Before the
Federal Communications Commission
Washington, D.C. 20554

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

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Introduction and Summary

Most commenters agree that something must be done to control growth of the high cost fund. However, many of the proposals offered would not effectively control growth, and could even lead to a greater increase in funding requirements. Verizon has proposed several measures – including a primary line limitation, freeze on per-line support to rural study areas upon entry of a competitive ETC, and the adoption of a presumption that it is not in the public interest to have more than one ETC per high cost rural study area – that, working together, could begin to bring the growing mountain of universal service expenses under control. Half-hearted measures will not work. Unless something is done to dramatically pull in the reins on universal service spending, carriers (and thus consumers) soon will face the prospect of paying a double-digit contribution factor.

The Commission should reject suggestions that, in an attempt to control the number of ETC applications and create regulatory parity between ILECs and their competitors, would end up imposing burdensome regulations on wireless carriers. The Commission should instead work toward the elimination of those regulations from *all* carriers, consistent with the deregulatory command of the Act.

Argument

I. The High Cost Fund Will Continue to Grow Dramatically Unless the Commission Takes Action Sufficient to Control Growth

Commenters largely agree that something must be done to control the size of the high cost fund. Rural ILECs point to the growing amount of support to competitive ETCs, which some parties have suggested could climb as high as $2 billion per year in additional funding.[1] Competitive ETCs, for their part, counter that the largest portion of funding still goes to rural ILECs, and that the current regime does not create incentives for rate-of-return carriers to control costs or otherwise limit universal service funding.[2] The fact is that both situations present a potential source of ballooning the universal service fund.

The largest portion of high cost funding goes to rural ILECs.[3] In 2004, it is projected that rural ILECs will have just under 13% of working high cost loops, but will receive over 80% of the high cost funding for loops.[4] 1347 out of 1433 incumbent study areas are rural.[5] Moreover, because of the way that universal service support to rural carriers is calculated, as they lose lines to competitors, the level of support they receive does not necessarily change.[6]

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1 *See* AT&T Comments, at 5 (quoting OPATSCO, Comments to Joint Board, CC Docket No. 96-45, at 10 (filed May 5, 2003)).

2 *See, e.g.*, CTIA Comments, at 6-8; Comments of General Communication, Inc., at 11, 14.

3 *See* Universal Service Administrative Company, *Federal Universal Service Support Mechanisms Fund Size Projections for the Fourth Quarter 2004* (filed Aug. 2, 2004) ("USAC Fourth Quarter Report"), *available at* http://www.universalservice.org/overview/filings/ (projecting that by fourth quarter 2004, rural ILECs will receive approximately $632 Million per quarter in high cost funding).

4 USAC Fourth Quarter Report, at Appendix HC01.

5 USAC Fourth Quarter Report, at 6.

6 *See Federal-State Joint Board on Universal Service*, Recommended Decision, 19 FCC Rcd 4257, ¶ 78 (2004) ("Recommended Decision").

Although competitive ETCs claim that they still represent only a small portion of high cost funding, their numbers are growing dramatically. In 1999, competitive ETCs were receiving \$535,000 per year, or .03% of high cost support; by 2003, they were receiving \$131 million (4%), and as of the middle of 2004, they had received almost that much (\$119 million) in the first half of the year alone, and accounted for 7% of funding.[7] Annualized, that represents a 55% increase in funding to competitive ETCs between 2003 and 2004. Moreover, the potential for future growth is enormous. As of the fourth quarter, there are competitive ETCs operating in 516 rural high cost study areas, with another 266 study areas subject to future competitive ETC entry.[8]

In opening comments, Verizon proposed several measures that, if adopted, could effectively control growth from both sources. Specifically, the Commission should:

- Establish a rebuttable presumption that it is not in the public interest to grant more than one ETC per rural study area;
- In rural areas, institute a primary line limitation on support when a competitive ETC is designated in the study area, and initially "rebase" support for rural ILECs to avoid rate shock;
- Freeze per-line support to all rural study areas, similar to the suggestion proposed by the Rural Task Force in 2000; and
- Adopt guidelines to assist the states in determining, in both rural and non-rural areas, whether it is in the public interest to designate additional ETCs.

Verizon Comments, CC Docket No. 96-45, at 3 (filed Aug. 6, 2004) ("Verizon Comments"). Although commenters criticize aspects of these proposals, none of those criticisms are sufficient to stop the Commission from adopting effective means to control the growth of the

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7 *See* Chart, "High Cost Support Mechanism: Disbursements to CETCs 1998 through 2Q2004," *available at* http://www.universalservice.org/hc/download /pdf/HC%20Disbursements.pdf.

8 USAC Fourth Quarter Report, at 6 and Appendices HC01, HC03, HC18, HC 19 and HC 20. In initial comments, Verizon stated that only 140 of 1487 total rural study areas – 9.4% – would currently be at risk for losing support to competitive ETCs. Verizon Comments, at 16-17. Those numbers were incorrect. In reality, it should be 516 of 1347 study areas, or 38%. USAC Fourth Quarter Report, at 6 and Appendices HC01, HC03, HC18, HC 19 and HC 20.

fund size. *See* Sections II, III, *infra*. Moreover, many of the "alternatives" to these proposals do little or nothing to check growth, and in many cases may actually lead to an increase in funding. *See* Section IV, *infra*.

The Commission should adopt the proposals set forth above, and look for additional ways to control the size of the high cost fund. For example, after issuing the Notice of Proposed Rulemaking in this proceeding, the Commission issued an order requesting the Joint Board to reexamine the rules relating to the mechanism of support to rural carriers. *See Federal-State Joint Board on Universal Service*, Order, 19 FCC Rcd 11538, ¶ 1 (2004). That proceeding should be used as a vehicle to further explore whether there are other ways that the system can be modified to further control growth of the fund, while continuing to ensure appropriate levels of support.

II. A Primary Line Limitation Is Consistent With the Purposes of the Statute, and Can Be Made Administratively Workable

A. Universal Service Support Should Be Targeted to Meet the Basic Goals of the Act

Some commenters have claimed that competition is one goal that should be subsidized by high cost funding. *See, e.g.,* Alltel Comments, at 2-4; Dobson Cellular Comments, at 3; General Communications, Inc. Comments, at 5-9. This is not correct. The goal of universal service support is to provide consumers in high-cost areas with access to a certain level of services, at rates comparable to urban areas. *See* 47 U.S.C. § 254. As more than one commissioner has recognized, it makes little sense to subsidize "multiple competitors to serve areas in which the costs are prohibitively expensive for even one carrier."[9]

Others assert that if there is any type of limitation on support, the fund size will not be "sufficient." *See, e.g.,* NECA Comments, at 5-6; Comments of Fred Williamson, at 38. This also is incorrect. When it is first implemented, the primary line plan will recalculate the amount of support to be provided to rural carriers, so they do not experience a decrease in support when the plan is initially implemented. *See* Verizon Comments, at 15-17.[10] To the extent the funds will not continue to grow in the future (if there is a freeze on per-line support upon competitive ETC entry) or will be reduced as ILEC lines are captured by a competitor, the fund will gradually require rural ILECs to become more efficient in the face of competition, or face being replaced by competitors who can operate more efficiently.

Similarly, commenters opposing a primary line limitation on support argue that it would not allow rural customers to access services and rates that are "comparable" to those available to urban customers. *See, e.g.*, Fred Williamson Comments, at 38. However, as the Joint Board

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9 *MAG Plan Order*, Separate Statement of Commissioner Kevin J. Martin, 16 FCC Rcd 19613, at 19746 (2001); *see also* Jonathan S. Adelstein, Commissioner, FCC, Remarks before the National Association of Regulatory Utility Commissioners (Feb. 25, 2003), *available at* http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-231648A1.pdf; *see also*, *See Federal-State Joint Board on Universal Service*; *Virginia Cellular, LLC Petition for Designation as an Eligible Telecommunications Carrier in the Commonwealth of Virginia*, Separate Statement of Chairman Michael K. Powell, 19 FCC Rcd 1563, at 1590 (2004) ("Despite the importance of making rural, facilities-based competition a reality, we must ensure that increasing demands on the fund should not be allowed to threaten its viability") ("Virginia Cellular Order").

10 The initial level of support would be calculated by rebasing the current level of per-line support, multiplied by the number of primary lines per carrier. Rural high cost support would be calculated based on primary lines to determine total rural high cost support. For example, if an ILEC were receiving $10 per line per month for 10,000 total lines, or $100,000 per month in high cost support, under the initial rebasing formula, if 8,000 of those lines were primary, its level of support would be increased to $12.50 per [primary] line per month so it would continue to receive the same total ($100,000) in rebased support. *See* Verizon Comments, at 15-17; Recommended Decision, at 56.

found, "[s]upporting a single connection provides access to all of the services included in the definition of universal service under section 254(c), because each ETC is required to provide all of the supported services." Recommended Decision, ¶ 62. "Thus, supporting multiple connections is not necessary to achieve reasonably comparable access in rural areas." *Id.* Because wireless ETCs have a different business model (providing multiple handsets per household), and because customers often choose to add these services, rather than substitute them for existing wireline service, designation of new ETCs in rural areas could lead to a tremendous increase in the *quantity* of service being subsidized in those areas. It is therefore necessary for the Commission to adopt some reasonable limit on the quantity of service to be subsidized in a rural area where more than one ETC has been designated.

Some commenters have challenged any limitation on support, suggesting that it will hurt broadband deployment in rural areas. *See, e.g.*, NTCA Comments, at 8-9. However, to the extent these commenters are suggesting that universal service funds have been used to fund *broadband* facilities, rather than facilities that fall within the basic definition of universal service, that is improper. The statute states that universal service support shall be used "*only* for the provision, maintenance, and upgrading of facilities and services *for which the support is intended*." 47 U.S.C. § 254(e) (emphasis added). Broadband service is not within the Commission's definition of services supported by universal service.[11] Other programs exist to encourage broadband deployment in rural America.[12] Universal service funds in high cost areas are not designed to subsidize such investments.

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11 *See Federal-State Joint Board on Universal Service,* 12 FCC Rcd 8776, ¶ 22 (1997).

12 *See, e.g.*, United States Department of Agriculture, Rural Utilities Service Broadband Loan and Loan Guarantee Program, information *available at* http://www.usda.gov/rus/telecom/broadband.htm.

Moreover, universal service principles are a balancing of different concerns. Those commenters who oppose any realistic limits on high cost funding ignore the fact that the Commission must also ensure that the fund size is sustainable, and will not become so large as to encumber all Americans with universal service costs that make rates no longer "affordable." *See* 47 U.S.C. § 254(b). The current trend of growing universal service costs simply cannot be allowed to continue indefinitely. The Joint Board properly determined that a primary line limitation "is necessary to preserve the sustainability of the universal service fund." Recommended Decision, ¶ 3.

B. Although the Commission Should Work to Minimize Administrative Difficulties With a Primary Line System, None of the Problems Identified Are Insurmountable

Although a number of commenters identify administrative difficulties with implementing a primary line plan, none of them make such a program unworkable. Some of the criticisms – for example, questions about how to define "primary line" and how to address concerns with carriers who might attempt to game the system, or slam customers – also could be made of other existing regulatory systems.[13] They are not unique to a primary line proposal. Indeed, one universal service program – Lifeline – already limits support to one line per customer.[14]

Having USAC administer the system would reduce many of these potential problems, because it would provide a central source for collecting and validating data. In fact, while USAC has identified some questions that must be answered in implementing any primary line approach,

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13 *See* Recommended Decision, ¶ 81 & n.297 (agreeing with one commenter, which pointed out that "rules distinguishing between primary and other connections are not unprecedented, and the Commission has successfully implemented regulatory initiatives involving consumer choice" and citing examples).

14 *See Federal-State Joint Board on Universal Service*, Recommended Decision, 18 FCC Rcd 6589, ¶ 4 (2003); 47 CFR § 54.411(a)(1).

it also has suggested methods for solving some of those problems.[15] Other commenters also have offered practical solutions for minimizing some of the concerns raised. For example, Verizon proposes that initial balloting only be made in those areas where there exists at least one competitive ETC, and only to customers of the competitive ETC; otherwise, the rural ILEC can self-identify the number of primary lines.[16] Regardless, concerns that some may try to abuse a newly implemented system should lead to more stringent measures to control against such potential abuses; they are not sufficient to prevent the Commission from adopting it in the first place.[17]

Moreover, the plan Verizon set forth reduces many of the administrative difficulties, by minimizing the areas in which primary line designation will be necessary. If the Commission were to adopt a rebuttable presumption that there should be only one ETC per study area, and implemented a primary line approach only in those rural study areas where there exists more than one ETC, that would dramatically reduce the number of study areas in which primary line must be adopted. *See* Verizon Comments, at 15-17. The Commission also should not adopt a primary line proposal in non-rural areas (including non-rural insular areas), which do not present the same concerns with potential expansive funding growth. *Id.*, at 19-21.

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15 *See* USAC Comments, at 6-19. For example, USAC recommends that primary line data be submitted to it directly, so it can review and manage the data prior to making payments, as well as have the ability to audit the data. *Id.*, at 9. It also proposes to conduct outreach to carriers and consumers about the impacts of a primary line system. *Id.*, at 12.

16 Verizon Comments, at 17. This would minimize administrative burdens associated with the initial determination of which line is considered "primary." *See also* Comments of the People of the State of California and the Public Utilities Commission of the State of California, at 9-10 (explaining procedures California has undertaken to certifying residential primary lines for a state program); Comments of the National Association of State Utility Consumer Advocates, at 23-27 (offering proposals for designation of primary lines).

17 *See* USAC Comments, at 6 ("Although the administrative issues may be more or less challenging depending on the approach selected by the Commission, USAC stands ready to implement any changes to current policy that may result from this proceeding").

III. The Commission Also Should Undertake Other Measures to Control Growth, Including Adoption of the Rural Task Force Suggested Freeze, and Adopting a Presumption of One ETC Per Study Area

As Verizon explained in prior comments, two other measures that the Commission could adopt to control growth of the high cost fund are (a) adopting a presumption that it is in the public interest to have only one ETC per rural study area; and (b) freezing per-line support to rural study areas upon entry of a competitive ETC.

A. Adopting A One-ETC-Per-Study-Area Presumption Would Control Growth Better Than Benchmark Proposals, And Is Most Effective If Combined with the Primary Line Limitation and a Freeze on Per-Line Support

Verizon has suggested that the Commission adopt a presumption that it is not in the public interest to fund more than one ETC per high cost rural study area. Verizon Comments, at 9-14. Some other commenters support a similar "benchmark" on the number of ETCs per study area.[18] However, to the extent these benchmarks allow more than one ETC per study area, they do not do much to control growth of the fund size. Likewise, a benchmark alone without other measures – such as a cap on per-line support, or primary line limitation – will not sufficiently control growth.[19]

Some have suggested that limiting the number of ETCs that can receive support in study areas is not competitively neutral.[20] However, that is not correct. To the extent that a competitive ETC can demonstrate that it is a better alternative than the rural ILEC, it can become the default ETC for that area.[21] Regardless, as stated above, the goal of universal service is to

18 *See, e.g.*, CenturyTel Comments, at 17-18.

19 *See generally* Recommended Decision, ¶ 78 (explaining how the fund size could continue to grow without a cap on per-primary line support).

20 *See, e.g.*, CTIA Comments, at 12-13.

21 Recommended Decision, ¶¶ 77-80.

provide basic access to consumers in rural areas, not to fund "competition" in areas where it is prohibitively expensive for even one carrier to operate. *See* Section II, *supra*; *see also* Verizon Comments, at 9-14.

B. Adopting a Freeze on Per-Line Support Will Not Undermine Rural ILECs, But Will Encourage Them To Use Universal Service Funding More Efficiently

The Joint Board also recommended adopting the prior suggestion of the Rural Task Force, to freeze per-line support in a study area upon entry of a competitive ETC. Recommended Decision, ¶ 77. Without a freeze, as the rural ILEC loses lines to a competitor, the amount of universal service support received in that area may continue to *increase*, even with the adoption of a primary line approach. This is so because, as the rural ILEC loses lines, its per-line support could be increased to cover the reduction in funding, and both the ILEC and competitor would receive support at the higher per-line rate. *See* Recommended Decision, ¶ 78.

The arguments opposing a cap on per-line support are similar to those opposing a primary line system: a lack of guaranteed support to the rural ILEC, which would either lead to an increase in ILEC rates, or an inadequate base of funding. *See, e.g.*, Comments of John Staurulakis, Inc., at 10-12. However, the freeze would not initially reduce the amount of support an ILEC receives, unless the ILEC loses a significant number of lines to a competitor. In that sense, the situation faced by the rural ILEC will not be unlike that of the ILECs that moved to price cap regulation. They have had to cut costs and operate more efficiently, or face being supplanted by intermodal competitors.

IV. Alternative Proposals Are Not Sufficient to Control Growth of the High Cost Fund, and the Commission Should Not Allow the ETC Process to Become a Way for Imposing Unnecessary Regulations on Wireless Carriers

Some commenters have suggested that instead of adopting a primary line limitation or any type of cap on high cost support, that the Commission instead create more stringent guidelines for designating additional ETCs. *See, e.g.*, NECA Comments, at 18-19. Verizon supports the adoption of some of the guidelines proposed by the Joint Board. *See* Verizon Comments, at 14-15. The Commission should also make it clear that any public interest analysis must rely on facts, not boilerplate assertions. *Id.* And, as the Commission already has recognized, there must be a public interest analysis before designating ETCs in both rural and non-rural areas.[22]

However, setting new standards for the public interest analysis cannot, standing alone, do much to stem the flood of growing ETC designations. Even the Commission's own recent experience demonstrates as much. Earlier this year, the Commission issued a pair of orders, setting more stringent guidelines that ETCs must meet.[23] However, since those orders were released, the Commission has issues orders on ten petitions seeking ETC status in various states; eight were granted in their entirety, and the remaining two were partially granted.[24] In addition,

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22 *See Virginia Cellular Order* ¶ 26. Commenters who claim that the public interest analysis should not apply to non-rural areas, *e.g.*, Sprint Comments, at 23-25, are therefore incorrect. The statutory language requires that additional ETC designations in both rural and non-rural areas be "consistent with the public interest." 47 U.S.C. § 214(e)(2), (6). *See* Verizon Comments, CC Docket No. 96-45, at 11-17 (filed June 21, 2004).

23 *See Virginia Cellular Order*; *Highland Cellular, Inc., Petition for Designation as an Eligible Telecommunications Carrier in the Commonwealth of Virginia*, 19 FCC Rcd 6422, (2004).

24 *See, e.g., NPCR, Inc. d/b/a Nextel Partners Petitions for Designation as an Eligible Telecommunications Carrier in Florida, Georgia, New York, Pennsylvania, Tennessee and Virginia,* CC Docket No. 96-45, DA 04-2667 (rel. Aug. 25, 2004); *Federal-State Joint Board on Universal Service, Guam Cellular and Paging Inc. d/b/a Saipancell Petition for Designation as*

regardless of the guidelines adopted, in most cases, states still will be the ones deciding whether or not to grant these petitions, and there is little incentive for them to control federal universal service costs.[25]

Moreover, in an attempt to stem the tide of applications from competitive ETCs, many commenters have suggested the addition of regulations that are not appropriate for wireless carriers and, in many cases, should be eliminated for ILECs as well. For example, some suggestions are that competitive ETCs be required to comply with certain ILEC regulations.[26] However, with the advent of widespread intermodal competition, the Commission should consider eliminating many "dominant carrier" regulations altogether, as ILECs who face competition from CLECs, wireless carriers, cable modem providers, and VOIP can no longer be considered "dominant" in many markets.[27] The Act contemplates that the advent of increased competition should lead to *less* regulation of *all* providers, not a reflexive imposition of outdated, monopoly-era requirements on new entrants.[28]

Some commenters have suggested that the fund size could be reduced by basing support to competitive ETCs on their own costs, rather than giving them the same amount of support that the rural ILEC receives. *See, e.g.*, NTCA Comments, at 13-14. There are several problems with this proposal as well. As an initial matter, it is not clear whether basing support on ETCs' costs

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an Eligible Telecommunications Carrier on the Islands of Saipan, Tinian and Rota in the Commonwealth of the Northern Mariana Islands, 19 FCC Rcd 13872 (2004).

[25] *See* Recommended Decision, Separate Statement of Lila A. Jaber, Florida Public Service Commission ("Some commenters believe that states have used multiple carrier ETC designation as a means to attract more universal service funds into the state").

[26] *See, e.g.*, Comments of Fred Williamson, at 23-32; Western Telecommunications Alliance Comments, at 11-17.

[27] *See, e.g., Petition of Qwest Corporation for Forbearance Pursuant to 47 U.S.C. § 160(c) in the Omaha MSA*, WC Docket No. 04-223 (filed June 21, 2004).

[28] *See, e.g.,* 47 CFR § 161.

would be less than or more than that of the rural ILEC.[29] Experience suggests that the process of estimating different costs for wireline and wireless carriers would not be an easy one. More fundamentally, compensating each ETC on the basis of its own costs would not be competitively neutral, and would effectively insulate competitors with higher costs.

In addition, it is unclear what would happen if the competitive ETC had high fixed costs and a low number of lines; would its level of support increase to cover all of its costs, regardless of the number of consumers served? This proposal could actually lead to an *increase* in the size of the fund, and create incentives for inefficient investment, if the effect of the rule were to give a competitor *more* support than it would have received based on the rural ILEC's costs. Moreover, as discussed above, this could lead to economic regulation of wireless carriers, which the Commission has traditionally recognized should be free from such regulations.[30]

A similar proposal suggests that wireless competitive ETCs be paid $3,000 per month per cell site if the cell site is in a county with populations of less than 100 people per square mile, and the population density "of the area within the cell site itself is less than 50 people per square mile." Commnet Comments, at 2. Again, this proposal creates perverse incentives, and could lead to an increase in funding. By guaranteeing a certain amount of high cost funding per cell site, regardless of the number of customers the ETC serves, and regardless of whether there already exist other facilities to serve customers in such areas, such a proposal could create incentives for carriers to create networks simply to gain high cost funding, rather than based on market conditions or customer need. For example, if the ETC's cell site served one customer,

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29 For example, in many countries where termination rates have been based on cost estimates, those for wireless carriers are higher.

30 *See, e.g.,* 47 U.S.C. § 332(c)(1); *Implementation of Sections 3(n) and 332 of the Communications Act, Regulatory Treatment of Mobile Services,* 9 FCC Rcd 1411, ¶ 173 (1994); *Wireless Consumers Alliance, Inc.,* 15 FCC Rcd 17021, ¶¶ 20-21 (2001).

this would effectively lead to high cost funding of $3,000 per line per month for that cell site, which would be a waste of universal service dollars. In addition, such a proposal would not eliminate the situation where customers are receiving duplicative funding for lines from both the ILEC and the competitive ETC.

Conclusion

The Commission should adopt rules that will control the growth in the rural high-cost fund. It should do so by setting a presumption that it is not in the public interest to grant more than one ETC per rural study area, adopting a primary line limitation on support in rural areas, and capping the per-line support to rural carriers.

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