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

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	

To: The Federal-State Joint Board

SPRINT JOINT BOARD REPLY COMMENTS

Sprint Corporation, on behalf of its local, long distance and wireless divisions ("Sprint"), submits these reply comments in response to the submissions filed regarding possible revision to the rules governing high-cost universal service support in rural areas, including areas where a competitive eligible telecommunications carrier ("ETC") is providing services.[1]

I. ALTHOUGH VOLUMINOUS, THE RECORD IN THIS PROCEEDING PAYS SCANT ATTENTION TO CORE ISSUES THAT MUST BE ADDRESSED BY THE JOINT BOARD AND THE FCC

The record in this voluminous proceeding conveys highly divergent views as to what ails the Universal Service Fund and how the fund can be saved. Numerous rural incumbent local exchange carriers ("ILECs") and their supporters oppose any changes to the USF program insofar as it may apply them.[2] Simply put, these parties principally argue that the solution to fund

[1] *See Public Notice,* Federal-State Joint Board on Universal Service Seeks Comment on Certain of the Commission's Rules Relating to High-Cost Universal Service Support and the ETC Designation Process, CC Docket No. 96-45, FCC 03J-1 (Feb. 7, 2003), 68 Fed. Reg. 10429 (March 5, 2003)("*ETC Public Notice*"). *See also Federal-State Joint Board on Universal Service,* CC Docket No. 96-45, *Order,* FCC 02-307, 17 FCC Rcd 22642 (Nov. 8, 2002)("*FCC Referral Order*").

[2] *See* generally Comments of OPASTCO at 15; USTA at 22-27; GVNW at 11; ICORE at 6; and Washington Independent Telephone Association at 9-20.

growth is to make it more difficult for competitive ETCs to receive universal service subsidies.[3] On the other hand, competitive providers, including Commercial Mobile Radio Service Providers ("CMRS") like Sprint, suggest that the Joint Board and the Commission must be guided by the Communications Act, as amended, and the requirement that any USF program comport with the principle of competitive neutrality.[4] With very few exceptions, however, most commenters in this proceeding fail to put forth solutions to continued USF growth – which almost all acknowledge is a concern for the long-term viability of the fund.[5]

Sprint submits that the Joint Board and the FCC must divert their attention from additional short-term or "interim" solutions to the USF crisis. Instead, the Joint Board and the FCC should focus on real reforms in the manner in which USF is administered and, more importantly, the way in which funds are disbursed. Until USF policy decisions are governed by a long-term view of the program, the above-referenced proceeding will remain in crisis mode and most stakeholders will continue to espouse the same well-worn positions.

II. UNIVERSAL SERVICE AND COMPETITION ARE NOT CONFLICTING GOALS

Although Sprint urges the Joint Board and the Commission to focus on longer term reform, it must first reiterate a core principle of its position on this matter: the Joint Board should not countenance the "false choice" between competition and universal service put forth by some rural ILECs in their proposals to restrict multiple ETCs from operating in certain markets.[6] Get-

[3] *See* generally Comments of Montana Telecommunications Association at 11-12; Century Tel at 5, 20-24; ACS at 10; Texas Statewide Telephone Cooperative, Inc. at 12-13; Washington Independent Telephone Association at 17.

[4] Comments of Sprint Corporation at 1-2; Comments of Western Wireless at 2-4.

[5] As Sprint noted in its comments, USF is growing at a rapid rate and at its current pace the size of the fund will increase to approximately $7.4 billion in 2007. Sprint Comments at 4. Others estimate that the fund will grow even more dramatically. *See* Comments of OPASTCO at 10 (fund with grow by yet another $2 billion – if all eligible CMRS providers begin receiving support as well).

[6] Sprint Comments at 2.

ting past this misguided proposal is critical to the adoption of a long-term solution that will make universal service support "specific, sufficient and predictable" as required by the Act.[7]

In its initial comments, Sprint thoroughly addressed this false choice. At its root, this argument suggests that granting ETC status to more than one provider in a given area is, at best, problematic and, at worst, a recipe for disaster in which existing rural carriers face financial ruin and the size of the Federal fund spirals upward out of control.

OPASTCO, for example, states that inter-modal competition already exists in rural areas and therefore the granting of ETC status to encourage competition is unnecessary.[8] OPASTCO also claims that if one CMRS provider is granted ETC status then others will follow in order to "remain competitive." Similarly, USTA notes that if Congress had intended multiple ETCs to provide service in high-cost areas served by rural ILECs it would have somehow limited the number of potential ETCs in an area in order to limit the amount of explicit support required.[9] In making these arguments both OPASTCO and USTA depict a worst-case scenario in which large numbers of ETCs compete with each other in highly rural areas – all driven by the pursuit of Federal USF dollars. But, as discussed more fully below, an economic analysis does not support such a nightmare scenario.

There is no debate that both wireline and wireless providers experience significant economies of scale when they provide the services supported by the Federal Universal Service Fund. Providers experience these economies of scales in every geographic area – urban or rural – in which they offer service. When any good or service has a production function that is characterized by significant economies of scale it is an economic fact that, all else held equal, the

[7] *See* 47 U.S.C. 254(b)(5).

[8] OPASTCO Comments at 3.

[9] Comments of USTA at 11.

market will tend to be served by fewer firms, as opposed to many firms. Natural monopolies represent the extreme example of this phenomenon: economies of scale are so significant that it is most efficient for a single firm to serve the entire market.

The natural monopoly case is technology-specific and service-specific. If two firms use different technologies to offer competing, but not identical services, and each technology exhibits economies of scale, then the market will be divided between the two competing providers based upon customer perception and customer preference. Although each firm will operate with spare capacity, such a result is, in fact, economically efficient. It is economically efficient because any inefficiencies that are created by each firm operating with spare capacity are outweighed by the *benefits that consumers enjoy by having a choice of providers and differentiated products.*[10]

However, because the firms exhibit economies of scale, it is not possible to increase the number of firms (and increase customer choices) *ad infinitum.* If additional firms enter the market the spare capacity of each provider will increase. A point will be reached very quickly where (1) the inefficiencies caused by the increased spare capacity are not outweighed by the benefits of increased customer choice and (2) the amount of spare capacity is too great for any individual provider to bear. At such a point, the market approaches equilibrium. The number of firms offering the differentiated-but-substitutable services will be greater than one, but it will not be a large number when economies of scale are present. The actual number will depend on the size of the market being served: the smaller the market, the smaller the number of firms. Therefore, market forces (supply, as determined by the technologies of firms, and demand, as determined by

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[10] For example, both cable television and satellite television enjoy significant economies of scale and each might be said to exhibit characteristics that make it a natural monopoly. But as long as customers perceive differences between the two, a single geographic market will have demand for each, and the result is efficient despite spare capacity.

customer preferences) will set a limit on the number of providers that will offer service in any region, rural or urban.

These basic economic tenets demonstrate that the nightmare-scenario suggested by USTA and OPASTCO will not occur. The economies of scale that both wireline and wireless carriers enjoy will set a limit on the number of providers that will offer service in any rural region. Moreover, these economies of scale extend well beyond the simple technical requirements of the service; they extend to activities such as marketing and customer service. Because of this, a point will be reached where it simply makes no sense for a carrier to enter a market that is already served by two or three providers offering substitutable, but not identical service.

The accuracy and applicability of these economic facts is borne out by the state of competition in the national CMRS market. Numerous industry commentators suggest that the CMRS market as a whole may soon experience significant consolidation because the market cannot support five or six separate providers of national wireless service.[11] A reduction in the number of firms is largely seen as inevitable and economically desirable. This consensus begs the question: if the entire country cannot support five or six separate wireless providers, how can a single rural market (consisting of, perhaps, fifteen hundred customers) possibly support a large number of ETCs – wireless or wireline?

Assuming *arguendo* that it was permissible to discriminate against certain providers as they seek ETC status, such restrictions are not necessary to limit the number of ETCs that will

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[11] *See, e.g.,* Written Statement of Kathleen Q. Abernathy, The State of Competition in the Telecommunications Industry, Before the Senate Committee on Commerce, Science and Transportation, at 1 (Jan. 14, 2003)("[A]s wireless providers struggle to achieve or maintain a positive cash flow, some analysts have argued that the wireless sector may be *too* competitive – that is, that some consolidation may be necessary to restore its fiscal health.")(emphasis in original); Merrill Lynch, The Next Generation VI: Wireless in the U.S., at 1 and 2 (March 8, 2002)("With growth slowing, with pricing declining, and with capital intensity remaining high, six (or five plus Nextel depending on how you want to think about it) national competitors are really just too many. . . . There is no question that the US wireless industry needs to consolidate.")

operate in rural markets.[12] The characteristics of the firms providing the services, combined with the preferences of customers, will effectively limit the number of firms, and will do so in a manner that is both efficient and market-specific.

The fact that firms will be limited by market-specific factors is of critical importance. Because market characteristics (such as demand) vary from location to location, it may be that one rural market can successfully support three providers while another might only support two. The proper number of providers is the number that any individual market can support. To impose regulation that artificially limits the number of providers, and does so in an arbitrary, overly-broad manner, denies markets the ability to operate effectively and meet customer demand as efficiently as possible. The end result of such unnatural restrictions is detrimental to rural consumers, since they will be deprived the innovative features and advanced services – not to mention mobility – that wireless providers offer.[13]

III. FUNDAMENTAL ISSUES THE JOINT BOARD SHOULD CONSIDER

In its comments Sprint identified two areas that the Joint Board should investigate as a means of providing some stability in the continuing growth of USF disbursements and in better ensuring that USF support is targeted more narrowly.[14]

A. THE JOINT BOARD SHOULD CONSIDER THE POSSIBLE USE OF A VOUCHER-BASED HIGH-COST PROGRAM

Sprint reiterates its suggestion that the Joint Board investigate the alternative of a customer voucher system. A voucher system is appealing because it is the one approach that is guaranteed to be competitively neutral since no service provider would receive USF subsidies

[12] Western Wireless demonstrates that portability (*i.e.,* non-discriminatory treatment of ETCs) is dictated by the Act. *See* Western Wireless Comments at 5-6.

[13] *See* Western Wireless Comments, Attachment E, *The Public Interest is Served by the Designation of Competitive Eligible Telecommunications Carriers.*

[14] Sprint Comments at 14.

directly. And, as Sprint noted in its comments, the extensive administrative costs associated with the current system (*e.g.,* cost studies, reporting requirements) would be eliminated, possibly allowing carriers to reduce the prices they charge customers for their services.[15] Sprint does not support the specifics of SBC's "affordability benchmark" proposal at this time; however, the concept of linking end users' ability to pay to the calculations of USF subsidies is worth exploring further.[16] The suggestion of Western Wireless that the Joint Board and the Commission consider allocating portable vouchers or "phone stamps" to consumers also merits broader discussion.[17]

Although there are difficulties associated with any plan to alter dramatically the USF regime, it is incumbent upon the Joint Board and the Commission to give full consideration to longer-term solutions to the USF dilemma, even if these approaches appear radical. Customer vouchers may be such a solution.

B. THE JOINT BOARD SHOULD RECOMMEND ADOPTION OF A MINIMUM PRICE FOR LOCAL SERVICE AS A CONDITION OF RECEIVING FEDERAL SUPPORT

Sprint also encouraged the Joint Board to "commence a public discussion regarding establishment of a minimum price for local service as a condition to receipt of USF support – and further modifying the USF program so that support levels reflect the higher revenues received by moving to a more cost-based system of universal service pricing."[18] Establishing a "minimum price condition" would help control the size and growth of the high cost program – and it would facilitate competitive entry in rural areas because incumbent ETCs would begin charging prices that are closer to their costs of service. Consistent with Sprint's comments, the rate disparity for

[15] Sprint Comments at 15.

[16] Comments of SBC Communications at 6.

[17] Western Wireless Comments at 18.

[18] Sprint Comments at 15-16.

local services clearly suggests that some high costs states could increase their rates for local service without having a major impact on telephone penetration rates.[19] Although the idea of rate rebalancing (*i.e.,* allowing local rates to approach costs) may not be attractive politically, the future viability of the fund requires hard choices and decisive action. Again, SBC's affordability concept may be relevant to Joint Board/Commission consideration of this issue. Similarly, Western Wireless recommends consideration of imposing a cap on the growth of the total amount of funding available to all ETCs in each competitive study area, and exploring alternative means of allocating funding among ETCs.[20]

In light of mounting pressure on the fund and unprecedented growth, Sprint again urges the Joint Board to consider recommending establishment of a national price for local service as a condition to receipt of federal USF support. Ultimately, it is consumers that bear the burden of a USF program that continues to grow without proper controls. The assessment imposed on consumers today is over 9% of interstate revenues and is likely to increase.[21] By recommending full consideration of longer-term solutions to problems facing the USF program, the Joint Board will properly consider not only the beneficiaries of USF subsidies, but also the consumers that bear the burden of these subsidies.

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[19] Sprint Comments at 16-17.

[20] Western Wireless Comments at 18.

[21] *See e.g.,* Public Notice, *Revised Second Quarter 2003 Universal Service Contribution Factor*, CC Docket No. 96-45 (March 21, 2003).

IV. CONCLUSION

For the foregoing reasons, Sprint Corporation respectfully requests that the Joint Board consider the positions set forth above.

Respectfully submitted,

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