Exhibit 1
Technical Comments on the Staff Model and Assumptions

The Wireline Competition Bureau Staff should be commended for its development of the Staff Study of Alternative Contribution Methodologies.[1] The Staff Study helps to add analytical clarity to the issues before the Commission, and does so in a transparent manner. AT&T's comments herein are preliminary, as the Staff Study and its underlying model and assumptions are extremely complicated, such that some of the interdependencies within the model will only become apparent with further experience operating the model. AT&T will supplement these comments as it develops further insights into the Staff Study.

For clarity, these comments are divided into comments with respect to the structure of the Staff Model, and comments with respect to input assumptions for the model.

I. Staff Model Structure.

The Staff Model has an odd interdependency that AT&T has not yet been able fully to diagnose. When the policy assumption regarding the level of the CMRS "safe harbor" is changed, the Staff Model apparently also changes its estimates of total ILEC Subscriber Line Charge ("SLC") revenue. It is not clear why the CMRS revenue allocation and ILEC SLC revenue should be related.

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[1] *Commission Seeks Comment on Staff Study re Alternative Contribution Methodologies,* Public Notice, FCC No. 03-31 (rel. Feb. 26, 2003) ("Staff Study").

II. Staff Study Input Assumptions.

A. Projections of Total Fund Size.

The Staff Study states that the Staff projected universal service program requirements by quarter.[2] Program requirements increase because of MAG plan increases, as well as growth in the high-cost support mechanisms resulting from line growth and inflation.[3]

Understandably, the Staff Study does not appear to attempt to estimate other potential sources of fund growth. For example, the Staff Study does not attempt to reflect any policy-based changes that the Commission may adopt. However, it is possible that the Commission will adopt such policy changes during the 2003-07 period. Indeed, the Joint Board recently recommended changes to the Lifeline program that could increase total universal service support by $105 to $123 million annually.[4]

Nor does the Staff Study attempt to estimate growth from supporting additional lines to a household that complement a subscriber's existing, supported service. However, as a greater number of wireless carriers seek ETC designation, they will be eligible for support for all connections provided, regardless of whether that connection substitutes for or complements another supported connection. This is also true for ILEC and CLEC ETC lines, although the potential magnitude of increase from CMRS connections is much greater.

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[2] *Staff Study* at 18.

[3] *Id.*

[4] *See Federal-State Joint Board on Universal Service*, Recommended Decision, CC Docket No. 96-45, FCC 03J-2 (rel. Apr. 2, 2003), at ¶ 10.

Both of these factors could push the total USF substantially above the levels projected by the Staff, especially in the later years of the Study.

B. Projections of End User Interstate and International Telecommunications Revenues.

1. Wireline End User Interstate and International Local and Long Distance Revenues.

Although the Staff Study takes account of significant declines in wireline long distance minutes of use, it also assumes that price decreases slow or, in the case of residential toll service, actually stop. In the residential market, the Staff Study assumes that residential toll revenues per minute have dropped and will drop at the following rates:

Date	Annualized Rate of Change Residential Interstate Switched Toll Revenues[5]
January 2001	-10 %
January 2002	-7.5 %
January 2003	-5 %
January 2004	0 %
January 2005, and after	0 %

[5] The description of the Staff's assumptions with respect to residential retail toll service price changes in the Public Notice, at 16, appears to be erroneous. The data above is as it appears on the worksheet entitled "Assumptions" in the Staff Model.

In the business market, the Staff Study assumes that business switched toll revenues per minute have declined and will decline at the following rates:

Date	Annualized Rate of Change Business Interstate Switched Toll Revenues[6]
January 2001	-25 %
January 2002	-20 %
January 2003	-15 %
January 2004	-6 %
January 2005, and after	-3 %

These assumptions regarding interstate switched toll revenue are extremely conservative, particularly in light of the emergence of flat-rate, "all-you-can-eat," calling plans, which have the practical effect of reducing revenue per minute with additional customer usage. If VoIP services are also offered on a flat-rate basis (as the Vonage offerings are), this trend is likely to accelerate. The basis for the Staff's projection of such a sharp deceleration in toll price declines is not clear. Increasing the rate of revenue-per-minute decline for interstate switched toll services above the levels assumed by the Staff will further shrink the contribution rate, and further increase the projected contribution factors.

In addition, toll revenue per minute, as well as the revenue per unit for other services, will also likely decline as carriers shift the allocation of revenues within bundles in response to customer demand. The Staff Study understandably does not expressly take

[6] The description of the Staff's assumptions with respect to residential retail toll service price changes in the Public Notice, at 16, appears to be erroneous. The data above is as it appears on the worksheet entitled "Assumptions" in the Staff Model.

into account whether wireline carriers will reallocate revenues currently labeled as "interstate" to intrastate or non-regulated portions of a bundled package. CLECs and IXCs, which are non-dominant, as well as ILECs with respect to services under Phase I or Phase II pricing flexibility, have broad discretion as to how to package and price their products. To the extent this "repackaging" accelerates, wireline interstate and international revenues would drop even more sharply than the Staff Study already projects.[7]

The published results of the Staff Study assume that the Commission maintains the *status quo* with respect to ADSL revenues. However, that question is currently pending in the *Wireline Broadband Internet Access Framework NPRM*.[8] The Staff Model appropriately allows this assumption to be modified, both to include ADSL and cable modem revenues, and to exclude ADSL revenues.

2. CMRS Interstate Allocated Revenues.

The Staff Study assumes that, with a "safe harbor" of 28.5 percent, CMRS providers will allocate 22.3 to 22.4 percent of total telecommunications revenues to the USF contribution base of "interstate telecommunications revenues." However, given that there were some wireless carriers that were already using their own company-specific allocator when the "safe harbor" was 15 percent, and that the Commission has allowed wireless carriers to recover contributions from end users irrespective of actual end user

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[7] *See Staff Study* at 16.

[8] *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities; Universal Service Obligations of Broadband Providers; Computer III Further Remand Proceedings: Bell Operating Company Provision of Enhanced Services; 1998 Biennial Regulatory Review - Review of Computer III and ONA Safeguards and Requirements*, Notice of Proposed Rulemaking, 17 FCC Rcd 3019 (2002) ("*Wireline Broadband Internet Access Framework NPRM*").

interstate usage, it is likely that a significant number of wireless carriers will be using company-specific allocators rather than the "safe harbor." A more reasonable estimate over time is likely 20 percent.[9]

C. Projections of Telephone Numbers and Special Access/Private Line Connections.

1. Numberless VoIP

The Staff Study assumes that by the end of 2007, 15 percent of business local exchange service will be provided via broadband Internet access, and apparently that when a business uses a broadband connection for voice service, it will cease using a telephone number.[10] This assumption, which the Staff stated "represents a conservative assumption . . . and is incorporated primarily to test the robustness of the proposed methodologies," is likely to be far too conservative.[11] DID numbers and Centrex

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[9] The FCC's preliminary report of 499-Qs filed for the Fourth Quarter 2002 shows wireless carriers reported 23.3 percent of revenue as interstate. *See* Industry Analysis & Technology Division, Wireline Competition Bureau, *Telecommunications Industry Revenues 2001*, Table 16 (rel. Mar. 20, 2003) ("*Telecommunications Industry Revenues 2001*"). However, the Commission is not using Fourth Quarter 2002 data for any universal service contribution calculations, and the data was also reported at approximately the same time that the Commission adopted its reconsideration order permitting wireless carriers to apply a company-specific factor in calculating USF recovery fees, irrespective of actual interstate usage. *See Federal-State Joint Board on Universal Service; 1998 Biennial Regulatory Review – Streamlined Contributor Reporting Requirements Associated with Administration of Telecommunications Relay Service, North American Numbering Plan, Local Number Portability, & Universal Service Support Mechanisms; Telecommunications Services for Individuals with Hearing & Speech Disabilities, & the Americans with Disabilities Act of 1990; Administration of the North American Numbering Plan & North American Numbering Plan Cost Recovery Contribution Factor & Fund Size; Number Resource Optimization; Telephone Number Portability; Truth-in-Billing & Billing Format*, Order & Order on Reconsideration, FCC 03-20 (rel. Jan. 30, 2003) ("*Wireless Clarification Order*"), at *11 (¶ 8). Thus, the Fourth Quarter 2002 percentage of CMRS revenue reported as interstate may not be representative of actual reporting under the current contribution mechanism.

[10] *See* Staff Study at 13, 18.

[11] *Id.* at 13.

extensions are important business tools, and even consumer market companies like Vonage are providing telephone numbers to their VoIP customers.

2. Special Access and Private Line Connections.

The Staff Study appears to underestimate the likely growth in special access and private line connections. The Staff Study projects that these connections will grow at only 2.87 percent per year. This is far lower than carrier reported growth in voice-grade equivalents for these types of connections for 2001-02.[12] AT&T believes that a more reasonable growth rate for special access and private line connections for 2003-07 would be 10 percent per year.

3. Uncollectibles.

The Staff Study appears to overstate the amount of uncollectibles that carriers would include in their modified 499-Qs under a numbers and special access-private line connections-based mechanism, and therefore incorporated into a USAC calculation of the per number assessment rate. As reflected in the carriers' projected uncollectibles reported for the first two quarters of 2003, uncollectibles for interexchange carriers are much higher than for wireless carriers or LECs: in the second quarter of 2003, ILECs projected slightly less than 2 percent uncollectibles, and wireless telephony providers projecting 2.8 percent uncollectibles, as compared with 4.3 percent uncollectibles for interexchange carriers.[13] These reports indicate that it is likely that the uncollectibles under AT&T's proposal would be lower than the 4 percent assumed in the Staff Study.

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[12] *See* Exhibit 3.

[13] *Telecommunications Industry Revenues 2001* at Table 18; *see also* Verizon Telephone Cos., Tariff Transmittal No. 252, Description & Justification, Appendix B at 3 (filed Oct. 15, 2002) (projecting approximately 2 percent uncollectibles).

D. IXC Presubscription and Household Usage.

The Staff Study also assumes that 99 percent of households have presubscribed long distance service. However, TNS data now show that approximately 19 percent of households do not have presubscribed long distance service.[14]

[14] *See* Exhibit 2.