

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

In the Matter of	)	
	)	
Federal-State Joint Board on	)	CC Docket No. 96-45
Universal Service	)	
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337

**REPLY COMMENTS OF VERIZON**

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**SUMMARY**

In the vast majority of the country, competitive pressure from wireless providers, cable telephony, VoIP providers, and other wireline voice providers has resulted in affordable phone rates for consumers. The current marketplace, therefore, ensures that the statutory goals of section 254 are met in most of the country without the need for universal service subsidies. Furthermore, the record shows that rates in rural areas are affordable and reasonably comparable to those in urban areas. In fact, data produced by Verizon, NASUCA, and other commenters in this proceeding show that rural consumers often pay *less* than urban consumers for wireline phone services.

Despite the fact that competition for voice services is flourishing, the universal service fund continues to grow. This continued growth is not only out of line with marketplace realities; it threatens the long-term viability of the universal service program and endangers the overall affordability of these services to consumers.

To remedy this imbalance, the Commission should eliminate high cost subsidies for both incumbent and competitive carriers in areas where rates provided by incumbent or competitive carriers would be affordable and reasonably comparable without such subsidization. Further, the

Commission should establish a presumption that no high-cost subsidy is appropriate in areas in which a carrier offers rates below the current rate benchmark without high-cost subsidies. And in the limited areas where funding is necessary going forward, the Commission should adopt a competitively neutral, economically efficient mechanism that subsidizes a single provider in a given area. This kind of reform will halt the growth of the fund, better reflect market conditions, and ensure the sustainability of the federal universal service program going forward. In parallel, the Commission should reform the contribution mechanism by adopting a telephone number based system so that all voice providers contribute to the fund in an equitable and competitively neutral way.

The Commission should resist pleas by commenters arguing for a larger or more unwieldy high cost subsidy mechanism. Section 254 does not compel a multi-billion dollar universal service program, and it certainly does not require universal service funding where a competitive market is already satisfying the necessary statutory objectives. Moreover, contrary to certain parties' claims, the Tenth Circuit did not mandate a bigger or more complicated fund. The Tenth Circuit simply required the Commission to consider all the statutory factors, offer a rational explanation for its interpretation of those factors, and demonstrate that its chosen subsidy mechanism advances the statutory goals based on an empirical record. The Commission can and should do so by explaining that competition and technology have replaced the need for subsidy in many "high-cost" areas and crafting a more focused high-cost mechanism that identifies and supports only those areas that require assistance in order to assure affordable and reasonably comparable rates.

**I. THE COMMISSION SHOULD BOTH RETARGET HIGH-COST FUNDING AND REFORM THE CONTRIBUTION MECHANISM TO BETTER REFLECT THE COMPETITIVE MARKETPLACE.**

**A. The Commission Should Retarget Subsidies Only To the Limited Areas Where Subsidization is Necessary.**

**1. The High-Cost Fund Should Assure Affordable and Reasonably Comparable Rates, Not Subsidize Competition.**

The Commission's primary objective in this proceeding must be to update and scale back its high-cost program to reflect current market conditions, while concurrently addressing the Tenth Circuit's concerns. Many commenters warn of the critical need to fundamentally control fund growth.<sup>1</sup> The high-cost fund has more than doubled in less than eight years: from \$1.718 billion in 1998 to over \$4 billion this year. The continued growth of the fund is the starkest evidence that the universal service program has become unmoored from its statutory basis, threatening the affordability of services and the sustainability of the fund itself.

Two years ago, the Joint Board explained that "fundamental changes are occurring in the telecommunications marketplace since the Commission's rules were first adopted in 1997, necessitating a thorough review of how to preserve and advance universal service." *Federal-*

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<sup>1</sup> *Comments of Dobson Cellular Systems, Inc.*, at 4-5; *Comments of Sprint Nextel Corporation*, at 2 ("Sprint Nextel Comments") ("any action the Commission takes in the instant proceeding must be made with a careful eye to the impact such action will have on the size of the fund"); *Comments of Qwest Communications International Inc.*, at 17 ("*Qwest Comments*") ("If the fund is not efficient in providing support, than [sic] the fund may ultimately harm the contributors more then [sic] it aids the benefactors."); *Comments of Vermont Public Service Board, Vermont Department of Public Service, and Maine Public Utilities Commission*, at 8 ("*Vermont and Maine State Commissions Comments*"); *Comments of BellSouth Corporation*, at 22 ("*BellSouth Comments*") (explaining that "if support exceeds what is necessary to preserve and advance universal service through rate comparability, access to affordable telecommunications services may diminish because the price of services increases as universal service charges are passed through to end-users on their monthly bills"); *Comments of CTIA- The Wireless Association*, at 6 ("*CTIA Comments*") (suggesting that the Commission "must consider the burden on universal service contributors in order to ensure affordability").

*State Joint Board on Universal Service Seeks Comment on Certain of the Commission's Rules Relating to High-Cost Universal Service*, Public Notice, 19 FCC Rcd 16083, ¶ 6 (2004) ("2004 Joint Board Notice"). And almost a decade ago, the Commission sought to "facilitate a market-based process whereby each user comes to be served by the most efficient technology and carrier." *Federal-State Joint Board on Universal Service*, Report and Order, 12 FCC Rcd 8776, ¶ 48 (1997) ("*First Report and Order*"). Despite those intentions a growing proportion of universal service funding is being spent not on basic infrastructure needs where customers otherwise would not be served, but to fund duplicative networks and competition.<sup>2</sup>

The Progress and Freedom Foundation has quantified this concern: "Although the costs of providing telephone service have fallen significantly over time, [universal service fund] spending has increased from \$15 per household in 1993 to \$52 per household in 2003." The Progress & Freedom Found., *Digital Age Communications Act: Preliminary Proposal of the Universal Service Working Group*, at 9-10 (Rel. 1.0, Oct. 2005) (footnote omitted). That expense has only increased further in the past three years, emphasizing again the need for prompt action to limit the size of the universal service fund.

For too long, universal service subsidies have also been used to subsidize carriers that were already serving an area prior to the receipt of a single high-cost fund dollar, or were only seeking duplicative high-cost funding because another carrier was receiving it.<sup>3</sup> Indeed, five

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<sup>2</sup> McLean & Brown, *Universal Service: Rural Infrastructure at Risk*, 39 (Rel. 2.0, Apr. 2006) (noting that 58 percent of study areas with a competitive eligible telecommunications carriers ("CETC") have two or more CETCs, and that 29 percent of such study areas have three or more CETCs).

<sup>3</sup> CETCs often provide quality competitive services without any universal service support, and typically serve a large number of consumers in an area prior to ever receiving universal service support. For example, Alltel served 162,949 lines in Alabama the quarter before it received high-cost support. Compare USAC, *Federal Universal Service Support Mechanisms*

years ago, Chairman (then Commissioner) Martin questioned the Commission's approach of subsidizing "multiple competitors to serve areas in which costs are prohibitively expensive for even one carrier."<sup>4</sup>

In effect, the current high-cost program turns on its head the appropriate relationship between competition and universal service under the Act. The market pressures of competition and innovation facilitate universal service (not the other way around), and reduce significantly the need for explicit subsidy mechanisms. As former Commission Economist Dr. David Sappington explains, "the competitive process, not regulatory pre-selection of a single universal service provider, is the best means to ensure the delivery of supported telecommunications services at minimum cost to consumers." *Comments of General Communication, Inc.*, Ex. 3, at 1

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*Fund Size Projections for the First Quarter 2005*, App. HC20, with USAC, *Federal Universal Service Support Mechanisms Fund Size Projections for the Second Quarter 2005*, App. HC21. Similarly Sprint served 55,786 lines in Alabama prior to receiving high-cost support. Compare USAC, *Federal Universal Service Support Mechanisms Fund Size Projections for the Second Quarter 2005*, App. HC21 with USAC, *Federal Universal Service Support Mechanisms Fund Size Projections for the Third Quarter 2005*, App. HC21. Indeed, in comments responding to Sprint's Alabama ETC petition, CenturyTel wrote "it remains unclear what benefits would flow from grant of Sprint's CETC Petition. Sprint entered the applicable Alabama market as a wireless carrier long ago and continues to provide competitive services without the aid of universal service support. It remains unclear to what extent Sprint *requires* any universal service funding to maintain rates that are affordable and reasonable comparable, as required by the Act." *Comments of CenturyTel of Alabama, LLC, CenturyTel of Eagle, Inc., and CenturyTel, Inc.*, CC Docket No. 96-45, at 5 (filed May 28, 2004).

<sup>4</sup> *MAG Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Second Report and Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 19613, 19770 (2001) (Separate Statement of Commissioner Kevin Martin). Commissioner Copps also has noted the "need to face the consequences of multiple designations in high-cost areas on the overall size of the fund." *Federal-State Joint Board on Universal Service*, Report and Order, 20 FCC Rcd 6371, 6437 (2005) (Separate Statement of Commissioner Michael Copps); see also *Federal-State Joint Board on Universal Service*, 19 FCC Rcd 4257, 4315 (2004) (Statement of Billy Jack Gregg, Public Service Commission of West Virginia) (noting that "there are certain areas of this country where it is so expensive to provide service that it makes no sense to have more than one carrier subsidized by the federal universal service fund.").

("GCI Comments"). Moreover, "in addition to preventing unnecessary subsidies, competition ensures just and reasonable rates – rates that necessarily reflect the actual cost of providing service." *Id.* at 13.

**2. The Commission Should Discontinue Funding in Areas Where It Is Not Necessary to Fulfill the Mandate of Section 254.**

Rather than needlessly providing substantial, often duplicative, per-line funding to incumbent or competitive carriers, the Commission should re-evaluate the landscape to identify the limited areas in which customers would not be served without explicit subsidies.

The Commission should first determine if rates in an area would be reasonably comparable and affordable without any explicit high-cost funding.<sup>5</sup> As noted above, the record shows that rural rates are often below urban rates today. Thus, in many areas, consumers have access to quality voice services at affordable and reasonably comparable rates from incumbent and competitive providers, with or without federal subsidies. The presence of a carrier serving an area, without high-cost subsidies, at rates below the current rate benchmark should be presumptive evidence that no funding is necessary. In such cases, high-cost subsidies to incumbent and competitive carriers alike should be phased out. Similarly, even in the absence of non-subsidized competition, if the Commission determines that an area would maintain affordable and reasonably comparable rates without high-cost funding, the goals of universal

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<sup>5</sup> The Wyoming Consumer Advocate similarly proposed that funding to competitive ETCs be eliminated "[u]ntil and unless competitors can show that either the competitiveness of the market itself will be diminished without levels of high-cost support to the high-cost incumbent providers or that customers will be harmed." *Comments of The Wyoming Office of Consumer Advocate*, at 10 ("*Wyoming Consumer Advocate Comments*"). There is no basis to limit that analysis to competitive carriers. All carriers should be required to justify the continued need for high-cost funding. Other proposals to limit funding to competitive ETCs, e.g., *Comments of AT&T Inc.*, at 32-33 ("*AT&T Comments*"), or establish a separate wireless fund, *Comments of the Nebraska Public Service Commission*, at 16 ("*Nebraska PSC Comments*"), miss an opportunity to control the fund size in a more comprehensive and competitively neutral manner.

service can be met without federal subsidies. This would be the case, for example, if local rates would be affordable and reasonably comparable after adding back the existing amount of per-line subsidy to current rates.

If the Commission determines that high-cost funding is still necessary to ensure affordable and reasonably comparable rates in an area, the Commission should provide a subsidy to only one carrier in that area. The Act does not require the Commission to fund multiple competitors in a service area. Rather, Section 214 provides only that ETCs "shall be eligible to receive universal service support." 47 U.S.C. § 214(e)(1). Similarly, the Act does not require the funding of duplicate networks to ensure competitive neutrality; rather, the Commission need only "allow[] fair competition among providers."<sup>6</sup> To impose appropriate limits on funding while assuring competitive neutrality, the Commission should consider a market-based allocation mechanism, like a reverse auction or competitive bidding-based structure.<sup>7</sup> Under a market-based approach, all ETCs in a high-cost area would bid/compete to provide subsidized service to that area, and the entity demonstrating that it can provide the requisite service quality with the least subsidization would be awarded the funding. The market-based criteria should not unfairly advantage the incumbent carrier; nor should they promote one particular technology. Finally, all

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<sup>6</sup> *GCI Comments* at 14.

<sup>7</sup> *First Report and Order*, ¶¶ 319-25 (finding that "competitive bidding is consistent with section 254, and comports with the intent of the 1996 Act to rely on market forces and to minimize regulation."); *see also Rural Caucus Forum on Reforming the Universal Service Fund: Hearing Before the Congressional Rural Caucus*, 109th Cong. 9 (2006) (Testimony of Paul W. Garnett, Assistant Vice President, Regulatory Affairs, CTIA-The Wireless Association) (indicating that CTIA is "open to other market-driven proposals (such as reverse auctions) that would encourage and reward efficiency"). Dr. Sappington further notes that "[c]ompetition can relieve regulators of the need to continually obtain extensive . . . information in order to continually select and motivate the most efficient universal service provider." *GCI Comments* Ex. 3 at 18.

ETCs should be required to demonstrate their ability to serve an entire area to ensure all customers have access to subsidized service.

**B. A Fair and Equitable Universal Service Program Absolutely Requires a Competitively Neutral Contribution Mechanism.**

Excessive funding under the high-cost program places added stress on a broken contribution mechanism, which already fails to reflect current market realities. The Commission has studied the need to fundamentally reform the contribution mechanism for almost four years. *See Federal-State Joint Board on Universal Service, Report and Order and Second Further Notice of Proposed Rulemaking, 17 FCC Rcd 24952 (2002).* During this review, the federal universal service tax has continued to rise, from 7.2 percent in December 2002 to almost 11 percent this quarter.<sup>8</sup> Sprint Nextel aptly characterizes the current situation, noting that "the stability and viability of the current universal service funding mechanism are becoming increasingly problematic for technological and economic reasons." *Sprint Nextel Comments* at 2. Likewise, the Mid-Atlantic Conference of Regulatory Commissioners cautioned that "the current allocation and distribution methodology is stressed." *Comments of the Middle Atlantic Regulatory Commission and State Commissioners of the MARUC States*, at 4 ("*MARUC Comments*"); *AT&T Comments* at 4.

Reining in growth alone as described above, however, is not sufficient to maintain the viability of the fund or ensure its continued compliance with section 254. The Commission must also address the competitive imbalance in its current revenue-based mechanism. Today, some voice providers are saddled with significant assessments while others avoid paying their fair

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<sup>8</sup> Compare Proposed Fourth Quarter 2002 Universal Service Contribution Factor, Public Notice, 17 FCC Rcd 16800 (2002), with Proposed Second Quarter 2006 Universal Service Contribution Factor, Public Notice, DA 06-571 (Mar. 13, 2006).

share altogether, simply because they use non-traditional voice technologies such as VoIP. As such, corrective action to broaden the base of contributors is fundamental to assuring a sustainable universal service system reflective of current market conditions. *Comments of the Iowa Utilities Board*, at 2 ("*IUB Comments*") (the "contribution base should be expanded"). Broadening the base is also necessary to ensure that the contribution mechanism is competitively neutral: The Commission adopted the competitive neutrality principle to ensure that "no entity receives an unfair competitive advantage that may skew the marketplace," yet the current contribution mechanism does just that for non-traditional voice providers. *First Report and Order* ¶ 48.

As an interim measure, the Commission could correct some of this imbalance by assessing contributions based on revenues using a safe harbor or proxy approach that calculates contributions based on percentages of retail revenues.<sup>9</sup> For example, one way to assess VoIP providers on an equitable basis with other voice providers would be to apply the existing safe harbor for wireless carriers (28.5 percent of retail revenues). Using this figure on an interim basis as a proxy to determine the percentage of retail revenues that would be assessed is equitable and nondiscriminatory by definition, given that these services would be treated identically.<sup>10</sup> Moreover, since the Commission has authority to make a universal service assessment on VoIP regardless of whether it is classified as a telecommunications service or an information service,<sup>11</sup> making such an assessment does not require resolution of the regulatory classification question.

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<sup>9</sup> See Letter from Kathleen Grillo, Verizon, to Marlene H. Dortch, Commission, CC Docket No. 96-45 (filed May 23, 2006) (stating that the Commission may require interconnected VoIP providers to contribute to the fund pursuant to a safe harbor or proxy approach).

<sup>10</sup> *Id.*

<sup>11</sup> *See Id.*

On a permanent basis, however, the most sensible means to broaden the contribution base is to adopt a number-based contribution mechanism.<sup>12</sup> Such a mechanism – based on flat assessments on in-use, working telephone numbers – would broaden the base of contributors by assessing all providers of voice services that connect to the PSTN, regardless of the technology used to provide those services.<sup>13</sup> A number-based mechanism also provides a more suitable foundation for the contribution mechanism for the future, given the continued decline in traditional interstate revenue sources and the continued bundling of telecommunications and information services. The Commission should move promptly to ensure that all providers of voice services contribute on the same basis (and, thereby, eliminate the inequities that are inherent in the current system) in order to fulfill the statutory requirement that contributions be assessed on an "equitable" and "nondiscriminatory" basis. *See* 47 U.S.C. § 254(b)(4).

**II. THE DEFINITIONS OF "REASONABLY COMPARABLE" AND "SUFFICIENT" SHOULD REFLECT A BALANCED APPROACH TO THE SECTION 254(B) PRINCIPLES CONSISTENT WITH THE TENTH CIRCUIT'S MANDATE AND COMMISSION PRECEDENT.**

**A. The Relevant Definitions Must Advance the Core Purposes of Section 254(b).**

Commenters generally agree that the Commission should not myopically focus on a particular 254(b) principle to the detriment of other individual principles or, more importantly,

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<sup>12</sup> *IUB Comments* at 2 (supporting a numbers based approach to contribution methodology); *see* Letter from Kathleen Grillo, Verizon, to Marlene H. Dortch, Commission, CC Docket No. 96-45 (filed March 3, 2006) ("*Verizon USF Letter*") (detailing Verizon's comprehensive number-based contribution proposal).

<sup>13</sup> *See, e.g., Verizon USF Letter*. Special considerations will need to be made with respect to low-income, pre-paid, and wireless family share subscribers under a number-based contribution mechanism to ensure equitable contributions. In addition, services not associated with numbers, *e.g.*, special access services, should continue to be assessed based on revenues. Broadband services should not be required to contribute under the number-based mechanism, except to the extent they use numbers. *Id.*

the principles viewed together.<sup>14</sup> Instead, the Commission should maintain a holistic view of the statutory principles, and the appropriate definition of "sufficiency" and "reasonable comparability" flow logically from this holistic approach.<sup>15</sup>

*Sufficiency*

As several commenters observed, "sufficiency" should be defined to encompass the advancement of all section 254(b) principles.<sup>16</sup> Moreover, the definition of sufficiency must recognize that subsidies should be no larger than necessary to accomplish section 254's objectives.<sup>17</sup> Indeed, the Tenth Circuit and the Fifth Circuit have recognized repeatedly that

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<sup>14</sup> *AT&T Comments* at 13 ("[A] fresh evaluation of [the Section 254(b)] principles, and one that takes *all* the statute's goals into account, should drive the Commission toward a revised universal service approach . . .") (emphasis added); *Comments of CenturyTel*, at 13 ("*CenturyTel Comments*") ("The Commission can address [the court's remand] by better explaining how the forward-looking cost-based mechanism promotes *all* of the interests underlying section 254(b) . . ."); *Qwest Commc'ns Int'l, Inc. v. FCC*, 398 F.3d 1222, 1234 (10th Cir. 2005) ("*Qwest II*") (finding that the Commission must "consider fully the Act's principles as a whole"). For example, CTIA explains that "each of the goals of Section 254(b) cannot be considered in isolation." *See CTIA Comments* at 3.

<sup>15</sup> The definition of sufficiency and reasonable comparability should apply equally to rural and non-rural carriers. Efforts of rural providers to insulate the rural mechanism from the definitions adopted in this proceeding are without merit. *See Comments of OPASTCO*, at 1-2 (advocating that definitions adopted in this proceeding should not apply to the rural mechanism); *Comments of Western Telecommunications Alliance*, at i, 1-4; *2004 Joint Board Notice* ¶ 9 (explaining that there is "no statutory requirement that the Commission use the Act's definition of rural telephone company for high-cost universal service purposes").

<sup>16</sup> *Vermont and Maine State Commissions Comments* at i, 3; *CenturyTel Comments* at 13; *Comments of the Rural Independent Competitive Alliance*, at 4-6; *Qwest Comments* at iii (explaining that "key principles that should be incorporated into the definition of 'sufficient' in addressing high-cost support are affordability, reasonable comparability of urban and rural services and rates, competitive neutrality and efficiency"); *Sprint Nextel Comments* at 3 (suggesting that "'sufficient' support can be provided to non-rural high-cost carriers consistent with [the seven universal service] principles, while balancing the reality of limited financial resources").

<sup>17</sup> *See, e.g., Dobson Cellular Comments* at 4-5 ("If service is affordable to certain persons or areas of the country with lower levels of support, or entirely without support, then providing

excessive subsidization may be inconsistent with the statute's sufficiency mandate.<sup>18</sup>

Accordingly, "sufficient" should be defined as "an affordable and sustainable amount of support that is adequate, but no greater than necessary, to achieve the goals of the high-cost program."<sup>19</sup>

Thus, proposals to define "sufficient" based on consideration of an individual principle are contrary to the global view of the section 254 principles.<sup>20</sup> Further, as detailed in Section IV, *infra*, efforts to expand the high-cost program generally, and the definition of "sufficiency" specifically, to promote greater broadband deployment ignore that broadband investment has been a deregulatory success story. *See Nebraska PSC Comments* at 13-14; *Vermont and Maine State Commissions Comments* at i. There is no basis to affirmatively subsidize broadband under an already stressed high-cost program, or to define sufficiency under the Act beyond access to basic telecommunications services.

#### *Reasonable Comparability*

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additional support would violate that aspect of the affordability principle that counsels against excessive subsidization."); *BellSouth Comments* at 22 ("[E]nough federal support to preserve and advance universal service.").

<sup>18</sup> *Qwest Corp. v. FCC*, 258 F.3d 1191, 1200 (10th Cir. 2001) ("*Qwest I*") ("[E]xcessive subsidization of universal services by long distance may violate the principle found in § 254(b)(1)."); *Qwest II*, 398 F.3d at 1234 (citing *Qwest I*); *Alenco Commc'ns, Inc. v. FCC*, 201 F.3d 608, 620 (5th Cir. 2000) ("[E]xcessive funding may itself violate the sufficiency requirements of the Act.").

<sup>19</sup> *GCI Comments* at 9-10 (defining sufficiency as the minimum amount of support necessary to achieve universal service goals); *Federal-State Joint Board on Universal Service, Order on Remand, Further Notice of Proposed Rulemaking, and Memorandum Opinion and Order*, 18 FCC Rcd 22559, ¶ 37 (2003) ("*Order on Remand*") (explaining that "amount of support should be only as large as necessary to achieve the relevant statutory goal").

<sup>20</sup> *CTIA Comments* at 4 (defining sufficient as "able to ensure that customers in rural, high-cost areas receive services at prices comparable to those available in urban areas"); *Comments of the Nebraska Rural Independent Companies*, at i (explaining that the "definition of 'sufficient' should remain focused on reasonably comparable rates").

"Reasonable comparability" for rural rates should be measured in the aggregate, so that rural rates are "within reasonable range" of "nationwide urban rates."<sup>21</sup> Section 254(b)(3)'s requirement that rates and services available to rural and urban areas be "reasonably comparable" does not require the Commission to demand or compel nationwide uniformity.<sup>22</sup>

As the Wisconsin Public Service Commission correctly notes, a certain disparity between the rates charged to rural and urban customers must be expected. *See* Comments of the Public Service Commission of Wisconsin, at 3-4 ("*Wisconsin PSC Comments*"). Specifically, the Wisconsin PSC noted that "[a] universal support system should temper the magnitude of those rate differentials, but does not need to eliminate them completely." *Id.* CTIA concurs that, "[w]hile Congress intended for rural rates to be reasonably comparable to urban rates, there is no statutory directive or policy rationale for urban consumers to subsidize rural rates below average urban rates."<sup>23</sup>

Efforts to broaden the scope of reasonable comparability to serve purposes beyond ensuring universal access to basic telecommunications services at comparable rates in rural areas

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<sup>21</sup> Comments of the National Association of State Utility Consumer Advocates, at 43-44 ("*NASUCA Comments*") (advocating that the Commission "adopt some range above the highest urban rate" to establish reasonable comparability); *Sprint Nextel Comments* at 6-7 (explaining that the "Commission should provide non-rural high cost support only to the extent that a carrier's rate for basic local service exceeds, by a specified amount, a prescribed benchmark")

<sup>22</sup> Tellingly, Congress's direction that local rates be *comparable* is in direct contrast to its requirements of long distance rate uniformity across urban, rural, and high-cost areas. *See* 47 U.S.C. § 254(g) (directing the Commission to adopt rules that require that the rates charged by interexchange providers "to subscribers in rural and high cost areas shall be no higher than the rates charged by each such provider to its subscribers in urban areas").

<sup>23</sup> *CTIA Comments* at 4; *see also NASUCA Comments* at 43 ("'Comparable' does not mean 'equal.' If Congress intended rural rates to be equal to urban rates, the 1996 Act would have said so. Congress even added the qualifier, 'reasonably,' so that rural rates were supposed to be only 'reasonably comparable' to urban rates.").

should be rejected. By way of example, Dobson Cellular contends that in considering reasonable comparability for rural areas, the Commission should include the availability of competitive wireless services. *Dobson Cellular Comments* at ii, 7. Competitive wireless service is a reality in the vast majority of the United States due to market conditions, not governmental mandate or subsidy programs.<sup>24</sup> There is no need to expand explicit universal service subsidies to provide what the competitive marketplace already produces. As Sprint Nextel notes, "the Commission should continue to define reasonably comparable rates in terms of local rates only," and should not include long distance, Internet, or other vertical features in the analysis. *Sprint Nextel Comments* at 7.

Notably, the majority of commenters bypass explicitly defining reasonable comparability in favor of explaining how their proposals would ensure the principle's satisfaction. Verizon addresses those proposals in Section III.B, *infra*.

**B. Existing Rates in High-Cost Areas Served by Non-Rural Carriers Are "Sufficient" and "Reasonably Comparable" Under any Reasonable Definition of Those Terms, and the Record Evidence Shows that the Current Fund Provides Excessive Subsidies in Many Areas.**

Rate data provided by other commenters corroborate the evidence submitted by Verizon that shows the current level of high cost funding is more than sufficient to assure reasonable comparability of rates in rural and urban areas. *See, e.g., NASUCA Comments; BellSouth Comments; Sprint Nextel Comments*. In fact, these data reinforce the conclusion that rural rates are not only reasonably comparable to urban rates; they are actually lower, on average, than

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<sup>24</sup> *See Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, Tenth Report, 20 FCC Rcd 15908, ¶ 41 (2005) (stating that 87 percent of the U.S. population lives in counties with five or more mobile telephone operators competing to offer service, and 41 percent of the population lives in counties with six or more mobile telephone operators competing to offer service).

urban rates. Moreover, not a single commenter suggests that rural rates in the aggregate are not affordable or reasonably comparable to urban rates under the current mechanism.

For example, Sprint Nextel submitted data showing that, in many instances, "non-urban rates for basic local residential service are significantly lower than the national average urban rate." *Sprint Nextel Comments* at 6, Attach. 1. Sprint Nextel further demonstrated that "rates in rural areas for various non-rural carriers" are well below the national average urban benchmark. *Id.* Overall, Sprint Nextel's data reveal that non-rural providers charge nearly \$5.00 or 33 percent less on average than the national average urban rate. *Id.* (analyzing rates of a group of non-rural carriers serving rural areas).

That analysis is consistent with other commenters' evidence. BellSouth concluded that, on average, "*the nation's rural residents pay \$0.89 less than the nation's urban residents.*" *BellSouth Comments* at 2-4, App. A. This finding was based on a review of rural and urban rate data in 146 urban and rural areas served by non-rural carriers. *Id.* Similarly, rate data from 11,000 wire centers served by non-rural carriers collected by NASUCA confirm "that there is not that much difference between current rural rates and current urban rates." *NASUCA Comments* at 2, 8, 41.<sup>25</sup>

While these data show that rural rates are reasonably comparable to urban rates, the available data likely understate the extent to which consumers in rural and urban areas enjoy comparable rates and services. Given the significant growth and success of competing voice technologies, and the fact that any-distance rates and service plans from wireless and VoIP

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<sup>25</sup> GCI also found that rates in many rural areas are *lower* than rates in urban areas. *GCI Comments* at 30-31 (explaining that "[n]othing in the statute suggests – or permits – urban customers to systematically pay higher rates than rural customers"); *see also Qwest Comments* at 27 (finding that "urban consumers pay on average over \$7 more per month for telephone services" compared to rural consumers).

providers are nearly uniform nationwide, the Commission's analysis under section 254 should no longer focus exclusively on wireline services for purposes of determining whether rates are reasonably comparable. *See* Comments of Verizon, at 8-16 ("*Verizon Comments*") (providing a detailed review of the growth and diversity of intermodal competition). However, commenters generally provided data on *wireline* rates whereas a complete analysis necessarily must include rates available from intermodal competitors, including wireless and VoIP services.

Even without including wireless and VoIP rates, the rate data provided in this docket are sufficient at this stage to address "the specific concerns raised by the Tenth Circuit." *NASUCA Comments* at 45. In fact, this evidentiary record establishes that the current high-cost programs exceed their statutory purpose by often providing rural consumers with rates that are lower than, not merely comparable to, urban rates. *See Qwest II*, 398 F.3d at 1237 ("return to [the court] with empirical findings"). Consistent with the Tenth Circuit's concerns, the Commission should, therefore, refocus its high-cost program on those specific areas in which funding is necessary to satisfy section 254's mandate. To this end, the Commission should institute a means of collecting geographically granular, consistently defined rate data nationwide in order to identify as accurately as possible those areas where federal high-cost subsidies remain necessary to assure reasonably comparable rates.

### **III. PROPOSALS TO EXPAND FURTHER THE HIGH-COST PROGRAM IGNORE PRACTICAL CONCERNS AND STATUTORY LIMITATIONS.**

Despite nearly universal recognition that the high-cost fund is already too large, some commenters nevertheless suggest that the Commission should increase the size of the fund directly, or should manipulate program rules and benchmarks to maximize funding opportunities for some subsets of providers. None of these measures is required by *Qwest II*, and each of these

proposals should be rejected on its merits. The Commission must take steps to wean carriers off unnecessary high-cost subsidies.

**A. The Empirical Record Demonstrates that Plans to Further Grow the Fund and the USF Tax Burden Borne by Customers are Contrary to Section 254(b).**

Several commenters urge the Commission to expand the non-rural fund and increase the total price paid by customers for service. For example, AT&T's comprehensive plan would balloon the non-rural fund, and the cost to consumers, by nearly *\$1.5 billion*. *AT&T Comments* at 33. Similarly, Qwest's proposal would "result in a total non-rural support fund of approximately \$1.9 billion, a significantly higher amount than the current non-rural fund size of \$290.9 million." *Qwest Comments* at 32.<sup>26</sup> These commenters fail to produce any evidence or argument demonstrating that such a huge increase in the fund and in the price to customers is necessary to ensure affordable or reasonably comparable rates.

These proposals to expand the non-rural mechanism are based, in part, on a simple comparison of the non-rural and rural mechanisms: Rural carriers receive almost six times the amount of subsidies, even though non-rural carriers serve twice as many rural consumers nationwide. *AT&T Comments* at 6-7.<sup>27</sup> These commenters ignore the rate data, noted in Section I above, which demonstrate that the non-rural fund is already larger than necessary to serve its statutory role. Specifically, the evidentiary record in this proceeding establishes that rural rates are not only reasonably comparable to urban rates; they are actually lower, on average, than

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<sup>26</sup> See also *BellSouth Comments* at 5 (suggesting that its RBB proposal would "increase somewhat" the universal service fund).

<sup>27</sup> See also *Comments of the Wyoming Public Service Commission*, at 4-5 ("*Wyoming PSC Comments*") (claiming that non-rural carriers receive insufficient support in comparison to similarly situated exchanges served by rural carriers).

urban rates. There is no basis then to expand federal subsidies to areas served by non-rural carriers, where affordable and reasonably comparable rates exist without federal funding. In this regard, the actual rate data suggest that the non-rural and rural mechanisms should provide *less* subsidizations to far *fewer* areas.

Qwest attempts to minimize the adverse effect of its proposal by rolling back and capping subsidies at 2004 levels. *Qwest Comments* at 32. Such a cap would redistribute subsidies from rural ETCs to non-rural ETCs, without any evidence that such subsidy is necessary for non-rural carriers to ensure the overall affordability and reasonable comparability of rates in Qwest's territory. *Id.* at 32. Similarly, AT&T proposes to eliminate subsidies to multiple CETCs serving the same area, which "exaggerates the size of the fund needed to provide universal service and is not an efficient use of federal funding." *AT&T Comments* at 33.

AT&T and Qwest are both correct with respect to their proposals to reduce inefficient and unwarranted subsidy levels; the dispute lies in whether such funding should be redistributed to equally undeserving larger carriers or eliminated altogether to the benefit of ratepayers nationwide. Of course, it should not be redistributed. It makes no sense to replicate the problems and defects of the rural mechanism in the non-rural fund. For both funds, the Commission should substitute market-based mechanisms for the current government-set formulae that require no affirmative showing that subsidies are truly necessary to ensure the affordability and comparability of services.

**B. The Commission Should Reject Efforts to Modify the Rate Benchmark In a Manner that Fails to Target Subsidies Appropriately.**

Several commenters offer a litany of proposals to modify and/or reduce the non-rural mechanism's rate benchmark, transition to a new type of funding mechanism, or greatly increase universal service funding. Each of these proposals would expand (or redistribute) funding in

some manner, without a clear demonstration that such subsidy is necessary to ensure that rates remain affordable and reasonably comparable, and each should be rejected.

**1. *Qwest II* Did Not Mandate Modifications to The Current Rate Benchmark.**

Because the Tenth Circuit did not require a narrower benchmark or a larger fund, the Commission may retain the presumption that rates that are within two standard deviations of the national average urban rate are "reasonably comparable." *Order on Remand* ¶ 53. The granular data provided in this docket confirm that the current non-rural mechanism provides sufficient (and, in some cases, excessive) subsidies when measured against appropriate definitions of sufficient and reasonable comparability. The court asked only that the Commission "return to the [court] with empirical findings supporting th[e] conclusion" that the Commission's benchmarks "resulted in reasonably comparable rates." *Qwest II*, 398 F.3d at 1237. The Commission now has the data to meet the *Notice's* charge to "provide stronger evidence that its universal service support mechanisms achieve the Act's rate-related goals." *Federal-State Joint Board on Universal Service*, Notice of Proposed Rulemaking, 20 FCC Rcd 19371, ¶ 23 (2005) ("*Notice*").

Nonetheless, a number of parties erroneously assert that the benchmarks under the non-rural mechanism must be reduced to be responsive to *Qwest II*, without any analysis of whether the additional resulting subsidies are necessary under section 254.<sup>28</sup> In reality, NASUCA's data

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<sup>28</sup> See *Vermont and Maine State Commissions Comments* at 31-32 (suggesting that the Commission lower the numerical standard for reasonable comparability to 125 percent of nationwide urban rates noting that the court demands "a far more aggressive reasonable comparability standard"); see also *Qwest Comments* at 22-23 (proposing that the Commission redefine "reasonably comparable" such that rural rates are reasonably comparable only if they are not more than 125 percent of the national average urban rate); *BellSouth Comments* at 13-16 (proposing a reduced funding threshold from two to one standard deviation).

show that the discrepancy between urban and rural rates is already no greater than "the discrepancy among urban rates." *NASUCA Comments* at 46; *see also* Decl. of Patrick Garzillo, ¶ 12 (attached to *Verizon Comments*) (finding that rural rates generally appear to be dispersed in the roughly same proportion as urban rates). As a result, a narrower benchmark inexplicably would require rural rates to be closer to the average urban rate than other urban rates, a result that is neither required nor even contemplated by the Act. *See Order on Remand*, at ¶ 43. The empirical record in this proceeding thus provides sufficient basis for the Commission to explain why the overall sufficiency of its non-rural high cost mechanism should be assessed by comparing the spread and distribution of rural and urban rates. *See Qwest II*, 398 F.3d at 1236. If particular rural rates are far above the nationwide benchmark, that means that subsidies should be targeted to those areas – not that the mechanism itself has failed.

Nor is greater high-cost funding necessary to respond to the court's directive to ensure that the universal service program both preserves and advances universal service. *Qwest II*, 398 F.3d at 1236 (suggesting that the Commission "ignor[ed] its concurrent obligation to advance universal service"). Efforts to advance universal service directly implicate affordability considerations, and the Massachusetts Department of Telecommunications and Energy concludes accurately that "the Commission previously determined that it was better to address affordability issues unique to low-income consumers through the federal lower-income programs specifically designed for this purpose rather than through the high-cost support programs." *Comments of the Massachusetts Department of Telecommunications and Energy*, at 10 ("*Massachusetts DTE Comments*"). Neither the court nor commenters offer any basis to revisit the Commission's decision to address advancing universal service through its low-income programs. *See Federal-State Joint Board on Universal Service*, Seventh Report and Order, 14 FCC Rcd 8078, ¶ 39

(1999). Accordingly, the high-cost program should not be extended to address statutory principles more efficiently and effectively addressed by other pre-existing universal service mechanisms.

## **2. Alternative Rate Proxies Raise Significant Adminstrability and Public Policy Concerns.**

Certain commenters submit proposals to adopt complicated alternative proxies that fail to reflect market-based determinations. In fact, each of these proposals shares the same fatal flaw: They do not discontinue subsidies to those areas that no longer require subsidies. Moreover, these proposals would require significant resources to develop and implement, and would interject significant uncertainty into the high-cost fund.

For example, the Wisconsin PSC supports a funding mechanism based on rates as opposed to the current cost-based mechanism. *See, e.g., Wisconsin PSC Comments* at 12 (supporting a variation of the Wisconsin HRAC program). Yet, these commenters fail to respond effectively to the Commission's prior reservations with a rate-based approach. *Order on Remand*, ¶ 23 (explaining that "[s]tates may base rates on a variety of factors, so that comparing only rates, which may or may not include implicit support, would not be a fair and equitable way to apportion federal support"). As Dobson Cellular explains, a "purely rate-based mechanism may face considerable challenges, including the prospect of state commissions or carriers themselves using the rate-setting process as an opportunity to maximize support inappropriately."<sup>29</sup> Therefore, not only is the Commission not required to adopt a rate-based

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<sup>29</sup> *Dobson Cellular Comments* at 10; *NASUCA Comments* at 54; *Vermont and Maine State Commissions Comments* at 26 ("A rates-based comparability standard . . . would force the FCC to provide universal service funding to address rate differences that arise, not merely from cost differences, but also from state policy decisions.").

mechanism, *see supra* p. 19, it should refuse to adopt such an approach for the reasons cited above.

Proposals based on affordability measures and household income are similarly off the mark.<sup>30</sup> These proposals would provide funding based on an affordability index, which would reflect household expenditures on telecommunications services compared to household incomes. As a threshold matter, as the Vermont and Maine State Commissions pointed out, basing high-cost support on median household income "is unfair to individual customers" because it "inaccurately assumes that income in a community is homogeneous and equally available to all." *Vermont and Maine State Commissions Comments* at 7-8 ("reducing support to wealthy communities . . . discriminates against poor people living in wealthy communities"). Household-specific calculations would also be problematic, raising significant privacy and administrative workability concerns. In addition, the Commission lacks the necessary experience and data to create an appropriate benchmark based on telephone expenditures and household incomes. This lack of experience casts doubt on the ability of the Commission to develop an affordability-based funding mechanism narrowly targeted to only those areas that require subsidies. In the end, affordability remains best addressed by the Commission's low-income programs. *See supra* Section III.B.2.

Still other commenters offer additional proxies that have similar shortcomings. For instance, Qwest supports the distribution of high-cost subsidies based, in part, on population density. *Qwest Comments* at 35-36. Qwest's proposal fails to reflect non-population-based cost

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<sup>30</sup> *See, e.g., AT&T Comments* at 23-35 (advocating an affordability/income based mechanism); *see Sprint Nextel Comments* at 3 (supporting the concept of linking high-cost support to an affordability benchmark); *Massachusetts DTE Comments* at 9 (support should be means-tested).

drivers such as unique geography and difficult terrain. Underlying Qwest's proposal is its contention that the high-cost model for non-rural carriers is a poor proxy for costs, and, therefore, a density-based approach's apparent limitations are also acceptable. *Id.* at 35-37. Replacing an imperfect cost model with an even more inferior cost proxy (density) makes no sense. Proposals that seek to incorporate net subscriber costs as a proxy for rates would also needlessly complicate and distort the high-cost program.<sup>31</sup> Specifically, this approach would inappropriately include revenues not associated with subsidized services – *e.g.*, vertical features, special access revenues, or other non-subsidized services and features – when evaluating the need for high-cost subsidies. The high-cost program subsidizes basic telephone services, and those services alone should be the basis for universal service funding evaluations. *See, e.g.*, 47 C.F.R. § 54.101.

Given the complications and limitations of these proposals, the Commission (and consumers) would be better served by devoting resources to the development of a more straightforward funding mechanism that is shaped by competitive market conditions. Thus, pending the transition to a market-based approach, a cost-based funding mechanism remains the most workable solution and the most consistent with the court's directive.

There is also no need to modify the current cost-based mechanism pursuant to the court's remand. Specifically, the FCC need not revisit its cost model in this proceeding.<sup>32</sup> Nor does the

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<sup>31</sup> *See Vermont and Maine State Commissions Comments* at 19 (proposing that net subscriber costs be used as a proxy for rates in its support calculation); *NASUCA Comments* at 69-70 (stating that the Commission should include revenues from vertical services, switched access, and DSL services when determining levels of support).

<sup>32</sup> *Wyoming Consumer Advocate Comments* at 16; *NASUCA Comments* at 63; *Vermont and Maine Commission Comments* at 38. AT&T explains that "it goes without saying that the sorely needed overhaul of the overall universal service support mechanism should take precedence over replacement of the underlying cost model." *AT&T Comments* at n. 55. Qwest also stresses how

Commission need to modify the manner in which eligibility is determined from a statewide basis to an individual wire center basis. *See supra* Section I.A.

Currently, the non-rural mechanism determines funding eligibility through a comparison of statewide costs to a national benchmark. The Commission has repeatedly found that this "statewide averaging is the best approach to further the goals of section 254," reflective of the proper federal funding responsibility. *Federal-State Joint Board on Universal Service*, Ninth Report and Order, 14 FCC Rcd 20432, ¶ 48 (1999); *Order on Remand*, ¶ 24. And the Tenth Circuit has upheld that determination, explaining that "[i]t would be impossible for the FCC alone to ensure reasonably comparable rates in urban and rural areas unless it were willing to *commit massive federal support* toward ensuring that rates in rural areas are no higher than those currently in place in urban areas." *Qwest I*, 258 F. 3d at 1203 (emphasis added). There is no basis for revisiting statewide averaging here, and doing so is not necessary to address the court's instructions on remand. Moreover, as a practical matter, subsidies already are provided on a wire center basis under Commission rules for eligible states, so claims that determining eligibility based on wire center specific cost will result in more accurate targeting of subsidies are mistaken.<sup>33</sup>

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the difficulties associated with the model, explaining that it requires "countless hours developing, analyzing and refining computer models that were designed to estimate the cost of serving high-cost areas." *Qwest Comments* at 35. Similarly, wireless carriers' call to determine efficient costs should also be rejected, because it would require substantial modifications to the cost model to incorporate wireless and other technologies with no clear benefit. *See CTIA Comments* at 3; *Dobson Cellular Comments* at 3. The efficiency concerns expressed by wireless providers are better addressed by the market-based proposal described in Section I.B.

<sup>33</sup> *See* 47 C.F.R. § 54.315. Proposals to transition to a wire center funding approach are again premised, in part, on a comparison with the rural fund, which provides support on a study area basis. Wyoming PSC suggests that the non-rural fund "imposes a stiff and[] unnecessary penalty on rural exchanges which have the misfortune to be served by a [non-rural] carrier." *PSC Comments* at 9; Comments of the Washington Utilities and Transportation Commission, at

**IV. THE KEY TO CONTINUING BROADBAND DEPLOYMENT IS FURTHER DEREGULATION AND COMPETITION, NOT EXPANSION OF THE FUND.**

The Commission should re-affirm its 2003 decision and reject any efforts to further expand the high-cost fund to subsidize costs of broadband and advanced services. Subsidizing broadband under the high-cost program would result in another significant increase in fund size, needlessly interfere with the competitive market, and could ultimately increase the cost of broadband access to consumers.<sup>34</sup> Qwest correctly notes that "any consideration that supported services should be redefined to include broadband must be balanced against its likely impact on the overall size of the fund and the affordability of services that contribute to the fund." *Qwest Comments* at 14.

Broadband providers have invested significant resources to deploy high speed networks and services, and the Commission has recognized that "[v]igorous competition between different platform providers already exists in many areas and is spreading to additional areas."<sup>35</sup> In the

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3 ("Washington UTC Comments") (observing that the current approach "disadvantages rural customers in most states where one or more low cost-of-service areas exist in the state"). As demonstrated above, such comparisons should speed reform of the rural fund, not encourage further expansion of this program.

<sup>34</sup> See *Federal-State Joint Board on Universal Service*, Order and Order on Reconsideration, 18 FCC Rcd 15090, ¶¶ 8, 11 (2003) ("If advanced or high-speed services were added to the list of support services, it could drastically increase the financial burden placed on carriers, and, ultimately, consumers . . .").

<sup>35</sup> FCC, Industry Analysis and Technology Division, Wireline Competition Bureau, *High-Speed Services for Internet Access: Status as of June 30, 2005*, at 4 (Apr. 2006) ("*High-Speed Services April 2006 Report*") (noting that 98 percent of the nation's zip codes, representing 99 percent of the U.S. population, have at least one high-speed Internet access service provider). A recent GAO report also found that broadband services are available to over 90 percent of the nation's households. See GAO, *Broadband Deployment is Extensive throughout the United States, but It is Difficult to Assess the Extent of Deployment Gaps in Rural Areas* (May 2006) ("*GAO Report*"); Ian Martinez, *Commission May Overstate Broadband Penetration, GAO Says*, Comm. Daily, May 8, 2006 at 6. The GAO concluded that for "many, if not most Americans,

last year alone, the number of broadband connections has jumped by almost one-third, from 32.4 to 42.8 million. *High-Speed Services April 2006 Report*, Table 1. For its part, Verizon has invested aggressively in FiOS fiber-based services, spending billions of dollars to bring fiber directly to millions of customers across its region.<sup>36</sup>

Commenters seeking explicit high-cost broadband funding, therefore, offer solutions in search of a problem. *See Comments of the Oregon Public Utility Commission*, at 1, 4-7 ("*Oregon PUC Comments*"); *Vermont and Maine State Commissions Comments* at 12-15. Considerable broadband deployment has occurred without universal service subsidies, and there is no reason to believe that such subsidies are needed now. As Qwest explains, while there is no "dispute that deployment of broadband to rural areas is in the national interest, it is simply not evident that this effort needs to be funded by universal service high-cost support." *Qwest*

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the burgeoning broadband marketplace is characterized by competitive choice in broadband access and creative and ever-expanding applications and content." *GAO Report* at 38.

<sup>36</sup> *See Jonathan Make, Martin Backs Video Franchise Relief for Telcos*, *Comm. Daily*, Mar. 20, 2006 at 2 (detailing Verizon's "\$20 billion FiOS" investment); *News Release, Verizon Customers in Tampa Have a Choice for TV Service* (May 17, 2006) (detailing the availability of FiOS TV in California, Massachusetts, Maryland, New York, Texas and Virginia); *Commissioner Deborah Taylor Tate, Closing Remarks to the Accenture Global Convergence Forum*, at 4 (May 12, 2006) (explaining that "loosening regulation resulted in more than \$6 billion in investment by Verizon and \$5 billion in investment by AT&T"). Critics of non-rural carriers' broadband investment ignore these substantial efforts and record of innovation and investment. *NASUCA Comments* at 93; *Vermont and Maine State Commissions Comments* at 13-14. In addition, non-rural carriers, as well as competitive broadband providers, continue to develop and seek out new technologies and service features to expand the reach of broadband services through improved DSL technology, fixed wireless, and satellite offerings. *Comm. Daily Notebook*, *Comm. Daily*, at 18, May 9, 2006 (announcing that AT&T will offer WildBlue satellite broadband in select rural markets not served by terrestrial broadband); *Ellen McCarthy, Hughes Looking at Rural Internet*, *Wash. Post*, Mar. 27, 2006, at D1 (stating that Hughes Network Systems LLC "see[s] the company's future more tightly tied to providing Internet access").

*Comments* at 14. Similarly, the GAO has found "little support for . . . expanding the USF program to include broadband service." *GAO Report* at 36.

Further, competitive neutrality dictates that market conditions, not subsidies, steer broadband development: There is no public policy basis to subsidize only select broadband platforms under the universal service program. Such a policy would place other competing platforms at a competitive disadvantage and could act as a disincentive to emerging technologies, contrary to the principle that universal service policy should "neither unfairly favor nor disfavor one technology over another." *First Report and Order*, ¶ 47. GCI similarly explains that "[p]ermitting some providers to use universal service dollars to construct a broadband capable network to compete with unsubsidized providers is profoundly anticompetitive, and destroys market incentives for deployment of advanced services in rural and remote areas." *GCI Comments* at 2.

**V. THE PROPOSED INSULAR MECHANISM SHOULD NOT BE EXTENDED BEYOND ITS LIMITED PURPOSE.**

The proposed non-rural insular mechanism is designed to remedy a specific funding gap in the Commission's high-cost loop program for non-rural, insular high-cost areas. *See, e.g., Notice*, ¶¶ 30-38; *Comments of Puerto Rico Telephone Company, Inc.* The Commission should reject efforts to expand the scope or purpose of the proposed mechanism: Proposals to expand the eligibility,<sup>37</sup> or the objective,<sup>38</sup> of the new mechanism bear no relation to the key structural

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<sup>37</sup> Commenters seek to expand the proposed definition of "insular" to include remote Alaska and Hawaii. *Comments of Hawaiian Telcom, Inc.*, at 2, 5-6; *Comments of Sandwich Isles Communications, Inc., et al.*, at 6 ("*Sandwich Isles Comments*"); *Comments of the Regulatory Commission of Alaska*, at 4 ("*Regulatory Commission of Alaska Comments*"). Yet Sandwich Isles, *et al.*, currently receives "sufficient" loop support under the rural mechanism based on its embedded costs. *Sandwich Isles Comments* at 2. Thus, transitioning to the non-rural insular

defects in the universal service programs, nor are they necessary to satisfy Section 254's principles.

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fund would have no consequence. Hawaiian Telcom, a non-rural carrier, does not receive loop support currently, and it would also not be eligible for high-cost loop support under an embedded cost mechanism because of its lower cost structure. *See* FCC, Federal-State Joint Board, *Universal Service Monitoring Report*, CC Docket No. 98-202, at 3-236 (Table 3.3) (May 2005) (showing that Hawaiian Telcom's average loop cost (\$258.54) is below the funding threshold of the proposed non-rural insular mechanism (\$276)).

<sup>38</sup> Sandwich Isles proposes to establish a comprehensive insular mechanism – inclusive of the current rural loop, access, and other high-cost programs – in place of a targeted non-rural insular mechanism. *Sandwich Isles Comments* at 13. Such a global insular fund is beyond the identified harm at issue, and there is no proof that such a fund is necessary or appropriate under section 254. Similarly, calls for an altogether new mechanism to carriers that provide interexchange service to rural communities is also beyond the scope of this proceeding. *AT&T Comments* at 38-41; *Regulatory Commission of Alaska Comments* at 4.

**CONCLUSION**

For the foregoing reasons, the Commission should review and revise the current high-cost mechanism to reflect market conditions and to remove subsidies that are no longer warranted.

Respectfully submitted,

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