitive bidding system, by contrast, might change slightly the *size* of the subsidy, but would also create serious competitive distortions and disincentives to enter.

D. There Is Widespread Consensus That The Joint Board's Recommendation For The National Benchmark Should Be Rejected.

Many comments also addressed the issue of how to determine the national benchmark. Indeed, a consensus has emerged that "the Commission should consider only those revenues that are directly caused by the customer's decisions to subscribe to basic local service." GTE at 25; See also BellSouth at 6, n. 14; Citizens Companies at 26; AT&T Comments to the Joint Board at 12-16. The commenters generally agree that the Board's proposed national benchmark, which includes access revenues, may violate the Act by promoting impermissible implicit subsidies. Unlike basic local service revenues, access revenues are not generated by the customer's decision to subscribe to the supported service; indeed, they result from a long distance customer's decision to make toll calls. Thus, inclusion of access revenues in the benchmark constitutes an implicit cross-subsidy.[8]

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[8] As AT&T will show in the Commission's access reform proceeding (CC Docket 96-262), all access revenue in excess of the forward-looking cost of providing access services should (continued...)

Like AT&T, "USTA strongly opposes a benchmark based on nationwide average revenue per line "which only serves to maintain the implicit support of the current system..." USTA at 10-11. Similarly, the California Small Business Administration (at 4) rejects the Joint Board's suggested methodology because it would result in "precisely the type of non-specific implicit subsidy that section 254 and this proceeding were intended to eliminate." Other carriers have reached similar conclusions.[9] Thus, the Commission should reject the Joint Board's recommendation and adopt a benchmark that includes just those revenues associated with providing universal service -- such as the benchmark methodology proposed by GTE (at 51-56).

The benchmark, moreover, should be stable. If it is changed frequently, it may cause undue fluctuation in USF support levels and "require more regulatory oversight and review to ensure an appropriately sized fund. . . ." U S WEST at 30.

The proper benchmark should also not result in an increase in the overall size of the fund. Thus, MFS (at 24-25) correctly rejects the national average revenue basis for the benchmark on the ground that "competition will increase the high cost fund rather than reduce it," and "raise[] administrative costs and churn among the included services." The fund's size will increase because, "[a]s competition develops in all segments of the local exchange market, that will reduce prices," thereby reducing average per-line revenues and,

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[8] (...continued)
be eliminated. Thus, there should not be any excess access revenue available to be used in establishing the benchmark.

[9] See MCI at 9; Citizens Companies at 26; BellSouth at 6; MFS at 24; GTE at 19-20; SBC at 34; U S WEST at 28; CBT at 9.

in turn, reducing the national benchmark. MFS at 24. The best approach to establishing a benchmark is one based on those revenues stemming directly from basic local service, as AT&T proposed in its Comments to the Joint Board, with a review of the benchmark every 3-4 years.

E. The Comments Support Defining USF Service Areas As Coterminous With Those Areas Served By Unbundled Network Elements And Limiting Universal Service Subsidy Qualifications To Those Expressly Contained In Section 214(e) Of The Act.

The commenters also raise two issues relating to Section 214(e). First, as most commenters acknowledge, carriers that provide service through unbundled network elements ("UNEs") fully qualify for universal service support under Section 214(e)(1). Although the Joint Board did not elaborate on this point, it did correctly indicate that carriers using UNEs qualify for USF support. RD at ¶ 155.[10] The Commission should reaffirm that conclusion.

As NYNEX suggests (at 32-36), the Commission should take one additional step to ensure that carriers using UNEs can effectively receive universal service support: promulgate a rule requiring states to define service areas for carriers using unbundled

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[10] Although AT&T does not necessarily concur with the Joint Board that carriers providing local service through resale alone do not satisfy § 214(e)(1)'s requirements (RD at ¶ 161), it is clear that such resale is completely distinct from the provision of service through unbundled network elements for purposes of USF subsidy eligibility. In the former case, the wholesale provider, not the resale carrier, must receive the USF subsidy so that it does not incur a loss in offering the service. In the latter case, however, the ILEC receives full compensation for use of its infrastructure (because UNEs are priced to recover total long-run incremental cost). Allowing the underlying provider of UNEs to receive both a cost-based rate for the UNEs plus USF support would result in an unwarranted windfall to that provider, and a substantial obstacle to alternative competitive entry.

network elements so that they are no larger than the areas in which the relevant unbundled network elements are offered and priced. For example, if a state has created three geographic zones for purposes of UNE pricing, the state should create three coterminous service areas for purposes of USF funding. As the Joint Board found, Section 214(e)(2) and (e)(3) invest the state commissions with ultimate authority to define the areas over which universal service support must be provided by eligible carriers. RD at ¶ 175. At the same time, however, the Board noted that Section 253 prohibits the commissions from defining service areas in a way that violates competitive neutrality, prohibits a carrier from providing interstate or intrastate telecommunication services, or is not "necessary to preserve and advance universal service." RD at ¶ 171 (citing 47 U.S.C. § 253(b)).

Failing to define service areas as coincident with the areas in which unbundled network elements are priced would contravene all three of these limitations. To the extent a state commission's definition of a serving area for high cost support differs from the geographic area for which UNE prices are determined, the purchaser of UNEs may have to pay more for UNEs than what it could recover from the both the customer and the USF. Such a discrepancy would effectively preclude that carrier from using unbundled elements to compete in that serving area. Making the universal service areas coextensive with the unbundled network element areas will safeguard against such an outcome, and ensure that the benefits of competition are available to consumers in both high cost and low cost areas.[11]

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[11] For similar reasons, the Commission must ensure that the calculation of costs for (continued...)

Second, a few commenters erroneously suggest that carriers must assume "carrier of last resort" obligations as a prerequisite to receiving universal service support. Such a requirement would be at odds with the plain terms of the statute. Section 214(e) expressly sets forth the obligations that must be assumed by any carrier that receives universal service support. For example, any carrier receiving universal service support must "offer the services that are supported by Federal universal service support mechanisms" "throughout the service area for which the designation is received." See § 214(e)(1). Moreover, under the clear terms of the statute, any carrier (including the "incumbent" LEC) may exit any area served by more than one eligible carrier, with the permission of the state commission and consistent with specific criteria set forth in the statute. See § 214(e)(4). If no carrier is willing to serve a particular community or area, then the state commission must designate a carrier to provide such service according to certain standards set forth in Section 214(e)(3). These statutory provisions are quite clear, and the Commission should not impose any additional requirements on carriers receiving universal service support.[12]

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[11] (...continued)
purposes of both universal service support and unbundled elements are consistent. As the Joint Board has already recognized, the economic principle of forward-looking costs is applicable regardless of whether one is determining the costs of universal service or unbundled elements. Equally important, the use of different cost estimates in the two contexts would inevitably lead either to uneconomic arbitrage (if unbundled elements are costed at levels below that used to calculate universal service support) or to barriers to entry (if universal service is costed at levels below that of unbundled elements).

[12] Similarly, the Commission should not adopt quality of service requirements as a prerequisite to universal service support. Such obligations would go beyond the statute and would constitute a competitive barrier to entry.

F. There Is Widespread Agreement That Modification Of The CCLC Should Be Referred To The Access Reform Proceeding And That The SLC Should Not Be Reduced.

Nearly all comments on the Joint Board's suggested changes in the SLC and CCLC reflect the same conclusions -- the Board's proposal is not competitively neutral, it perpetuates inefficiencies, and any modifications should be deferred until the access reform proceeding.[13] As Bell Atlantic notes, "Commission examination of SLC and CCL recovery is long overdue. However, that examination should be undertaken in the Commission's forthcoming access charge proceeding, rather than in the context of universal service, because the issues are intimately related to the restructuring of access charges and should not be addressed here, in isolation." Bell Atlantic at 23. And CompTel (at 18) correctly urges the Commission not to make adjustments in this docket because such a decision would be "based upon an incomplete examination of the issue."

AT&T agrees with the numerous commenters that reject a SLC decrease in this docket.[14] As USTA correctly points out (at 20), "[t]here is no evidence on the record that would justify decreasing the SLC." As the Joint Board found, current rate levels, which include a $3.50 SLC, are generally affordable. RD at ¶ 133. Thus, lowering the SLC would serve no valid universal service objective.

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[13] See GTE at 40; Ameritech at 15-16; SBC at 35; Bell Atlantic at 23; CompTel at 18; CSE Foundation at 14; Sprint at 16; Citizens Utilities Company at 20-22; MCI at 14; MFS at 34; USTA at 20; Pacific at 29; BellSouth at 3; U S WEST at 23.

[14] See GTE at 40; Ameritech at 15-16; SBC at 35; CSE Foundation at 14; Sprint at 16 (the SLC should be increased); Citizens Utilities Company at (20-22); MCI at 14; USTA at 20; Pacific at 29; U S WEST at 23.

Moreover, as AT&T demonstrated (at 12-13), reducing the SLC would increase the revenue required to provide universal service in high cost areas as well as increase the number of areas requiring USF contributions. The comments endorse this conclusion. For example, U S WEST (at 23) maintains that decreasing the SLC would necessitate "additional funds and funding mechanisms."

Furthermore, lowering the SLC would also run afoul of the Act's requirement that USF subsidies must be explicit. According to GTE (at 40), "[t]he FCC should not adopt the recommended SLC cap reduction because it would result in continuation of the implicit subsidy provided through the CCL charge in violation of the mandate in Section 254(e)...." A SLC reduction, then, is inappropriate at this time.

By contrast, if the Commission decides to adjust the CCLC in this docket, it should be eliminated entirely. In its support of reducing CCL charges, BellSouth (at 3) characterizes them as "a carry-over to the post-divestiture environment of the mechanism of supporting local rates through interstate toll charges." The fundamental flaw in the CCLC is that it is not assessed directly on the "cost causing" purchaser of the subscriber line. The commenters largely agree that this "arrangement is inherently inefficient and sends incorrect signals both to end users and interexchange carriers" (AT&T at 11), and that the CCLC should be eliminated altogether. For example, as Sprint (at 16) notes: "pricing distortions are avoided by recovering loop plant costs from the cost causer, eliminating the interstate CCL, and decreasing the interstate local switching rate by the amount associated with currently allocated NTS loop costs."

For these reasons, the vast majority of commenters do not concur with the Board's tentative proposals regarding the CCLC. The principal problem, as many commenters recognize, is that the Board's solution does not address the need to assess loop cost recovery directly on the cost causer instead of the interexchange carrier. Consequently, as GTE (at 41) finds, "[c]ontinued use of a CCL rate element also fails to be competitively neutral and violates the 'pro-competitive' intent of the 1996 Act." Simply changing the usage sensitive nature of the CCLC alone will not eliminate the inefficiencies of this implicit cross-subsidy. And any continued assessment of the CCLC would violate "the mandate in Section 254(e) of the 1996 Act that all support be explicit." GTE at 40. Where the SLC is insufficient to recoup the forward-looking costs of the loop from the end user, a competitively neutral USF funded by surcharges on all retail revenues should be used to compensate for the shortfall.

G. There Is Broad Consensus That A Proxy Model Should Be Used To Determine USF Support Requirements On A Forward-Looking Cost Basis.

No commenter seriously disputes the Joint Board's recommended application of forward-looking costs as the basis for determining USF requirements. RD at ¶ 270. Sprint (at 4), like virtually every other commenter, agrees that "[u]se of forward-looking costs -- the costs of providing local service by an efficient firm -- is economically rational and encourages carriers to operate efficiently."[15] While most comments reflect support for the use of a cost proxy model in establishing USF support requirements on this basis,[16] some ILECs have spent considerable energy criticizing the Hatfield Model. These attacks are not only misguided, but premature. First, many of the attacks focus on versions of the model that predate Version 2.2, Release 2, which was submitted in CC Docket No. 96-45, and even the attacks that address the filed model are plainly without merit. But all of these attacks are also premature, because the proposed proxy models will be examined and improved even further through the industry-wide, face-to-face discussions and the federal and state staff coordinated workshops on this issue. Moreover, as AT&T discussed in its Comments (at 13), the next version of the Hatfield Model, set for release early in 1997, will address all of the concerns expressed in Appendix F to the Recommended Decision, and will continue to be the best cost proxy model for use in administering the Universal Service

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[15] See also ALTS at 6; MCI at 2-3; CompTel at 10; CSE Foundation at 5.

[16] See SBC at 27-29; Pacific at 6; U S WEST at 30-32; Oregon at 4-5; CBT at 8-9; Ohio at 7; Sprint at 4; MFS at 20; MCI at 2.