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April 9, 2001

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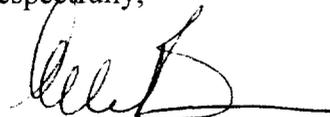
Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: *Ex Parte* Submission, CC Docket No. 96-45/

Dear Ms. Salas:

On April 5, 2001 the Consumer Energy Council of America released a report entitled "Universal Service: Policy Issues for the 21st Century." The report is based on meetings held by the Consumer Energy Council of America to discuss the future of the Universal Service Program. The meetings were widely attended by members of the telecommunications industry and policy makers. In accordance with the Commission's rule, tape recordings of those meetings were submitted in February. We wish to now submit a copy of the report.

Respectfully,



Ellen Berman

cc: Dorothy Attwood, Common Carrier Bureau
Carol Matthey, Common Carrier Bureau

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Leadership on Essential Services for Consumers

A CECA FORUM

UNIVERSAL SERVICE

Policy Issues for the 21st Century



FINAL REPORT

THE CONSUMER ENERGY COUNCIL OF AMERICA

2000 L Street, N.W. ♦ Suite 802 ♦ Washington, DC 20036 ♦ www.cecraf.org

MARCH 2001

Founded in 1973, CECA is the senior public interest organization in the U.S. focusing on the energy, telecommunications and other network industries that provide essential services to consumers. CECA is a leading national and international resource for information, analysis, and technical expertise on a wide variety of public policy initiatives. CECA works with government, industry and public interest organizations, and has become distinguished for building consensus between organizations with divergent interests. The result has been nearly three decades of policy development that has ensured reliable, sustainable and affordable essential services to consumers.

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2000 L Street, N.W. ♦ Suite 802 ♦ Washington, DC 20036 ♦ www.cecraf.org

MARCH 2001

Foreword

In the Fall of 2000, the Consumer Energy Council of America (CECA) launched a consensus-building forum to bring together a blue ribbon panel of national leaders to provide guidance for policymakers on the Federal Universal Service Program. The participants shared a vision of a vibrant and constantly evolving national telecommunications infrastructure. While ideas for improving the program varied widely, the prevailing theme of the many discussions was that the Universal Service Program is an essential component of one of America's most valuable social policies. To that end, participants in the Forum offered their expert advice and suggestions on how to make key aspects of the program most efficient, effective, and equitable.

The following report represents the combined input of the participants. It reflects, as well, background information provided by key administrators of the Universal Service Program. A report this rich in empirical detail and representative of such a variety of viewpoints could only result from the collective contributions of such an expert and involved group of stakeholders. This report reflects the most comprehensive information to date on the program's details, background, and stakeholder views on universal service.

This report is an essential guide for policy-makers. It provides recommendations that will contribute to the continued evolution and viability of important aspect of the Program. It serves as a valuable reference tool and roadmap for the Low-Income and High Cost components, and the strengths and weaknesses of the program in its current form.

I am most grateful to the project Chair, Kathleen Wallman, CEO of Wallman Strategic Consulting, former Deputy Assistant to the President for Economic Policy, and former Chief of the Common Carrier Bureau of the FCC, for her expert leadership in conducting meetings, reviewing drafts, and skillfully building bridges between stakeholders. I am grateful as well to the Vice Chairs, Elizabeth (Libby) Beaty, Executive Director of the National Association of Telecommunications Officers and Advisers (NATOA), and Nanette Thompson, Chair of the Regulatory Commission of Alaska and member of the Federal-State Joint Board on Universal Service, for their expert insights and leadership throughout the Universal Service Forum meetings. Chair Thompson guided the discussions but abstained from the decision process because of her appointment during this project to the Federal-State Joint Board on Universal Service.

The panoply of issues contained in the report could not have been elucidated or recommendations made without the skillful efforts of the three Subcommittee Chairs, Robert Blau of BellSouth, Russell Frisby of CompTel, and Earl Comstock of Sher & Blackwell. I appreciate their generous time and attention to the complexity of details and their sensitive guidance through issues often characterized by diverse views and interests. CECA Project Consultant Barry Johnson was invaluable in providing support and direction in the early stages of the project. The members of the Universal Service Administrative Corporation (USAC), especially Robert Haga, provided valuable contributions in synthesizing and compiling the vast amounts of data on universal service that are presented in this report. Brett Tarnutzer of Wallman Strategic Consulting did an outstanding job working with the CECA staff in writing and shaping the content of the report.

Finally, I am indebted to Davis Bookhart of CECA for his prodigious efforts as Project Manager of the Universal Service Forum. Davis was responsible for drafting background papers, orchestrating nearly 20 meetings of the Forum and the three subcommittees over a highly compressed timetable, facilitating conference calls to resolve contentious issues, and personally interacting with Forum participants on a daily basis.



Ellen Berman
President
March 2001

CECA is pleased to present its report on Universal Service. We could not have produced this report without the thoughtful input of consumer leaders, industry officials, and government agency experts who attended the Universal Service Forum meetings. CECA attempted to promote agreement on as many issues as possible, and this report reflects the diversity of views expressed in those meetings. This report does not purport to represent the official position of any agency, company or organization. CECA assumes full responsibility for the report and its contents.

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We gratefully acknowledge the following individuals who provided assistance to CECA in understanding the complexities of existing universal service programs and the dynamics affecting them. These individuals did not represent the official views or the positions of their respective government agencies, and this report does not purport to express the agreement of these individuals or their agencies with the views expressed herein.

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EXECUTIVE SUMMARY

I. Introduction

The CECA Universal Service Forum grew out of a shared vision of the value of the national telecommunications infrastructure to society. The Universal Service Fund, created by mandate in the Telecommunications Act of 1996 and administered by the Federal Communications Commission, ensures access to this vibrant telecommunications network by many who otherwise might not be served.

The Universal Service program is uniquely situated to provide the assistance necessary to maintain this national asset. However, with the dramatically changing telecommunications landscape, the program must evolve accordingly to remain effective. Fortunately, the drafters of the Telecommunications Act of 1996 anticipated an environment that would be regularly changing, and embedded mechanisms in the text of the Act that allows the Universal Service program to evolve as necessary. The CECA Universal Service Forum was convened to determine just how that evolution should take place, and to provide the necessary input and recommendations to policymakers so that the program can continue to benefit future generations of Americans.

A. The CECA Universal Service Forum

In February 2001, CECA completed a six-month consensus-building forum to examine key aspects of the federal Universal Service program. The CECA Universal Service Forum was comprised of a blue-ribbon panel of over 50 national leaders, representing local and interexchange carriers, information technology companies, Internet service providers, local, state and federal regulators, legislators, and consumer organizations.

The CECA Universal Service Forum convened the major stakeholders in a constructive dialogue about universal service in order to facilitate sound policy-making. While many divergent views were represented, a goal of the Forum was to focus on areas of common interest among the stakeholders—universally available basic telecommunications and the continuation of universal service as a long-standing goal of U.S. telecommunications policy—and narrow the differences among the stakeholders on the various policy options. Forum members, through a series of day-long meetings in Washington, DC and through meetings of focused subcommittees, engaged in a variety of contentious topics through frank and open discussions. The process culminated in CECA's specific recommendations to the federal and state policymakers with responsibility for these programs.

B. The CECA Process

As in previous consensus-building projects, CECA convened a broad-based panel of stakeholders to serve in the Universal Service Forum. The objective of the process was to arrive at one of three outcomes for developing policy guidance on issues under discussion:

- Consensus on policy options;
- Agreement on which policy options are clearly not acceptable;
- Identification of policy options that participants in the Forum consider acceptable.

The report culminates with recommendations to policymakers made by CECA, based upon a careful analysis of the stakeholder perspectives and interests. CECA attempted to promote agreement on as many issues as possible, and this report reflects the diversity of views expressed by stakeholders. This report does not purport to represent the official position of any agency, company or organization. CECA assumes full responsibility for the report and its contents.

During the CECA Universal Service Forum meetings, subcommittees and working groups were appointed to focus on specific issues of funding, supported services, and eligibility. Each subcommittee met on numerous occasions and produced a series of findings that were later discussed in the full committee meetings, and which laid the foundation for this report.

While the conclusions and recommendations of this report do not necessarily represent the consensus of all the Forum members, CECA could not have reached its conclusions without the careful reflection and thoughtful insights of all those who participated. As the goals and principles of universal service tended to be the central point of agreement, the next step was to elucidate the issues that will enable the Universal Service program to be as effective, efficient, and equitable as possible. The main questions that arose were:

- As the program evolves, and as social and industry conditions change, is the program well situated to remain fiscally healthy and sustainable?
- How can the program better reach the intended recipients of support, both from the consumer and the industry perspectives?
- How can the program continue to evolve to support services that are important to maintaining the goals of universal service?

These broad themes were examined, and more specific issues were discussed in the three subcommittees described below:

1. Who Pays and How? Subcommittee

This subcommittee focused on the various pressures being exerted on the Fund and how these pressures affect the Fund's stability and sustainability. The subcommittee also developed a set of alternative options for revenue generation outside the scope of the current mechanism.

2. Eligibility Criteria Subcommittee

This subcommittee focused on principles of eligibility for support and affordability of services, both from the consumer perspective and from the carrier perspective. For consumers, the focus often centered on how to improve the system so that the low-income households that are eligible for support receive that support. For carriers, issues included the role of competition, how wireless carriers could be brought into the competitive mix, and how service and support can be disaggregated for greater competition and efficiency.

3. Supported Services Subcommittee

This subcommittee examined whether additional services – such as advanced services – should be included in the provision of universal service. The subcommittee discussed how to contribute to a system that places an emphasis on forward compatibility, i.e., being able to continue building on the platforms without being “locked in” to certain technology. The subcommittee also focused on digital divide issues, examining the relevant components of the digital divide and how well the universal service program is equipped to address these issues.

C. Overview of the Issues

The concept of universal service has evolved measurably over the past 100 years and every indication is that it will continue evolving well into the 21st Century. Several questions have endured at every stage, and some new questions have arisen:

- **Supported Services** – Does the existing level of supported services comply with the requirements of the Telecommunications Act of 1996? What services should be added to the definition of supported services and over what timetable? Would adding these services significantly increase the size of the Fund required to sustain these services? Is there any evidence that shows that the inclusion of these services now will have a positive effect on society and the economy?
- **Stability of the Fund** – Can the Fund sustain itself? Should the base of revenue be broadened? Are there better alternatives for funding this program?
- **Efficiency of the Fund** – Does the Fund deliver support in a manner that is most consistent with maximizing consumer welfare and avoiding economic distortions?

- **Competition** – Will the Fund help competition in the rural and insular areas, or is it structured in a way that discourages competition in these areas? Is the program creating barriers that prevent competition or protect the incumbents? Is the structure and funding consistent with the goal of all segments of the telecommunications industry becoming effectively competitive?
- **Low Income** – If the estimates are correct that the subsidies intended to assist the poor and impoverished are missing approximately 75 percent of households that could be deemed eligible, how can this be rectified?
- **The Digital Divide** – Is it appropriate for the Fund to be used to address concerns that a gulf exists between the information “haves” and “have-nots?” Is it reasonable to assume that the gulf will close on its own without intervention? Is it too early to know?

These issues were discussed at length and the various stakeholder perspectives are presented in the report.

II. Issues Affecting the Funding of the Universal Service Program

A successful universal service mechanism begins with a clear and sustainable source of funding. On this, most constituencies agree, even though they may not agree on how the fund should be collected or who should be required to contribute. For the time being, it is clear that the current funding mechanism is adequate to fulfill the mission of universal service. There are important issues concerning which telecommunications providers should contribute to the system and how the necessary funds should be collected. There are fundamental questions concerning which companies should be considered telecommunications providers, and therefore subject to funding requirements. There are arguments that since universal service is a national social and economic policy, perhaps even non-telecommunications industries should contribute. Some even suggest that the entire system should be removed from its current funding mechanism and that Congress should allocate funds through general tax revenues, as other social policy or public works programs are funded.

The changing face of the telecommunications industry – through both the introduction of new competitive players and technological innovations – has created a need to reassess the means by which the Universal Service Fund (USF) is supported. As once distinct industry segments and markets converge – and as providers offer bundles that include both interstate and intrastate telecommunications services as well as non-telecommunications services at a single flat rate – new questions arise as to how the current mechanism is able to handle the evolving marketplace. For example:

- Is the Fund sustainable in the future given the means by which it is currently funded?

- Are the contributions collected in an equitable manner with respect to both carriers and end users paying into the Fund?
- Are the contributions collected in a competitively neutral fashion so that no class of carrier is either aided or hindered competitively because of the means by which funds are collected?
- Is the current collection mechanism efficient in terms of the incentives it may create and how these incentives operate to allocate the resources?

Some argue the answer to each of these questions is no – that competition and new technologies may undermine the foundation of the program; that some users of the network may not be paying into the program leaving others to shoulder more of the burden; and that the current payment scheme creates economic inefficiencies. There are also opposing viewpoints to these statements. Based on the analysis that follows, the Forum had sufficient concern regarding the vulnerability of the current funding mechanism to warrant an examination of several alternative funding mechanisms that potentially could better serve the public by being more sustainable, equitable, competitively-neutral, and efficient.

III. Alternative Funding Options

The CECA Universal Service Forum identified concerns about the sustainability and competitive neutrality of the fund. While the current system should be adequate to handle the current demands of universal service, there is potential for erosion of the interstate revenue base as well as the possibility for increased future demands on the system. CECA believes that the Universal Service Program, as a valuable social policy, needs to be strong and stable so that its mandate can be fulfilled. It must be flexible so that it can adapt to new demands that may arise in the evolving telecommunications environment. While the program is stable today, there are concerns that it might not be sustainable unless new funding sources are identified, if new services, including advanced services, are added, or even if the Low-Income program reaches its peak constituency. Universal service has benefited generations of Americans, and attention should be paid to make certain that it stays vibrant for generations to come.

The base from which revenue is currently generated is somewhat narrow, primarily collected by carriers from end users. This has led some to suggest that the higher rates associated with a narrow base is more inefficient than lower rates that would result from spreading the collections over a broader base. Consumer benefits come from raising funds in ways that minimize competitive, technological, and consumption distortions. With this in mind, some feel there is reason to be concerned about the current system having elements that are not competitively neutral, equitable and efficient, from both the consumer and the contributors' perspectives.

Based on these findings, it is prudent to examine options for modifying the universal service collection system to address the issues of sustainability, competitive neutrality,

equality, and efficiency. The Forum considered several options that are discussed below. In any decisions made regarding funding, policymakers must carefully consider the pros and cons of each option. Given the mandate of the Act regarding universal service and the authority granted to the FCC by Congress, some of these options would require Congressional action before they could be implemented. The options include:

1. Include All Interstate Revenues

This option maintains the general structure of the current funding mechanism, but modifies it to create a broader base of support from interstate service providers. Primarily this would mean including Internet service providers.

2. Include Interstate and Intrastate Telecommunications Revenues

This option includes all interstate telecommunications revenues similar to the previous option, but would include all intrastate telecommunications revenues as well (currently they are excluded). An impact analysis, provided in Appendix 4 of this report, shows that incorporating interstate and intrastate telecommunications revenues could result in considerably lower rates paid by contributors to the Fund.

3. Include Support from All Services

This option includes all interstate and intrastate telecommunications revenues, as in the previous option, but also includes the revenues from services and products that recover discounts under the schools and libraries fund. This option would include not only telecommunications service providers, but could also include companies that manufacture goods or provide other services that are clearly not telecommunications services.

4. Use Funding from the General Tax Revenues

Instead of relying on telecommunications revenues to fund universal service, support for the program could be drawn from general tax revenues appropriated through the normal federal legislative process. As a variation on this idea, general tax revenues could be used to supplement rather than replace telecommunications revenues. The supplement could be in the nature of a pure supplement to make up for funding shortfalls if they occasionally occur or, more boldly, to fund expansion of the program to underwrite broader access to advanced and enhanced network services as they become more essential tools for economic self-sufficiency. A further variation could be to use general tax revenues as a guarantee against shortfalls, much as existing federal facilities are available to guarantee borrowings or the solvency of financial institutions.

5. Use the Existing Excise Tax

A current excise tax on telecommunications services, originally created a century ago to fund the Spanish-American War, now funnels revenue into the general tax fund. The amount generated by this tax, at slightly less than three percent of all telephony revenues,

is the approximate size of the current Universal Service Fund, and could be directed instead into the Universal Service Fund.

6. Create a Flat Per-Line Assessment

One way to collect universal service funds from all users of the public switched telephone network is to make the assessment on a per-line basis. Since it is easier to identify lines than revenues, this would be an administratively efficient mechanism. Questions of equity could be addressed by setting the per-line rates higher for business lines than for residential lines, and the rate could be dropped to zero for low-income consumers. Analysis in Appendix 3 of the report hypothesizes three different levels of monthly per-line assessments (from \$0.75 to \$1.25) and the resulting impact on business assessments.

7. Assess a Per-Number Charge

Funding for universal service could be collected via a surcharge on every telephone number. This would apply to the actual numbers in use, as well as new phone numbers that are assigned in blocks. This option is similar to the Per Line Assessment, but would not cover any telephony that does not use traditional 10-digit telephone numbers, such as IP telephony.

IV. Eligibility Issues

The CECA Universal Service Forum undertook an analysis of issues regarding the eligibility qualification for two of the programs in the Universal Service program, the High-Cost and Low-Income programs. Because of time constraints, the Forum did not examine the eligibility requirements and issues associated with the Schools and Libraries Program (E-Rate) or the Rural Health Program. The eligibility processes are central to the dissemination of the monies in the program and therefore to the ultimate success of its programs. The topic of eligibility for support from the program was divided into two distinct areas of USF administration and policy for purposes of examination in the Forum:

- Consumer eligibility for Lifeline and Link-up services
- Carrier eligibility for subsidies to serve high cost areas

Some Universal Service Fund allocations go to states to support specific customer services offered at discounted prices, i.e., Lifeline and Link-up, while other funds support carriers for providing services to areas that are expensive to serve because of geography or terrain. In addition to issues that relate directly to standards of eligibility, the CECA Universal Service Forum also addressed issues regarding portability of support and disaggregating support areas.

V. Which Services Merit Support?

Judgments about which services merit support by the program are crucial because they may mark the dividing line between the “haves” and the “have-nots” in a society in which economic empowerment increasingly depends upon access to information and the technologies that deliver it. A significant portion of the population (some six percent of American households, representing more than six million households) for one reason or another does not have access to even “plain old telephone service” (POTS). This is evidenced by the data on telephone subscribership and the Lifeline and Link-up programs presented in the report.

More and more, Americans are taking part in the information age and the growth of the Internet shows that Americans are increasingly interested in more than just POTS. The 1996 Act provides some high-level and long-range guidance for the evolution of the Universal Service program, but leaves many of the details to the Federal-State Joint Board and the FCC to flesh out. As technology evolves and becomes vitally important to the social and economic well-being of all Americans, so too must universal service evolve. The services that are supported by the Universal Service program must be carefully examined to ensure that it is in touch with the needs of all Americans.

VI. Recommendations

The following recommendations have been developed by CECA based on the ideas generated during discussions and the exchange of views from the Forum participants.

A. Supported Services

CECA believes that the services supported by the Universal Service Program are vital to the social well-being of all Americans. CECA also asserts that advanced and enhanced services, as links for maintaining connectedness among Americans and as tools for economic viability, will continue to increase in importance. Therefore, **CECA recommends that all supported services be maintained and that steps be taken to determine when and how additional services, including advanced services, should be included in the definition of supported services.** CECA recommends taking the following steps:

1. Create a Technological Task Force to Advise Policymakers on the Evolution of Supported Services

CECA recommends that a Technological Task Force (TTF), in an advisory capacity to the FCC and the Federal-State Joint Board, be created to determine the optimal time for inclusion of additional services, including advanced services. The TTF would be a stakeholder group that would take a comprehensive examination of the social, political, economic, and technological landscape within which advanced services are

considered. The TTF will have several advantages as a supplement to the FCC review process:

- The TTF would be comprised of a broad balance of stakeholders, much like the Rural Task Force, so that a variety of viewpoints on advanced services could be considered. Ensuring that the key stakeholders are represented is essential to the success and credibility of the TTF;
- The TTF could monitor progress on a more continuous basis than the regular review mandated by the Act;
- The TTF would have the flexibility to examine issues outside the boundaries of jurisdiction of the FCC, and if appropriate, could present observations and recommendations to other governmental and non-governmental agencies.

CECA recommends that a TTF consisting of approximately 20 members be established to advise the Commission. The TTF should include a balance of key representatives of stakeholder interests, including:

- Industry and business representatives;
- Consumer leaders;
- Payer states and payee states;
- Academics and technical experts;
- Low income advocates and ratepayer advocates.

2. Utilize a Deliberative Approach for Determining Essential Services

The 1996 Act mandates that universal service be “an evolving level of telecommunications.” As such, the Federal-State Joint Board and the FCC must determine precisely *how* universal service should evolve and *what* it should evolve into. **CECA recommends that decision-makers take a deliberative approach to determining such issues as whether to include advanced services in the definition of supported services.** To guide the process of reaching a decision, CECA has developed a series of questions for the FCC and the Joint Board to explore. Those are included in Appendix 5 of the report.

3. Coordinate the National Development of Advanced Services through the USF

CECA recommends that federal, state, and local governments should engage in an effort, nationally coordinated through the Universal Service Program, to encourage deployment of advanced services in all possible venues, specifically including economic development agencies. The Universal Service Program is a valuable asset in the provision of telecommunications services to Americans, and is also excellently

positioned to oversee, plan, and synchronize governmental efforts to create the conditions under which advanced services are deployed.

B. The Low-Income Program

CECA believes that efforts should be made to ensure that the maximum number of low-income individuals are served by the Low-Income program. The recommendations below are intended to enhance the operational effectiveness of the program and encourage broader outreach efforts.

4. Use “Star” States as Benchmarks for Low Income Policies

The less than optimal penetrations rates suggest that most states could work more efficiently to ensure that Low Income support goes to all those who are in need. While state officials acknowledge that the Lifeline and Link-up programs are not benefiting a great number of eligible low income households, some states have policies that result in better targeting and support for households that are in need of assistance. **CECA recommends that the FCC examine the various state programs and determine which state policies can be held up as models for other states to adopt or replicate.**

A nationwide benchmark, such as the standard used in Vermont—where a flat threshold of 175 percent of the poverty line is used to determine who is eligible and then all eligible households are automatically enrolled into the system—can reduce the guesswork and produce clear numbers for state regulators.

5. Create a Compendium of Successful Outreach Tools

Even when states can determine more precise numbers of eligible households for Low Income support, a problem remains that many of those households may not realize that support is available. Publicizing this support is a requirement for Eligible Telecommunications Carrier (ETC) status, but it is not clear what the best means of publicizing might be. Currently, efforts to inform eligible individuals takes the form of:

- Bill stuffers from carriers;
- Television, radio, and print commercials;
- Information detailed on tax returns;
- Door to door, literally extending the message by word of mouth;
- Through web pages, such as the CALLS website;
- Information distributed through educational and social service agencies;

- Direct mailing to qualified customers.

This list gives examples of the variety of techniques available for making the program known to those hardest to reach. **CECA recommends that the FCC create a compendium of public education and outreach methods currently being used, along with an objective summary of the merits and limitations of each method.** This compendium can then be available to state regulators who wish to compare the methods used in their states with other demographically similar states.

C. Streamline ETC Certification Procedures

CECA believes that the goal of the Act—to introduce competition—will be enhanced if the ETC certification process is made most efficient, if undue delays are avoided, and if ease of certification is improved, thereby better enabling new entrants to compete. CECA acknowledges that many states have gained sufficient experience with the process over the past four years so as to have substantially accomplished streamlining. **CECA recommends that federal and state regulators, with the input of interested small carriers, continue to oversee progress in this area to ensure a technology-neutral and carrier-neutral approach to competition.**

PART ONE: THE CECA UNIVERSAL SERVICE FORUM

I. The Urgency of a Consensus on Universal Service

In February 2001, CECA completed a six-month consensus-building forum to examine key aspects of the federal Universal Service programs. The CECA Universal Service Forum was comprised of a blue-ribbon panel of over 50 national leaders, drawn from local and interexchange carriers, information technology companies, Internet service providers, local, state and federal regulators, legislators, and consumer organizations.

The CECA Universal Service Forum took as a point of departure a shared vision of the value of the national telecommunications infrastructure to society. A ubiquitous communications network benefits all Americans. Without federal Universal Service programs, many people would not be able to afford access to this vibrant telecommunications network. Many have low incomes and cannot afford even basic service. Others would pay much higher rates because they live in areas of the country that are costly to serve.

Without the programs, many of America's schools and libraries would not have the funds for the internal wiring and equipment necessary to connect to the Internet, leaving millions of children without a means of access to the information gateway to the world. Without the Fund many rural hospitals and health care facilities would not have the high-tech connections that transmit critical health information essential to remote diagnosis and treatment of patients. Simply put, without the assistance of a program such as the Universal Service Fund,¹ a portion of our society would be left behind.

CECA fully supports the idea that America's telecommunications and information network is critically important to our society, and that the social goals of the Universal Service program² are valuable to the strength and integrity of the Nation. Using this premise as the foundation for discussion, the CECA Universal Service Forum focused on the strengths and weaknesses of the program, and how the program could operate most effectively.

This examination is essential and timely. While the Fund in its present form was established by the 1996 Act, key parts of the program were implemented many decades earlier when the telecommunications industry (1) was characterized by the monopoly provision of service, and (2) was not experiencing convergence from other industries. In light of competitive market developments and the explicit decision of Congress in the Telecommunications Act of 1996 to foster the competitive provision of telecommunications services, some aspects of the existing Universal Service mechanisms need to be revised to better conform to current national policy. Determining how to do this has been a source of contention.

¹ The term *Universal Service Fund*, as used in this report, refers to the existing Federal universal service programs, rather than simply to the high-cost support fund, as the term has been used in the past.

² The Universal Service Fund is actually comprised of four different programs, the High Cost, the Low-Income, the Schools and Libraries, and the Rural Health Care. Further descriptions of these programs are offered throughout the report, especially in Part Four.

CECA convened the Forum because an exchange of ideas on universal service is urgently needed. Changes to universal service affect the interests of diverse constituencies whose positions can be difficult for decision-makers to reconcile. That difficulty in the decision-making process, combined with the large amounts of money at stake, can make change hard to accomplish and can prolong the process.

Such a decision-making process is continuing to evolve. Thus, the timing of the CECA Universal Service Forum is driven by a desire to provide useful input to state and federal policymakers as they make decisions affecting the universal service mandate of the Telecommunications Act of 1996. Much of that work has been done, but some important decisions about universal service have yet to be finalized. Among other things, the Federal-State Joint Board created a Rural Task Force to advise it on its recommendation to the Federal Communications Commission (FCC) regarding its treatment of rural carriers under the high cost mechanism. Further, the FCC has formally referred to the Federal-State Joint Board the periodic examination of the definition of which services should be supported by universal service, as well as an examination of the Lifeline and Link-up programs. Moreover, irreversible market forces for convergence are rendering old regulatory boundaries uncertain.

The CECA Universal Service Forum convened the major stakeholders in a constructive dialogue about universal service in order to facilitate sound policy-making. Because of the time limitations, the Forum focused its attention on two of the four components of the Universal Service Fund: the High-Cost and the Low-Income programs. The Forum did not address issues associated with the Schools and Libraries (E-Rate) Program or the Rural Health Care Support Mechanism.

While many divergent views exist, a goal of the Forum was to focus on areas of common interest among the stakeholders—universally available basic telecommunications and the continuation of universal service as a long-standing goal of U.S. telecommunications policy—and narrow the differences among the stakeholders on the various policy options. Forum members, through a series of day-long meetings in Washington, DC, and through meetings of focused subcommittees, engaged in a variety of contentious topics through frank and open discussions. The process culminated in a series of specific recommendations to federal and state policymakers with responsibility for these programs.

A. Overview of Issues and Stakeholder Views

The concept of universal service has evolved measurably over the past 100 years and every indication is that it will continue evolving well into the 21st century. Several questions have endured at every stage, and some new questions have arisen:

- **Supported Services** – Does the existing level of supported services comply with the requirements of the Telecommunications Act of 1996? What services should be added to the definition of supported services and over what timetable? Would adding these services significantly increase the size of the Fund required to sustain these services? Is there any evidence that shows that the inclusion of these services now will have a positive effect on society and the economy?
- **Stability of the Fund** – Can the Fund sustain itself? Should the base of revenue be broadened? Are there better alternatives for funding this program?
- **Efficiency of the Fund** – Does the Fund deliver support in a manner that is most consistent with maximizing consumer welfare and avoiding economic distortions?
- **Competition** – Will the Fund help competition in the rural and insular areas, or is it structured in a way that discourages competition in these areas? Is the program creating barriers that prevent competition or protect the incumbents? Is the structure and funding consistent with the goal of all segments of the telecommunications industry becoming effectively competitive?
- **Low Income** – If the estimates are correct that the subsidies intended to assist the poor and impoverished are missing approximately 75 percent of households that could be deemed eligible, how can this be rectified?
- **The Digital Divide** – Is it appropriate for the Fund to be used to address concerns that a gulf exists between the information “haves” and “have-nots?” Is it reasonable to assume that the gulf will close on its own without intervention? Is it too early to know?

1. *What Should the Fund Do?*

From its origins as a vague expression of an ideal national communications system to the much more specific statutory and regulatory delineation of the Universal Service program as it exists today, the goals and practical applications have been under constant pressures to keep pace. The last few years of the 20th Century may have seen the beginnings of an even more fluid and unpredictable landscape than has ever before been experienced. As the range of commercially available telecommunications services has expanded, two kinds of pressures have been exerted on the system.

First, there is an inclination in some quarters to explore whether the system should do more to support the availability of these new telecommunications services. There is a natural reaction in other quarters that the system is already doing all it should; expanding the responsibilities would be too expensive. Second, not all of the new services can be clearly or fairly classified as telecommunications services within the statutory and regulatory definitions, even though consumers may view them as substitutable products, which may create opportunities for arbitrage that reduce payments into universal service programs and favor one provider over another.

On the first point, despite the broader and more clearly defined Universal Service program that emerged from the Telecommunications Act of 1996, some experts argue that the services defined as being eligible for universal service funding are still not adequate to deal with the needs of today's society. While the definition includes basic services used for telephony, some have argued that the definition is already out of date and should be further expanded to include advanced services³ (such as broadband connections to an Internet access provider) that are rapidly being utilized by significant numbers of Americans.

2. What Services Should the Fund Support?

On a fundamental level, some claim that the Fund is not accomplishing even the most elementary portion of its mandate, which is to provide basic service to all Americans. Recent data shows that 94 percent of U.S. households have wireline telephone service,⁴ but in a country that is approaching 300 million people, the remaining six percent without telephone service equates to many millions of Americans without basic service. Perhaps even more egregious is that this population lacking basic telephone service is disproportionately composed of ethnic minorities. Thus, some experts argue that, in terms of deployment, even the current program is far from "universal."⁵

Some criticize the Fund for setting the floor for basic services too low. With changing technology, some equipment can be deployed today that satisfies the requirements for basic services, but may not be suitable for upgrading or supporting advanced services at a later date. For example, it is possible to deploy plant that provides voice-grade service, but will not support even the slowest of dial-up modems. The Fund, these critics contend, needs to be more far-sighted so that it can subsidize carriers for providing basic services today without compromising the ability to add more services later. Even worse, the Fund

³ The FCC's definition of advanced services (often referred to as broadband) is "having the capability of supporting, in both the provider-to-consumer (downstream) and the consumer-to-provider (upstream) directions, a speed (in technical terms, 'bandwidth') in excess of 200 kilobits per second (kbps) in the last mile." From Inquiry Concerning the Deployment of Advanced Telecommunications Capabilities, cc Docket No. 98-146, Report, 14FCCRcd 2398,2406 (1999).

⁴ Bureau of the Census, March 1997.

⁵ See Cooper, Mark, "Ensuring Telephone Access in the Digital Age," February 25, 1998, (<http://www.cme.org/access/universal/telephoneaccess>). The 6 percent figure also includes people who may, for a variety of reasons, simply not want telephone service.

could actually be providing incentives for the deployment of substandard “plant”⁶ by creating an environment whereby carriers deploy the most inexpensive equipment but are still rewarded by gaining universal service subsidies.

Others point out that the Universal Service program is still not the right mechanism for policing carrier plant investment decisions since the program has never had a mechanism for auditing how recipients spend funds and whether the funds are used to build quality network facilities. The fund is intended to keep subscriber rates low, regardless of the quality of the plant used to provide the service. They maintain that there are a variety of other government programs, such as the subsidized loan programs of the Rural Utilities Service (RUS), that include auditing and enforcement mechanisms that provide a better mechanism for policing broadband investment.

3. How Should the Fund Evolve?

While advanced services are becoming more a part of the daily lives of a significant number of Americans, some consumer groups and other stakeholders argue that the Internet and the emerging digital economy are exacerbating societal inequalities and there is a danger that rural and low-income Americans will be left out of the economic, social and political benefits of the IT revolution. Many consumer and public advocacy groups warn that there is growing evidence that a “digital divide” between information and technology “haves” and “have-nots” is emerging and have called for direct government regulatory action to address this divide. More specifically, these stakeholders feel that the Universal Service program should be the means for addressing this divide, and that the program should be expanded to include advanced telecommunications services. Others point out that recent surveys show some of these gaps closing, and that the gaps are a function of a variety of factors, including the lack of computer equipment and skill training or education, factors that are outside the purview of the current Universal Service Program.

Some groups have taken a different approach to the issue of advanced services. They contend that if the Universal Service Fund is going to support telecommunications carriers that deploy new lines and equipment, then the Fund should be used for new lines and equipment that are broadband capable. While addressing the digital divide may be an important consequence of the action, the real issue, they contend, is in investing in the future. Economic development is evolving from the traditional bricks and mortar establishments and industrial zones to a greater reliance on information services and e-commerce. It is true that the current universal service program is front-loaded to assisting the low income and rural households gain telephone service, but the real issue, some insist, is building the high-speed data infrastructure that is capable of bringing economic development into even the most remote and impoverished areas.

Other experts have opposed this call for expanding the Universal Service program, arguing that it is too soon to tell whether funding is necessary. At this point, the market is

⁶ Here the term “plant” refers to all facilities used, including lines, buildings, and physical equipment, by telecommunications carriers to provide services to end users.

delivering broadband service without the market-distorting effects of a subsidy. Moreover, if regulation supercedes market forces in bringing advanced services to all customers – as in the case of essential services such as the telephone system and electricity – there could be a premature technological “lock-in” and increased prices for many users. While recognizing the well-intentioned effort to address equity concerns, opponents of including advanced services argue that universal service subsidies for advanced services would distort investment patterns and lead to inefficient resource allocation, raising overall costs.

They add that there is no real evidence that market forces will not prevail as the most economically efficient means of deploying telecommunications and information services. They contend that advanced services – broadband – are being deployed at a rate that is as rapid as capital and human resources will allow. They believe that increasing the size of the Fund will not increase the rate of deployment, and may even slow the progress since it could result in the distortion of business plans, stress fragile supply chains, and scare off potential investors. The bottom line, they insist, is that the industry is just getting started in building a ubiquitous high-speed data infrastructure, and that given more time, the market will bring advanced services to all areas. This will happen not necessarily because it is good policy, but rather because it is simply good business.

4. How Should the Fund Be Managed?

Some stakeholders question how the program is currently managed and criticize the process by which telecommunications providers qualify for access to the Universal Service program. If the program is not managed well now and is not providing a level playing field for competition, these critics argue, then there is no basis for expanding the program’s scope until reforms are made.

This argument is shared by a variety of stakeholders for a variety of different reasons. Some low-income advocates criticize the management of the Fund for not efficiently directing the resources to those the Fund is intended to help. While one component of the Fund is the Low-Income Fund, aimed at partially subsidizing the basic costs of local service for Americans at or below the poverty line, some estimate that these subsidies are only reaching one-quarter of those eligible. Most will admit that there are many obstacles to reaching all eligible households, and there is evidence that suggests that a small portion of members in some households may not in fact want telephone service, but reaching only one-quarter of the eligible participants is simply unacceptable public policy.

Some state consumer advocates are also becoming disillusioned with the Fund. In high-population density states, the costs of providing telecommunications services are lower and therefore these states have less need for High-Cost universal service support. Therefore, groups from these states are increasingly unhappy about contributing to a mechanism from which they essentially do not benefit. While contributing to the viability of the network is acceptable, the way the high cost program is implemented is not. Carriers in rural areas, they contend, receive universal service funding based on the costs of providing basic services, but they can then make high profits on vertical or “premium” services, like voice