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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, and Universal Service Support Mechanisms	)	CC Docket No. 98-171
	)	CC Docket No. 90-571
Telecommunications Services for Individuals with Hearing and Speech Disabilities, and the Americans with Disabilities Act of 1990	)	
	)	
Administration of the North American Numbering Plan and North American Numbering Plan Cost Recovery Contribution Factor and Fund Size	)	CC Docket No. 92-237 NSD File No. L-00-72
	)	CC Docket No. 99-200
Number Resource Optimization	)	
	)	CC Docket No. 95-116
Telephone Number Portability		

COMMENTS OF WORLDCOM, INC.

WORLDCOM, INC.

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I. INTRODUCTION AND SUMMARY

WorldCom, Inc. ("WorldCom") is pleased that the Commission has initiated this proceeding to streamline and reform the manner in which the Commission assesses carrier contributions to the Universal Service Fund ("USF") and the manner in which carriers may recover those costs from their customers.[1] The Commission is correct to be concerned that fundamental and irreversible market changes render the existing contribution system unsustainable. Universal service is a cornerstone of American telecommunications policy, but it will be threatened if the current assessment system is not reformed.

Universal service is explicitly incorporated into the Communications Act of 1934, as amended ("the Act"). Section 254(d) of the Act requires "Every telecommunications carrier that provides interstate telecommunications service [to] contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service."[2] Under the Commission's current universal service rules, carriers' contributions are assessed as a percentage of their interstate and international end-user telecommunications revenues.[3] This is not as broad an assessment as the Commission initially implemented, but rather a narrower base that the Commission had to implement as a result of a court decision.[4] As the Commission itself has observed, there have been many significant developments in the interstate telecommunications marketplace since the Commission's initial implementation of Section 254 of the Act in 1997. These changes include the convergence of previously separate markets, the large-scale substitution of new services for traditional interstate wireline voice services, and the bundling into a single offering at a single fixed price of interstate telecommunications services with intrastate telecommunications services, non-telecommunications services, and even customer premises equipment. These

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1 *In the Matter of Federal-State Joint Board on Universal Service*, Notice of Proposed Rulemaking, CC Docket No. 96-45 (rel. May 8, 2001) ("*Notice*").

2 *See* 47 U.S.C. § 254(d).

3 47 C.F.R. §§ 54.706, 54.709, 54.711.

market developments have reduced traditional interstate telecommunications revenues and made it increasingly difficult to identify and measure the "new" interstate telecommunications revenues, thus rendering the current narrow assessment base insufficient to sustain the USF in the long run. This is especially significant in light of the potential for the fund to grow substantially from its current annual level of $5.5 billion to $8 billion or more. These market developments also have rendered the current contribution system discriminatory and inequitable. As explained below, the current revenue-based contribution system is not sustainable and should be replaced by a connection- and capacity-based system.

Among its many drawbacks, the current system has placed an unfair burden on particular classes of carriers – particularly, established long distance carriers – and their customers. This bias against long-distance carriers directly contravenes section 254's requirement that contributions be equitable and nondiscriminatory. In addition, the current system suffers from numerous other flaws, including the fact that it is not adaptable to changes in the marketplace, competitively neutral, or administratively efficient. The Commission therefore should replace the revenue-based mechanism currently in place with a more equitable, efficient, and sustainable system.

Specifically, WorldCom proposes that the Commission determine carriers' Universal Service Fund contributions based on the number and capacity of connections carriers provide to end-user customers to connect to the public switched network or the public Internet,[5] or to

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[4] In Texas Office of Public Utility Counsel v. FCC, 183 F.3d 393 (5th Cir. 1999), the Fifth Circuit overturned the Commission order assessing intrastate as well as interstate telecommunications revenues to fund the schools and libraries portion of the USF.

[5] The term "public Internet" is used to describe the Internet that can be accessed by the general public through dial-up, DSL, or dedicated circuits. The public Internet would exclude, for example, corporate virtual private networks and corporate intranets.

otherwise originate or terminate interstate traffic. This connection- and capacity-based approach has many advantages, including eliminating the need to determine under which jurisdiction particular revenues or minutes of use fall. As new technologies and new communications networks undermine traditional market boundaries and engineering and pricing paradigms, a connection- and capacity-based contribution system provides the most equitable and nondiscriminatory basis on which to assess carrier contributions. It provides a neutral allocation of contribution obligations among all carriers involved in the provision of interstate services. It applies a uniform standard for recovering contributions from all carriers that provide interstate telecommunications service. Compared to any other contribution system, it has a minimal impact on customers' purchasing decisions (how much service to purchase or which type of carrier or technology to select), and thus least harms allocative efficiency. It is competitively neutral, avoiding distinctions (and hence market distortions) based on the technology or categories of providers.

Because all end-users of interstate telecommunications services need connections to the public switched network or public Internet or to otherwise originate or terminate traffic, whatever service, technology, or carrier they choose, a connection- and capacity-based contribution approach best assures the sufficiency and sustainability of the federal USF. It also is predictable and adaptable to changing market conditions, because the number of end user connections a carrier provides fluctuates much less than the interstate revenues a carrier earns from its customers. Finally, once implemented a connection- and capacity-based contribution system would be easy to administer – determining a carrier's end user connections is much more straightforward than attempting to classify a carrier's revenues by jurisdiction.

WorldCom proposes that the Commission set specific low monthly universal service assessment rates for connections for residential, pager, and single-line business customers, and that the remainder of the fund contributions be made by the remaining business connections at the assessment levels required to meet universal service needs. The assessment obligation would fall on the carrier who has the relationship with the customer for whom the connection is made, not on a carrier that is just provisioning the line for another carrier. Thus, when carrier A is providing a special access, unbundled network element- platform ("UNE-P"), or UNE-loop connection to carrier B, so that carrier B can provide service to its end-user, it is carrier B, not carrier A, who would have the assessment obligation. Specifically,

- A monthly per connection charge would be assessed on carriers that provide end-user connections to the network as follows:

*	Non-Lifeline residential wireline and wireless (other than pager) customers	$1.00
*	Lifeline residential customers	$0.00
*	Residential and business pager customers	$0.25
*	Wireline and wireless single-line business customers	$1.00

The per connection assessments on carriers for the remaining business connections – multi-line business ("MLB") wireline and wireless and special access – would bear the remainder of the funding burden, with the per connection assessments based on the capacity of these connections. WorldCom proposes the following simple three-level system for facilities other than traditional switched access lines.

LEVEL	FACILITY CAPACITY	USF CONTRIBUTION CHARGE
1	Less than 1.544 Mb/s	Base multi-line business USF charge
2	1.544 or greater but less than 45 Mb/s	5 x (base MLB USF charge)
3	45 Mb/s or greater	40 x (base MLB USF charge)

Given the current size of the federal USF and the number and capacity of current connections to end users, these three capacity levels would yield a base multi-line business USF charge in the range of $2.50 to $3.25.[6]

WorldCom proposes that there be a transition to this new connection- and capacity-based contribution system and the related recovery system. For certain connections – residential wireline and wireless connections, pager connections, and single-line business connections – the information technology ("IT") systems needed to perform the contribution and collection tasks either already exist or can be readily implemented, and therefore a rapid transition is both possible and desirable. Carriers should be required to report their residential, pager, and single-line business end-user connections to the Universal Service Administrative Company ("USAC") within two months of publication of the Order in this proceeding in the Federal Register. For more complex business connections, a longer – but explicit – transition period is needed to allow carriers to develop the IT systems needed to perform the contribution and collection tasks without disrupting on-going business activities. Carriers should be required to report these end-user connections to USAC within 12 months of publication of the Order in the Federal Register. In the interim, the carriers should continue to contribute to the USF using the current revenue-based system.[7]

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6 WorldCom does not have data on the distribution of wireless service across customer classes and thus can only provide a range.

7 Since there do not appear to be accurate data on the interstate telecommunications revenues of wireless carriers, during this transition period the Commission might choose to require wireless carriers to contribute $1.00 for each of their multi-line business connections. But since it would not be competitively neutral to require wireline carriers to contribute more per multi-line business connection than wireless carriers, as soon as the transition period is over, wireless carriers should be required to contribute on the same MLB USF charge basis as wireline carriers.

WorldCom urges the Commission to adopt this proposed connection- and capacity-based approach to assessing USF contributions.

II. THE FCC MUST REFORM THE EXISTING CONTRIBUTION SYSTEM TO TAKE INTO ACCOUNT ONGOING MARKETPLACE TRENDS

Section 254(d) of the Communications Act of 1934, as amended, requires the Commission to establish a mechanism for assessing contributions to a federal USF is specific, predictable, and sufficient.[8] The system must yield sufficient revenues to meet the needs of the USF and must do so in a predictable fashion, avoiding unnecessary disruptions to telecommunications markets, such as those caused by volatile changes in individual carrier contribution obligations. This requires a contribution system that remains stable as market changes occur and the size of the fund continues to grow. Section 254(d) also requires that all providers of interstate telecommunications services contribute to the federal Universal Service Fund on an equitable and non-discriminatory basis. In addition, as the Commission pointed out in the *Notice*, the system for allocating contribution obligations "should be adaptable to changes in the marketplace, competitively neutral, and relatively simple to administer."[9]

The *Notice* recognizes the "need to revisit the concepts underlying the existing contribution system, in light of current market trends, to ensure that providers of interstate telecommunications services continue to 'contribute, on an equitable and nondiscriminatory basis, to the specific, predictable, and sufficient mechanisms established by the Commission to preserve and advance universal service.'"[10] WorldCom strongly supports this objective. Although the current contribution system was adopted only four years ago, market trends have

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8 47 U.S.C. § 254(d).

9 *Notice* at para. 16.

10 *Notice* at ¶ 3 (quoting 47 U.S.C. § 254(d)).

quickly made it outdated. As set forth more fully below, the current system (1) places a disproportionate burden on interexchange wireline voice services; (2) unduly favors wireless carriers; (3) fails to take into account new technologies that compete against traditional interexchange voice services; (4) ignores the trend toward bundling of services; (5) gives new entrants an unfair competitive advantage over existing interexchange carriers; and (6) is unduly complex. As a consequence, the current universal service contribution system violates the Commission's statutory mandate by imposing inequitable and discriminatory assessments against certain segments of the telecommunications industry. Prompt reform is needed to ensure that the federal universal service support mechanisms will remain "specific, predictable and sufficient" in an industry that continues to undergo enormous change.

A. The Current System Places a Disproportionate and Inequitable Burden on Interexchange Wireline Voice Services

Under the current system, universal service is funded primarily through assessments on providers of wireline, interstate interexchange voice services. As a result, the traditional interexchange carriers – and their customers -- bear 77 percent of the federal USF burden.[11] At the time the current system was devised, revenues from these services were growing at a rapid pace. The expectation was that such growth would exceed any increase in the size of the USF, and the assessment base was therefore both sufficient and sustainable.

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[11] Common Carrier Bureau, Industry Analysis Division, "State by State Telephone Revenues and Universal Service Data," April 2001, Figure 1 and Table 1. (In 1999, the most recent year for which data are available, IXCs accounted for $62.464 billion, or approximately 77.3 percent, of industry interstate end-user telecommunications revenues of $80.844 billion. Because universal service contributions are based on interstate end-user telecommunications revenues, IXCs would be responsible for approximately 77 percent of the total contribution burden.)

This assumption, however, is no longer valid given the rapid marketplace changes that have occurred since the Commission's current system was adopted in 1997. Providers of wireline long distance voice services are facing increasing competition, and the capacity of long haul networks in the United States has grown exponentially, far outpacing demand.[12] These factors have placed extreme downward pressure on retail as well as wholesale rates, which in turn have significantly reduced revenue growth. Indeed, in a September 8, 2000 report entitled "Telecom Services,"[13] J.P. Morgan Securities Inc. projected a decline in wireline long distance voice revenues from a peak of approximately $84 billion in 1999 and 2000 to $71.1 billion in 2005. The report further estimated that, for long distance voice service, average revenues per minute of use for consumer markets had fallen from $0.23 in 1995 to $0.19 in 1999, with estimates of continued reductions to $0.16 in 2001 and to $0.11 in 2005. For business markets, the report projected that the average revenues per-minute of $0.15 in 1995 and $0.12 in 1999 would fall to $0.10 in 2001 and to $0.06 in 2005.

At the same time that long-distance revenues are declining, the funds required for universal service programs appear to be expanding. Given various proposals to expand such programs, as well as organic growth permitted by existing rules, the annual fund may be expected to grow from its current size of $5.5 billion to $8 billion over the next few years.[14]

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12 *See, e.g.*, "How the Fiber Barons Plunged the Nation Into a Telecom Glut," *Wall Street Journal*, June 18, 2001, p. A1. ("All told, about 39 million miles of fiber-optic cable stretch underneath [the] U.S. ... enough to circle the earth 1,566 times. Companies racing to build or expand nationwide networks laid some $90 billion of fiber during the past four years. Merrill Lynch & Co. estimates that only 2.6% of the capacity is actually in use. Much of it may remain dark forever.")

13 J.P. Morgan Securities Inc., "Telecom Services, A Fresh Look at the Industry," September 8, 2000.

14 There currently are a number of formal and informal proposals to increase the size of the federal USF. WorldCom does not believe that this is the appropriate venue for addressing the merits of these proposals, but recognizes that some of these proposals may be adopted by the

Commission and therefore the Commission must estimate what the dollar impact of these proposals would be on the fund and take this into account when evaluating the sufficiency and sustainability of alternative contribution systems. If all of these proposals were adopted, the USF could double to more than $10 billion. WorldCom does not expect there to be such a huge expansion of the USF, but the fund could grow from its current annual level of $5.5 billion to $8 billion. WorldCom has identified at least four areas where USF growth is possible; there may be others.

The Commission has opened a proceeding to consider the Multi-Association Group proposal to expand the High Cost fund by, among other things, replacing implicit subsidies that allegedly currently reside in the access charges of rural telephone companies with an explicit new Universal Service charge. (Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers, CC Docket No. 00-256, Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Access Charge Reform for Incumbent Local Exchange Carriers Subject to Rate-of-Return Regulation, CC Docket No. 98-77, Prescribing the Authorized Rate-of-Return for Interstate Services of Local Exchange Carriers, CC Docket No. 98-166, Notice of Proposed Rulemaking, FCC 00-448, rel. Jan. 5, 2001) The proposal explicitly rejects placing any caps on the size of the fund and could increase the fund size by as much as $1 billion each year.

The current rules for high cost rural telephone companies allow the Universal Service Fund to grow as the number of rural lines grows. There are no restrictions on the type of lines — they can be business lines or non-primary residential lines as well as primary residential lines. Competitive and technological neutrality require that wireless carriers who qualify to be eligible telecommunications carriers ("ETCs") have the same access to universal service funds as incumbent local exchange carriers. As wireless technology grows in popularity, many rural customers will have a strong incentive to purchase wireless service, either as an alternative to wireline services (providing the primary line) or as a supplement to primary-line wireline service, especially if the wireless service is subsidized by the USF. To the extent that wireless service replaces wireline service, there would be no impact on the size of the federal USF. But to the extent that customers use wireless service to supplement primary wireline service, under current Universal Service funding rules this would increase the size of the fund. It is difficult to place a dollar estimate on the impact of funding these non-primary wireless connections in high cost areas served by rural telephone companies, but it could be in the hundreds of millions of dollars nationwide.

The Communications Act explicitly instructs the Commission to review the definition of universal service, to consider expanding its scope to consider advanced services. One possible outcome of this process is a determination sometime in the future that universal service support for basic service is not sufficient; that such support should be expanded to cover advanced services that can best be provided over DSL technology. This could have a price tag in the multi-billions of dollars.

The Lifeline and Link-up programs are the universal service programs designed to ensure affordability for low income households. The Commission has delegated to the States much of the responsibility for implementing these programs. One state, California, has implemented a self-certification system without audits. Any customer who self-certifies as qualifying is automatically given the subsidies. As a result, California receives approximately 55 percent of all federal low income support dollars (See www.universalservice.org/li USAC-Low Income

Without significant reform of the current contribution methodology, the universal service contribution factor assessed on carriers' interstate telecommunications revenues, which now is almost 7 percent, could easily exceed 10 percent to sustain universal service.

Such a contribution factor would impose inequitable burdens on carriers and consumers, thereby distorting the efficient functioning of the marketplace. In particular, the increased assessments will have to be passed through to that subset of telecommunications users who purchase interstate telecommunications services subject to the current contribution requirements. For large customers, this could translate into hundreds of thousands if not millions of dollars in additional charges every year. These customers will have both the incentive and the ability to find technological options that will allow them to bypass this burden, placing an even greater burden on smaller customers who have no alternatives available.

In sum, WorldCom believes that in a world of declining interexchange carrier revenues the current system inevitably will lead to a USF "death spiral," where increasing universal service demands chase fewer interstate dollars.

Support Mechanism, Low Income Program Dollars Reported, January 2000-December 2000, as of March 30, 2001, Appendix LI 6, page 1, May 2, 2001) even though its population is only 13.34 percent of the total U.S. population (Population Reference Bureau, 2000 United States Population Data Sheet, Section 1, Resident Population, 1999 & 2015). Nationwide, the total number of households that receive Lifeline support is only 29 percent of total households receiving means-tested cash or non-cash assistance (public housing, heating assistance, rent assistance, Medicaid or Medicare, supplemental security income, hot food lunch, food stamps, veterans benefits, public assistance, or welfare). (*See* <u>Universal Service Policy Issues for the 21st Century</u>, Final Report, The Consumer Energy Council of America, March 2001, ("CECA Report") Table Four, p. 13.) But in California, the number of households receiving Lifeline support is 122 percent of those total households receiving means-tested cash or non-cash assistance. (*Id.*) If other states, in the desire to maximize their residents' access to Lifeline support, were to follow California's lead in implementing non-audited self-certification, and if the "take rate" were the same in those states as in California, the Lifeline fund would increase three-fold, from about half a billion dollars to one and a half billion dollars.

B. The Interim Safe Harbor Gives Wireless Carriers an Unfair Advantage

Under the current system, wireless carriers may take advantage of an interim safe harbor in calculating their interstate revenues for universal service contribution purposes. Instead of reporting their actual interstate and international revenues, wireless carries may simply report a fixed percentage of revenues ranging from one to 15 percent.[15] The wireless industry has enjoyed substantial growth since the adoption of the interim safe harbor in 1998. The number of wireless telephony subscribers doubled between 1997 and 2000, from 55 million to 109.5 million, and the annual revenues generated by the wireless industry exceeded $52 billion in 2000.[16] A significant amount of this revenue undoubtedly derives from interstate calls, especially given the prevalence of bundled local and long-distance wireless service packages now offered to consumers.

As the Commission acknowledges in the *Notice*, given this growth, "it is possible that the actual percentage of interstate wireless telecommunications revenues may now significantly exceed the Commission's interim safe harbor percentages."[17] WorldCom believes that this is, in fact, the case, and urges the Commission to eliminate the favorable treatment wireless carriers enjoy under the current system. Not only do wireless carriers fail to foot their fair share of universal service funding, the current system creates an inefficient, artificial incentive for long-distance consumers to use wireless services instead of wireline services.

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15 *Notice* at ¶ 11.

16 FCC News Release, "FCC Adopts Annual Report on State of Competition in the Wireless Industry" (released June 20, 2001).

17 *Notice* at ¶ 12.

C. The Current System Fails to Take Into Account New Technologies that Provide Consumers Alternatives to Traditional Interexchange Voice Services

New technologies, particularly the Internet, have transformed the way people communicate. These technologies are providing consumers at least partial substitutes to traditional interexchange telecommunications services. Instead of placing a long-distance call, for example, a consumer may very well send an email. Consumers have also begun using "voice-over-Internet" technology for both interstate and international voice communications.

As these alternative communications technologies grow in popularity, they will invariably decrease the total amount of interstate minutes and revenues that would be reported under the current universal service contribution system. They also may exacerbate the already difficult task of classifying particular revenues (and associated minutes of use) as interstate or intrastate. The Commission must keep these technologies and market trends in mind as it reforms the current system. In doing so, it should avoid discouraging technical innovation and new services, while at the same time recognizing the impact these services may have on the current method of funding universal service.

D. The Trend Towards Bundled Services Makes It Increasingly Difficult to Identify and Measure Interstate Revenues

Telecommunications carriers are increasingly offering bundles of services for a single fixed price rather than charging consumers for each particular service based on usage. These bundles can include, in addition to interstate telecommunications services, intrastate telecommunications services (toll and local), enhanced services, and customer premises equipment. Many wireless carriers now offer consumers buckets of minutes for both local and long-distance calling for a fixed monthly fee. These innovative service offerings are now being offered by wireline telecommunications carriers as well, initially for large business customers.

In the near future, these offerings will allow those customers to meet all their needs for data and voice services, for interstate and intrastate services, for telecommunications and enhanced services, over an Internet network, with pricing that does not in any way conform to old usage-based rates.

This trend will make it increasingly difficult to distinguish between interstate and intrastate services, or between telecommunications and non-telecommunications services, let alone allocate revenues to the interstate telecommunications portion of a bundled service. A universal service contribution mechanism that imposes artificial service distinctions where they do not exist in the marketplace is likely to cause uncertainty and create inequitable and anticompetitive contribution requirements.

Finally, it is worth noting that carriers that have never been subject to jurisdictional separations as part of rate-making (e.g., non-dominant carriers) find it especially challenging to definitively determine interstate vs. intrastate revenues.

E. The Current System Gives New Entrants an Unfair Competitive Advantage Over Existing Interexchange Carriers

By basing USF contributions on a carrier's interstate revenues during the previous six-month period, the current system places existing long-distance carriers at a competitive disadvantage compared to new entrants to the long-distance marketplace, including the Regional Bell Operating Companies ("RBOCs") that have received authority to provide in-region long-distance service under section 271 of the Act. As an initial matter, these new entrants are not required to contribute to the Universal Service Fund for six months because they have no historical revenues upon which to base contributions. As the *Notice*, at ¶ 14, points out, this enables these new entrants to undercut the prices offered by established providers who are contributing to the Universal Service Fund. Moreover, this competitive advantage continues in subsequent years given that, "to the extent that new entrants increase their long distance market share and recover contributions against current end-user revenues, the revenue base against which they recover contributions would remain greater than the revenue base against which their contributions are assessed."[18] In contrast, established long-distance carriers confronted with declining market share and revenues face the opposite effect: under the current system, they will have to recover from a declining current revenue base their universal service contributions assessed against a larger revenue base from a prior period.[19] The Commission should reform the current system to eliminate this bias against established long-distance carriers.

F. The Current System is Unduly Complex

The current system for contributing to the Universal Service Fund and recovering these costs from end-users often involves highly complex reporting, billing, and record-keeping procedures. For example, the task of distinguishing between interstate and intrastate revenues (and associated minutes of use) can be difficult and complicated. It is increasingly becoming a contrived task, driven wholly by regulatory requirements, as carriers are more frequently offering packages of bundled services at unitary prices that are not tied to distance or jurisdiction. The existing system of assessing federal USF contribution obligations ignores these marketplace realities and creates unnecessary uncertainty and complexity.

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18 *Notice* at para. 14.

19 *Id.*

III. WORLDCOM SUPPORTS THE COMMISSION'S PROPOSAL TO REPLACE ITS OUTDATED REVENUE-BASED METHODOLOGY WITH A FLAT-FEE ASSESSMENT MECHANISM AND RECOMMENDS THAT THE COMMISSION BASE THIS SYSTEM ON THE NUMBER AND CAPACITY OF EACH CARRIER'S INTERSTATE END-USER CONNECTIONS

A. The Universal Service Fund Contribution Assessment Should be Determined by the Number and Capacity of Connections Each Carrier Provides its End-user Customers

As shown in the preceding section, the current system for assessing carrier USF contributions is unfair, discriminatory, and unsustainable. It imposes a disproportionately large share of the contribution obligation on established interstate long distance providers, at a time when their revenues are declining. The current system similarly assesses a disproportionately small share of the obligation to other providers of interstate services, such as wireless carriers, whose revenues are growing rapidly. Moreover, the problems that afflict the current system demonstrate clearly that it is not adaptable to changes in the marketplace, competitively neutral, or easy to administer. Indeed, even if the Commission were to modify the current revenue-based contribution system to eliminate the biases created by the use of historical revenue data and the insufficient wireless safe harbor, it still could not be confident that the interstate telecommunications revenue assessment base will grow over time at a sufficient pace to accommodate the potential growth in the federal USF. There is substantial danger that the current funding mechanism is not sustainable.

In WorldCom's view, the current system for assessing universal service contributions must be completely overhauled. Most fundamentally, as discussed below, the Commission should replace the existing revenue-based scheme for allocating responsibility among carriers with one that is based on the number and capacity of network connections that carriers provide to their end-user customers.

The Commission seeks comment on the relative advantages and disadvantages of assessing contributions on a flat-fee basis, such as a per-line or per-account charge, and whether levels of interstate revenues would be relevant in such a system.[20] WorldCom supports the movement to a flat-fee system precisely because it would eliminate the need to classify the jurisdiction of particular revenues (and associated minutes of use), an increasingly difficult, if not impossible, task, as discussed above. Rather than a per-line or per-account basis, WorldCom proposes that the Universal Service Fund contribution obligation of a telecommunications carrier that provides interstate service be determined on the basis of the number and capacity of connections the carrier provides to end-user customers to connect to the public switched network or the public Internet or to otherwise originate or terminate interstate traffic.

B. WorldCom's Proposed Plan for Assessing Universal Service Fund Contributions Among Carriers Takes Into Account Ongoing Marketplace Trends, Is Consistent with the Statutory Requirements, and Is Far Superior to the Existing System

A connection- and capacity-based approach to allocating universal service responsibility among carriers is both consistent with the statute and superior to the existing revenue-based mechanism. As shown below, a connection- and capacity-based approach is consistent with section 254(b)'s requirement that "[a]ll providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service."[21] In addition, consistent with section 254(d) of the Act, WorldCom's proposed system for allocating contribution obligations is predictable and sufficient, adaptable to changes in the marketplace and thus sustainable over time, competitively neutral, and relatively

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20 *Notice* at para. 25.

21 47 U.S.C. §254(b).

simple to administer. Finally, consumers will benefit because a connection- and capacity-based approach will better ensure sufficient universal service funding without imposing inequitable burdens on any particular class of end-user.

Equitable. A connection- and capacity-based approach provides a neutral, fair allocation of the contribution duties among all interstate carriers rather than unfairly burdening traditional long distance providers with the overwhelming share of the contribution obligation. Moreover, the broad funding base of the connection- and capacity-based approach will operate to limit the contribution requirements of any particular class of telecommunications providers and, accordingly, the amounts recovered from their customers.

Nondiscriminatory. A connection- and capacity-based approach encompasses the broad array of carriers providing interstate telecommunications services covered by the Commission's existing rules, including local exchange, interexchange, wireless, paging, satellite, and private carriers. This approach is nondiscriminatory because carriers that offer competing services are subject to equivalent contribution requirements. Unlike the end-user revenue model, which relies on complex, outdated, and increasingly irrelevant jurisdictional allocations, a connection- and capacity-based approach relies on an objective, uniform standard for recovering contributions from all carriers that provide interstate telecommunications services.

Competitive Neutrality. The connection- and capacity-based approach is competitively neutral because it does not distinguish between particular categories of service providers or the technologies they use in providing service. Accordingly, a connection- and capacity-based approach will not distort how carriers choose to structure their businesses or the types of services that they provide. A corollary benefit is that use of connections would avoid the competitive disadvantages that the current system imposes. In fact, a connection- and capacity-based approach will remain competitively neutral despite changes in the profitability of categories of interstate telecommunications service providers and the calling patterns of their customers. By avoiding a revenue-based measurement, the contribution mechanism would not place competitors with declining interstate end-user revenues at a competitive disadvantage compared to competitors with increasing revenues.

In addition, using the connection- and capacity-based approach will eliminate the need for providers of bundled services to estimate the portion of revenues generated that is attributable to interstate telecommunications services. Moreover, this approach can be applied readily to emerging technologies, such as the provision of telecommunications services by cable operators.

As markets converge and customers have the opportunity to choose among providers that use different technologies to provide similar, but not identical services, it becomes especially important that the universal service assessment not in any way distort the choice that customers make among alternative providers. Indeed, identification of what constitutes a nondiscriminatory and equitable – as well as competitively neutral – funding mechanism must be made in the context of market dynamics. Does the assessment mechanism discriminate against any carrier or treat any carrier inequitably in its ability to compete in the marketplace? Discrimination will occur if two carriers offer competing services (e.g., wireline interstate telecommunications service and wireless interstate telecommunications service), but the assessment is placed on only one of the carriers, because then one carrier has a cost imposed on it that the other carrier does not, and the harmed carrier either must add a charge to its customers that its competitor does not have to add, or the carrier has to absorb costs that its competitor does not have. But in the case of a per connection charge, even if the contribution burden falls only on the interstate carrier that provides the connection, this will not place the "interconnection carrier" in either a competitive disadvantage vis-à-vis other carriers or in an impaired financial situation as long as the carrier is allowed to recover all the costs (including collection costs) associated with contributing to the fund and is able to identify any associated charge on its customers' bills as a federal Universal Service charge. Except to the extent the charge keeps a customer from connecting with the U.S. telecommunications network altogether, customer decisions (and the market in general) are not distorted by requiring the carrier providing the connection to pay the assessment. Since the customer could not evade the universal service surcharge by changing its choice of carrier, no carrier is placed at an inequitable, discriminatory, or competitive disadvantage.

Predictable, Sufficient, Adaptable, and therefore Sustainable. A connection- and capacity-based mechanism satisfies the requirements of predictability and adaptability to changing market conditions because connections are far less susceptible to significant, rapid changes than interstate revenues have proven to be. Moreover, because every end-user of interstate telecommunications service needs a connection to the public switched network or to the public Internet or to otherwise originate or terminate traffic, a connection- and capacity-based assessment provides the broadest possible base for capturing interstate telecommunications activity, and ensuring sufficiency. While rapid market changes can erode the revenues in specific narrowly defined markets, and thus undermine the on-going sustainability of a fund based on such a narrow definition, connectivity is not subject to such drastic market changes. Moreover, a connection- and capacity-based approach eliminates the incentive for carriers and customers to utilize less efficient means of service provision in an attempt to avoid the assessment.

Easy to Administer. WorldCom's proposed approach, with three easily identified capacity levels, also would be relatively easy to administer. Although time will be needed for carriers to develop the systems needed to implement a connection- and capacity-based contribution system, carriers can easily determine the number and capacity of connections that serve their customers. By contrast, the task of determining interstate revenues is much more complicated in an industry where prices are increasingly insensitive to distance or jurisdiction and services are combined in packages at unitary prices.

In analyzing any universal service funding mechanism, it is important to consider its impact on capital-intensive IT resources. The scarcity and expense of these resources drives many industry decisions. Before any product can be offered, carriers must develop mechanisms for provisioning services and billing customers. Long distance carriers, in particular, must carefully scrutinize every new service offering to ensure that any revenues from these products will exceed the costs of their introduction. In current market conditions, where access to capital is constrained, it is essential that the federal USF contribution mechanism does not unnecessarily harm the telecommunications industry by diverting a substantial portion of scarce IT resources to the implementation of regulatory requirements that are unnecessarily complicated and inefficient.

As an initial matter, converting to a connection- and capacity- based system will require carriers to deploy scarce IT resources for the development of new contribution and collection systems. But if carriers are given an appropriate transition period in which to develop the necessary systems, this one-time effort pales in comparison to the ongoing time and resources required to determine contributions under the existing revenue-based approach.[22]

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[22] WorldCom has suggested 12 months in order to permit carriers to include the necessary systems changes in their capital budgets and to schedule the development that must be done.

Consumer Benefits. WorldCom's proposed connection- and capacity-based contribution system would help consumers in a number of ways. First, the proposal intentionally sets low assessment rates for residential connections and leaves the residual burden on business connections. Second, Lifeline connections would be exempt from the assessment. Third, the $1.00 per connection assessment is significantly lower than the current assessment on a typical residential customer under today's revenue-based system. Fourth, for price-conscious customers attempting to compare the rates of different carriers, it would be much easier to compare a per-connection charge that will not vary from month to month to a percentage-of revenue-based charge that produces a dollar amount that varies each month with the customer's usage. Fifth, by assuring the on-going sufficiency and sustainability of the USF, the connection- and capacity-based contribution system protects the most vulnerable consumers.

C. The WorldCom Proposal Resolves the Commission's Implementation Concerns About Flat Fees

WorldCom proposes that the Commission determine carriers' USF contributions based on the number and capacity of connections carriers provide to end-user customers to connect to the public switched network or the public Internet or to otherwise originate or terminate interstate traffic. As explained above, specific rates would be set for residential, pager, and single-line business connections, and the remaining needs would be met by setting rates on the remaining business lines. Connections made via other technologies, such as cable or satellite, would be treated the same as wireline or wireless connections.

In the *First Report and Order,* the Commission declined to adopt a per-connection approach because of its concern that such a mechanism "would require the Commission to adopt and administer difficult 'equivalency ratios' for calculating the contribution of carriers that do not offer service on a per-line or per-minute basis."[23] The Commission's concerns can now be resolved because there now is a lot of useful market information to use as the basis for setting "equivalency" levels.

The contribution assessments on higher-capacity connections should be set according to two criteria: (1) minimizing administrative burdens and complexity by creating a simple system with a few contribution levels; and (2) ensuring that the USF contribution charges do not materially change the "crossover" point between different facility types or otherwise distort customer choices.

WorldCom's proposal for three capacity levels – Level One for connections of less than 1.544 Mb/s, Level Two for connections 1.544 Mb/s or greater but less than 45 Mb/s, and Level Three for connections of 45 Mb/s or greater – is based on the following market information:

The 5:1 ratio between the Level 2 and Level 1 charges is consistent with the price cap LECs' current practice of assessing a PRI ISDN USF charge that is five times higher than the base USF charge. (PRI ISDN facilities have a capacity of 1.544 Mb/s.) The 5:1 ratio also is consistent with the 5:1 ratio between the PRI ISDN PICC and end-user common line charge ("EUCL") and the multi-line business PICC and EUCL.[24] The 40:5 or 8:1 ratio between Level 3 and Level 2 charges approximates the "crossover" point between DS-3 and DS-1 facilities purchased from ILEC special access tariffs. These are robust, market-generated capacity levels that are simple to identify and administer.

In contrast, WorldCom has determined that a capacity charge based on per-voice grade equivalents, such as the one indicated in Appendix 3 to the CECA Report,[25] would not be

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23 *First Report and Order* at para. 852.

24 47 C.F.R. §§ 69.152(1)(2); 69.153(d).

25 CECA Report at p. 70.