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

Federal-State Joint Board on Universal Service	)))	CC Docket No. 96-45
AT&T Request to Contribute to Universal Service Based on Projected Revenues	)))))	

AT&T PROJECTED REVENUE PROPOSAL REPLY COMMENTS

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TABLE OF CONTENTS

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Pursuant to Section 1.415 of the Commission's Rules, 47 C.F.R. § 1.415 and its Public Notice, DA 02-376, published in 67 Fed. Reg. 13332 (March 22, 2002), AT&T Corp. ("AT&T") submits this reply to other parties' comments on its proposal to use projected revenues as the basis for assessment of contributions to the universal service fund ("USF") pending modification of the existing discriminatory and inequitable methodology based on historical revenues.[1]

INTRODUCTION AND SUMMARY

On December 13, 2001, AT&T requested permission to base its contributions to the USF on projected revenues commencing January 1, 2002, because the continued existence of a 6-month lag between the assessment and recovery of carriers' universal service contributions, coupled with AT&T's sharply diminishing interstate and international telecommunications revenues, AT&T would be forced to charge its residential customers a universal service contribution of 11.5% under the Commission's proposed 0.068086 USF contribution factor for the first quarter 2002.[2] The 11.5% surcharge represented an increase of 160 basis points over AT&T's then-existing 9.9% USF line-item for residential customers. Because AT&T was and remains highly concerned about the impact of an 11.5% factor on consumers, AT&T proposed the projected revenue approach, which would have allowed it to charge residential customers a 9% line-item charge.

AT&T acknowledged that because its USF contribution base would be smaller, this would impact the overall USF contribution base and would require the Commission to revise the contribution factor upwards. AT&T's 9% line-item charge to residential customers assumed for illustrative purposes that the assessment rate would increase by approximately 0.2%. As AT&T pointed out, if the Commission had adopted a USF assessment mechanism for the first quarter 2002 based on actual revenues (*i.e.,* no lag), the resulting AT&T and industry USF contributions would be the same as under AT&T's proposed projected revenue approach, assuming no projection errors. AT&T suggested a true-up that would serve to correct any projection errors, thus leaving all contributors in the same position as they would have been under a USF assessment based on actual revenues.

As shown in Part I, AT&T agrees with commenters that *prompt* resolution of the Commission's pending rulemaking and implementation of a connection- and capacity-

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(footnote continued from previous page)

1 The Association of Communications Enterprises ("ASCENT"), BellSouth Corporation ("BellSouth"), SBC Communications, Inc. ("SBC"), Sprint Corporation ("Sprint"), Verizon, Verizon Wireless, and WorldCom, Inc. ("WorldCom") filed comments.

2 *See* Letter from Robert W. Quinn, Jr., AT&T, to Ms. Magalie Roman Salas, Secretary, FCC, dated December 13, 2001, CC Docket No. 96-45.

based USF assessment and recovery mechanism based on *current* data that would eliminate once and for all the anticompetitive and discriminatory impact of the lag is the superior solution to AT&T's and other similarly-situated carriers' USF problems. However, if such resolution is not forthcoming by July 1, 2002, then AT&T's projected revenue proposal should be granted.

As demonstrated in Part II, contrary to some commenters' suggestions, AT&T is *not* seeking a competitive advantage either *vis-à-vis*: (i) similarly-situated IXCs with declining long distance revenues, such as WorldCom and Sprint, *or* (ii) the RBOCs with increasing long distance revenues. Rather, AT&T acknowledges that the Commission should allow all carriers a one-time election to base their USF contributions on projected revenues pending full elimination of the lag. This will enable similarly-situated IXCs to be on equal footing as AT&T. As for the RBOCs, the lag generally provides them with an enormous competitive advantage. Grant of AT&T's proposal will tend to match appropriately their USF contributions with their current long distance market share.

As shown in Part III, parties' protestations to the contrary notwithstanding, AT&T has made a legally sufficient showing to be permitted to use projected revenues in these circumstances.

I. PROMPT RESOLUTION OF THE USF RULEMAKING IS THE BEST SOLUTION BECAUSE IT WOULD DEFINITIVELY ELIMINATE THE THE DISCRIMINATORY, ANTICOMPETITIVE IMPACT OF THE LAG.

In the currently pending *USF Contribution FNPRM*,[3] the Commission is considering revising the existing assessment method for determining carriers' universal service contributions based on their prior period revenues.[4] Specifically, the Commission seeks comment on "whether to assess contributions based on the number and capacity of connections provided to a public network" so as to "ensure the long-term stability, fairness, and efficiency of the universal service contribution system in a dynamic telecommunications marketplace."[5]

As AT&T and the Coalition[6] show in their April 22, 2002 comments in response to the *USF Contribution FNPRM*, changes in telecommunications markets have rendered the existing revenue-based universal service assessment and contribution mechanism obsolete and competitively-biased. The dramatic decrease in wireline interstate revenues, coupled with increasing universal service funding requirements, will force the universal service system into a "death spiral," with ever-increasing contribution factors that consumers and providers will seek to avoid through new offerings. The discriminatory

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3 *Federal-State Joint Board on Universal Service, et al*., CC Docket Nos. 96-45, 98-171, 90-571, 92-237, 99-200, 95-115, 98-170, 02-43, rel. Feb. 15, 2002 ("*USF Contribution FNPRM*").

4 The Commission's USF recovery mechanism was originally predicated on "prior year" revenues and there was a 12-month lag between assessment and collection. *See Federal-State Joint Board on Universal Service*, 12 FCC Rcd 8776 (1997) ("*Universal Service Order*").

5 *USF Contribution FNPRM,* ¶ 2.

impact of the 6-month lag will continue to strain the system. In short, a fundamental revision of the USF assessment and recovery mechanism is long overdue, not only to ensure its sustainability, but also to restore fairness to the universal service contributions borne by IXCs and their customers, and to comport with Congress's mandate that such contributions be equitable and nondiscriminatory. The collect-and-remit aspect of the Coalition proposal will best eradicate the lag by basing all USF assessments and recovery on current data.

To be sure, AT&T has *repeatedly* demonstrated that assessment of carriers' USF contributions based on historical revenues seriously disadvantages certain carriers, violates competitive neutrality and discourages local competition.[7] The USF lag creates an artificial competitive advantage for telecommunications carriers with increasing interstate or international revenues because those carriers – unlike established long distance carriers – are not obligated to contribute to the universal service fund for 6 months – when they will be able to spread the recovery of those contributions over a larger revenue base. To the extent the RBOCs increase market share following in-region long distance entry, the revenue base for recovery of their USF obligations will always be greater than the revenue

(footnote continued from previous page)

6 The members of the Coalition for Sustainable Universal Service are Ad Hoc Telecommunications Users Committee, AT&T, e-commerce Telecommunications Users Group, Level 3 Communications, and WorldCom ("Coalition").

7 *See Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, AT&T Petition for Reconsideration, filed Mar. 1, 2000; AT&T Reply to Oppositions to and Comments on its Petition for Reconsideration, filed May 1, 2000; AT&T Comments on USF Lag FNPRM, filed Nov. 30, 2000; AT&T Reply Comments on USF Lag FNPRM, filed Dec. 14, 2000; Comments of AT&T Corp., filed June 25, 2001, at 9-11; Reply Comments of AT&T Corp., filed July 9, 2001, at 8-10; AT&T Comments on USF Contribution FNPRM, filed Apr. 22, 2002, at 11-13.

base on which their USF obligations were assessed. In fact, the RBOCs will be able to use this discrepancy to finance their market share growth. By contrast, carriers with declining interstate revenue accrue large assessments, which then must be spread over a smaller revenue base.

Only after *years* of requesting the Commission to eliminate the lag and and starkly confronted with its own sharply diminishing interstate and international telecommunications revenues that required a precipitous increase in its residential line-item USF charge, did AT&T on December 13, 2001 ask the Commission for permission to base its USF contributions on projected revenues. By then, the Commission had recognized the serious competitive distortions engendered by the 12-month lag and reduced the interval between the accrual of revenues and the assessment of USF contributions based on those revenues to 6 months,[8] stating that the "shortened interval will allow contributors to better reflect market trends influencing carriers' revenues, such as the entry of new providers into the interstate marketplace."[9] Despite these observations, the indisputable fact remained that even a 6-month lag did *not* cure the competitive inequity and burden imposed on AT&T's consumers by a USF mechanism predicated on historical revenues.

Most commenters acknowledge the "serious problems with the current system to recover the costs associated with federal universal service support" and urge expeditious resolution of the *USF Contribution FNPRM*. Sprint at 4; Verizon at 4 (rulemaking pending); Verizon Wireless at 4. As WorldCom notes, the industry would be

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[8] *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, Report and Order and Order on Reconsideration, FCC 01-85, released March 14, 2001 ("*6-Month Lag Order*").

[9] *6-Month Lag Order,* ¶ 9.

"better served by addressing the underlying problem" rather than granting relief by allowing carriers to base their USF contributions on projected revenues. WorldCom at 3. Given its longstanding, relentless advocacy to eliminate the lag which is the root cause of the problem, it should come as no surprise that AT&T *agrees*.

Expeditious resolution of the rulemaking and adoption of the connection-based USF assessment and recovery predicated on a collect-and-remit approach is the best solution because it would avoid the need for forecasting revenues, true-ups to actuals and the associated administrative burdens. Thus, AT&T urges the Commission to implement that system by July 1, 2002. However, if it does not modify the USF contribution methodology by then, it should grant AT&T's proposal to use projected revenues to avoid burdening millions of consumers with the effects of the lag.

II. AT&T IS NOT SEEKING A COMPETITIVE ADVANTAGE.

A number of commenters point out that grant of AT&T's request to use projected revenues for USF assessment purposes would mean that other contributors would pay more. BellSouth at 2; Verizon Wireless at 2. Verizon accuses AT&T of seeking to shift its USF burden to the rest of industry because AT&T conceded that the impact of allowing it to use projected revenues would likely require a 0.2 additive to the USF contribution factor. Verizon at 4.

WorldCom asserts that special treatment for AT&T would be at the expense of other contributors, especially those with declining revenues, because, all other things being equal, WorldCom's long distance prices overall would be higher than AT&T's. WorldCom at 2-3, 10. Accordingly, WorldCom contends that if the Commission grants

AT&T's request it would be faced with a rash of "me, too" waivers that it would have to grant to avoid creating further competitive distortions. WorldCom at 3, 14.

Contrary to these suggestions, AT&T is *not* seeking a competitive advantage relative either to: (i) similarly-situated long distance carriers, such as WorldCom and Sprint, or (ii) the RBOCs. Rather, AT&T acknowledges that if it grants AT&T relief, the Commission should allow all carriers a one-time election to base their USF contributions on projected revenues pending elimination of the lag. *Accord* WorldCom at 4, 16; ASCENT at 8-9. This would avoid any competitive inequity by allowing carriers with declining interstate and international revenues to elect to base their USF contribution on projected revenues, as well as the administrative burdens associated with review of a large number of individual waiver requests.

Although it is true that AT&T's proposal would shift some of the USF burden that it is now carrying to the RBOCs, there is nothing inappropriate about that fact. The lag generally provides the RBOCs with an enormous competitive advantage as they enter the long distance market which, under the existing USF mechanism, is underwritten by IXCs with diminishing revenues.

As Oncor (at 2) demonstrated in earlier comments filed on November 30, 2000, "basing universal service contributions on prior year revenues unfairly awards a competitive advantage to carriers that have experienced revenue growth over the previous year and improperly imposes a significant and unfair competitive disadvantage on those carriers that have suffered declines in revenues over the previous year." This is because for "carriers whose revenues have increased since the preceding year, . . . their contribution is a smaller percentage of their current year's revenue" than for those carriers whose year-over-year revenues have declined. "In a year in which its revenues decline, the carrier's universal service assessment will be a higher proportion of its current year revenue base than carriers with increasing or stable revenues." NOS Comments, filed November 30, 2000, at 1-2. "As a result, established providers or carriers with declining revenues may need to charge their end-users non-competitive rates in order to generate the additional revenue needed to meet their universal service contributions." *Id*.

The salient fact is that AT&T's projected revenue proposal would do no more than what would have been accomplished if the Commission had adopted a USF assessment mechanism based on actual revenues (*i.e.,* no lag). In other words, the resulting AT&T and industry USF contributions would be the same under AT&T's proposed projected revenue approach, assuming no projection errors. AT&T suggested a true-up to correct any projection errors, thus leaving all contributors in the same position as they would have been under a USF assessment based on actual revenues. There is nothing unfair about that.

III. AT&T HAS MADE A LEGALLY SUFFICIENT SHOWING.

Various commenters contend that AT&T has not made a legally sufficient showing to justify a waiver. BellSouth accuses AT&T's request of having no public interest benefit, just AT&T's own pecuniary and competitive interests. BellSouth at 1. Sprint and WorldCom allege that there are no special circumstances justifying an AT&T waiver because they also have sharply declining interstate and international revenues. Sprint at 2, 12; WorldCom at 7-9; *see also* Verizon at 2 (stating its access lines are currently declining). SBC similarly attacks AT&T's request for lack of a special circumstances showing. SBC at 1-4.

Without question, AT&T is not the only carrier that is significantly harmed by the USF lag. Rather as ASCENT (at 3) points out, "AT&T's request dramatically highlights the flaws inherent in a system which assesses universal service contributions predicated upon stale revenue data." The inevitable result of the lag is that "carriers with declining revenues pay an effectively higher percentage contribution than their competitors with stable or increasing revenues." ASCENT at 6.

As Hertz correctly explained (at 6), in comments filed on AT&T's March 1, 2000 petition for reconsideration, the fact that "some carriers are experiencing declines in market share and revenues is undoubtedly attributable to market forces that are independent of the Commission's rules. *It does not follow, however, that the Commission's rules, when applied to these pre-existing market conditions, have no separate or distinct competitive effect*" (emphasis added). Thus, the special circumstance justifying a waiver, or preferably a one-time election to use projected revenues for all carriers with declining interstate revenues, is the radical shift in industry revenues that has established a critical need to revamp the USF mechanism and yet, to date, the problem, albeit identified, has *not* been solved. The public interest would be well served if consumers were not forced to bear the discriminatory impact of the lag.

Verizon questions AT&T's need for use of projected revenues because, when AT&T made its request, the Commission had just announced a lower USF contribution factor than had been previously in place. Verizon at 1. The fact is that AT&T's declining revenue base nonetheless required AT&T to impose a significantly higher surcharge rate. Had the Commission's factor increased, AT&T's surcharge would have been higher than 11.5%.

Nor is there any basis to various commenters' allegations that AT&T has made a marketing decision to collect disproportionately more of its USF obligation from residential customers than business customers. Verizon at 3; Verizon Wireless at 2. AT&T has consistently assessed its USF obligations on residential and business customers according to the revenues generated by each sector. Contrary to SBC's innuendos, AT&T Broadband files its own FCC Form 499, is outside the scope of the instant projected revenue request, and does contribute to USF on its cable telephony revenues. SBC at 3.

Several commenters oppose AT&T's projected revenue proposal because of associated administrative burdens. They note that with use of projected revenues, there will always be issues as to forecasting, true-ups, incentives to underforecast and possible gaming, as well as more filings with USAC. WorldCom at 5, 11, 13-14; Verizon at 1, 3; Verizon Wireless at 1, 3-4. The fact that use of projected revenue for USF assessments by some carriers would require more frequent reporting and true-ups and thus would place some additional burden on carriers is not an unreasonable trade-off to ensure competitive neutrality. Neither the existing historical revenue-based assessment nor any other mechanism that fails to redress the inequity of the lag can be justified based on administrative convenience because it is flatly inconsistent with the dictates of Section 254(d) of the Act.

AT&T strongly urges the Commission to immediately revise its USF assessment methodology and adopt a contribution mechanism based on the number and capacity of end-user connections that an interstate telecommunications provider has in-service which will allow the USF operate in a competitively neutral and sustainable manner. Failing prompt implementation of that mechanism, the Commission should grant all carriers a one-time election to use projected revenues so that as end-user revenues shift among carriers, so would their USF contribution obligations. Although this would not insulate any carrier from competitive losses, it would ensure that no carrier is competitively disadvantaged by the USF program and that customers are free to select carriers based on the quality and price of their services, as contemplated by the Act.

CONCLUSION

To the extent and for the reasons stated above, the Commission should: (a) modify and implement by July 1, 2002 its USF assessment and recovery mechanism as proposed in AT&T's and the Coalition's *USF Contribution FNPRM* Comments filed today, or, at a minimum, (b) grant all carriers a one-time election to base their USF assessments on projected revenues pending final elimination of the USF lag.

Respectfully submitted,

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April 22, 2002

CERTIFICATE OF SERVICE

I, Tracy L. Rudnicki, do hereby certify that on this 22nd day of April, 2002, a copy of the foregoing "AT&T Projected Revenue Proposal Reply Comments" was served by U.S. first class mail, postage prepaid, on the parties named on the attached Service List.

/s/ Tracy L. Rudnicki
Tracy L. Rudnicki