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FEDERAL COMMUNICATIONS COMMISSION
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January 14, 2000

Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, SW Room TWB-204
Washington, DC 20554

RE: Notice of Ex Parte Meeting
In the Matter of the Funding Mechanism of the Universal Service Fund
CC Docket No. 96-45

Dear Ms. Salas:

Yesterday, Mark Lemler and I, both of AT&T met with Lawrence Strickling, Chief of the Common Carrier Bureau, Jack Zinman, Counsel to the Bureau Chief and Katherine Schroder, Deputy Chief, Accounting Policy Division. During that meeting, we discussed matters related to the referenced proceedings using the attached document as an outline.

Two copies of this Notice are being submitted in accordance with Section 1.1206 of the Commission's rules.

Sincerely,

Joel Lubin/pr

cc: L. Strickling
J. Zinman
K. Schroder

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THE USF LAG ADVANTAGES CARRIERS THAT ARE GROWING MARKET SHARE AT THE EXPENSE OF CUSTOMERS OF CARRIERS THAT ARE LOSING MARKET SHARE

- **Mechanism sets up an effective 12-month lag between a carrier's assessed revenues and its contributions to the USF.**

  - The average contribution a carrier makes in the first half of 2000, centered on April 1, 2000, is based on its average retail revenues in the first half of 1999, centered on April 1, 1999. *(See Illustrative Example 1)*

  - Similarly, the average contribution a carrier makes in the second half of 2000, centered on October 1, 2000, is based on its average retail revenues in the second half of 1999, centered on October 1, 1999.

  - Carriers must recover these obligations from their *current* year operations.

- **The lag advantages new entrants' future provision of LD by avoiding USF obligations for the first 12-months of operation.**

  - Problem has become more critical in light of 5th Circuit Court Order which requires the entire federal USF be assessed on End-User Interstate and International Revenues.

- **Carriers with growing LD market share are able to "buy" market share through the USF recovery rate.**

  - USF obligations are a real cost of doing business and cannot be competed away.

  - IXCs with losing LD market share cannot afford to lower their USF charge to match competition as their USF obligations are fixed, having been based on the previous year's higher revenues. IXCs must increase their USF collection rate to make up for their lost market share. *(See Illustrative Example 2)*

- **This competitive advantage violates the competitive neutrality provisions of Section 254(d).**

ILLUSTRATIVE EXAMPLE 1: DEMONSTRATION OF A 12-MONTH LAG BETWEEN USF ASSESSMENTS AND CARRIER CONTRIBUTIONS

Assume USF Assessment rate of 5%

	Carrier A Retail Revenues ($M)		Carrier A USF Obligations ($M)
January 1999	20	January 2000	1
February 1999	17	February 2000	1
March 1999	22	March 2000	1
April 1999	19	April 2000	1
May 1999	23	May 2000	1
June 1999	19	June 2000	1
Total Revenues	120	Total Obligations	6

Average Monthly Revenue (April 1999) = $20M

Average Monthly Obligation (April 2000) = $1M

ILLUSTRATIVE EXAMPLE 2: DEMONSTRATION OF HOW IXC1 CUSTOMERS SUBSIDIZE IXC2 CUSTOMERS

Assume: USF Contribution Factor of .05 for First Quarter of 2000 which was assessed against January 1, 1999 – June 30, 1999 Revenues to determine Industry USF Obligations in 2000.[1]

Assume: IXC1 has $10,000 revenue base, but loses 5% of LD Revenues to IXC2 in current year

		Comment
Assessed IXC1 Historical Revenue Base	$10000	
Assessment Rate	5%	Assumed USF Contribution Factor of .05
IXC1 Current Year USF Obligations (Based on historical revenues)	$500	IXC1 owes this amount regardless of market share in current year
IXC2 Current Year USF Obligations	0	IXC2 had no historical LD revenues
Effective IXC1 collection rate with 5% Revenue share loss to IXC2	5.263%	IXC1 must charge a higher line-item from remaining customers to recover its $500 USF Obligation
Result is IXC2 collection rate is either:	0 or 5.263%	Either result is not competitively neutral; distorts the LD market place

[1] The Common Carrier Bureau proposed a 0.058770 universal service contribution factor for the first quarter of 2000. (Public Notice DA-99-2780, December 10, 1999)

THE COMMISSION CAN ACHIEVE COMPETITIVE NEUTRALITY BY REQUIRING CARRIERS TO CONTRIBUTE TO USF BASED ON *CURRENT* REVENUES

- **Elements of Proposal:**

  - Carriers complete USAC Form 499 twice a year as they currently do.

  - USAC calculates a quarterly factor reflecting USF support requirements divided by the appropriate Interstate and International Retail Revenues from the Form 499s.

  - The quarterly factor is converted to a monthly USF assessment rate that is applied to the Retail Revenues of each telecommunications service provider's monthly end-user billings to determine that service provider's obligation.[2]

  - Carriers would remit to USAC within 30 days of the end of each month their monthly assessments.

  - USAC performs a quarterly "true-up" and adjustments are reflected in the next quarter's factor.

  - USAC performs an annual reconciliation (April) with each telecommunications service provider to ensure that the total monthly revenues billed the previous year correspond to the March 31 Form 499 submissions. An officer of service provider certifies to the accuracy of the Form 499 submission.

- **Proposal is efficient and competitively neutral.**

  - USAC's assessment rate is based on historical revenues, but its assessments come from current revenues. No forecasts of revenues are in the process.

  - The quarterly true-up ensures that there are sufficient funds to meet the following quarter's funding obligations.

  - Carriers contribute to USF at the same rate from their current revenues, independent of their historical revenues.

- **Proposal eliminates controversy and confusion.**

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[2] In the Texas USF, the factor is converted to a monthly assessment rate. For the Colorado USF, the factor is applied to quarterly billings.