BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the matter of the Federal-State Joint Board on Universal Service Seeking Comments on the the Merits of Using Reverse Auctions to Determine High-Cost Universal Service Support	))))	WC Docket No. 05-337 CC Docket No. 96-45

COMMENTS OF THE
OKLAHOMA CORPORATION COMMISSION

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I. INTRODUCTION

The FCC is seeking comments on the appropriateness of the use of reverse auctions to reduce the overall level of high cost universal service funding paid to Eligible Telecom Carriers ("ETCs"). The Federal Universal Service Fund ("USF") is based on several principles, including, but not limited to, quality services at just and affordable rates, access to advanced services, and universal access in rural and high cost areas. While these basic principles are laudable, the USF has grown significantly in recent years and this has placed a greater burden on end users who fund the USF. The concept of reverse auctions would allow ETCs to participate in a bidding process in order to compete for universal service funding provided in specific geographic areas, with the goal of controlling the growth of, or reducing the size of, the USF. These comments should not be considered binding upon the Oklahoma Corporation Commission ("OCC") in any proceeding before the OCC. The OCC respectfully submits these comments to propose that reverse auctions are not the best solution to temper the size and growth of the USF.

II. APPROPRIATENESS OF REVERSE AUCTIONS

Historically, reverse auctions have been used to "bid down" the price of a good or service, as opposed to traditional auctions, which "bid up" prices. In other words, Reverse Auctions ("RAs") are a sourcing tool used to procure goods and services wherein the bidding mechanism is "reversed." In theory, this process would create a competitive atmosphere where the bidders compete for the opportunity to be the "supported" provider. Because of the reversal of the traditional auction process, the bidders and sellers have vast amounts of asymmetric information. This information gap creates a rift, which distorts an otherwise equilibrium-based process wherein factors other than price are considered. These factors include, but are not

limited to, quality and history of service, as well as the appropriateness of such an auction for a given product.

A primary problem with reverse auctions is that "price" may be the only factor considered when determining the winning bid while only a loosely held set of agreements about the integrity of the service would potentially exist at both the federal and state levels. Yet other factors, such as customer service, service quality, and the capacity to offer advanced services are of equal or greater importance. In order to effectuate a workable, real world reverse auction, it would be necessary to clearly delineate the parameters for submitting and delivering on the bids. It is also possible that imprudent bidding may occur if bidders submit bids without thorough assessment of long-run strategies, costs and benefits.

Furthermore, the bid evaluations would need to include a review of technical ability and financial viability, and more importantly, winning bidders must possess a commitment to providing the required services. Within these variables, there are underlying issues that do not consider the importance of price variability (providing identical services from one location to the next), differing labor pools (wage demands), and other factors such as time and economic variables that "lowest-price" bids may fail to incorporate. As a result of the numerous potential unforeseeable or unidentifiable considerations, litigation and legal costs may increase significantly.

Quality, reliability and safety standards would be better achieved through a means whereby the buyer could openly convey all relevant information to the seller. Negotiated and sealed bidding are two methods of auctioning that allow non-price variables to play a more dominant role in selecting winning bids. A study by Valter Sonrana[1] from Stanford University suggests that under a RA paradigm, collusion is possible among bidders, and those who opt out

[1] *Auctions for Universal Service Subsidies*, Valter Sorana, November 1998, p. 2.

of the collusive cartel could be economically harmed. Another problem with RAs is that large incumbents could enter into predatory pricing behavior and force smaller carriers in the bidding territory to sell out. While RAs are a price-reducing paradigm that can provide a significant amount of incentive to drive prices down, non-price variables may ultimately lead to even more costly end results.

RAs would likely not be viable mechanisms to lower USF support in high cost markets where there is little or no competition. Safeguards would need to be designed and implemented to ensure that service quality and integrity are paramount in rural markets where competitive forces do not provide the same safeguards that are prevalent in urban areas. Due to the uniqueness of rural service areas, RAs would not serve as a parity mechanism applicable to all providers. Furthermore, the potential negative outcomes of a post bid-era may be too costly to justify enactment of RAs.

III. LEGAL ISSUES AND FRAMEWORK

Universal Service has been and will continue to be a primary goal of the FCC. With this objective comes the need to preserve and advance universal service while maintaining the important statutory goals of service and rate comparability. The Telecommunications Act of 1934 ("Act"), as amended in 47 U.S.C. §254, requires just, reasonable and affordable rates. The Act also requires the establishment of specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service so consumers in all parts of the country can have access to comparable services at reasonably comparable rates.

The predictability and sufficiency of support and the advancement of universal service could be challenged if the RA proposal is adopted. As to predictability, there is no assurance that the ETC serving an area could predict USF support levels over time when the support would

be subject to the outcome of a periodic bidding process. This could result in delayed or reduced investment to maintain facilities or deploy new technologies. As to sufficient support, winning bidders may not possess the technical expertise or experience to properly set the bid amount at a level that will ensure adequate support to maintain acceptable customer service and quality standards. Further, the bid losers would likely be forced to increase rates in an attempt to recover the lost universal service funds, so customers served by both the winner and the loser could be negatively impacted. Significant rate increases could also result in the demise of losing bidders or, in a worse scenario, winning bidders could employ predatory pricing tactics to drive out competitors and then increase rates once there is no competition.

Without specific, predictable and sufficient support, the goals of Universal Service could be in jeopardy. A carriers' inability, or lack of incentive, to maintain adequate facilities and deploy advanced technologies due to decreased USF support could eventually result in a system of "haves" and "have-nots," which is contrary to the goals of the Act.

IV. SUPPORTED AREA(s)

A primary predictor of successful reverse auction bidding would be the "level of competition" in the supported area(s). Areas that do not have robust competition, or a sufficient presence of viable competitors, would likely not produce successful auctions and should probably not be considered for the RA process. In order to make this determination, it would be necessary to develop "competitive criteria" to evaluate the level of competition in a service area as a test for RA eligibility. When developing the competitive criteria, it would be vital to eliminate companies that are affiliated with or related to Incumbent Local Exchange Carriers (ILECs) from the list of "competitors." After performing this analysis, there would likely be many areas throughout the country that would not meet this test and, therefore, RAs would not

be appropriate. In areas that do meet the competitive criteria, RAs could possibly work, provided that specific criteria such as customer service and quality standards are established up front. Nonetheless, if RAs can be successful in only some supported areas, the overall objective of reducing the size of the USF would be partially, or significantly, negated.

V. QUALITY OF SERVICE OBLIGATIONS AND ENFORCEMENT

As previously mentioned, quality of service should be an essential element of consideration when determining winning bids. However, the baseline for service quality can be subjective with diverse standards and parameters. The concept of providing quality service at the lowest bid price can be a challenging proposition for any business.

If the RA model is implemented, it is likely that the FCC or a neutral third party would be the governing authority or administrator. Along with administering the bidding process, the governing authority would need to enforce contract or service commitment violations. However, enforcement of strict performance penalties, such as the loss of the right to receive USF support in a service area, could be detrimental to end users if there are no other carriers serving the area. In other words, RAs could potentially destabilize telephone service delivery in many areas.

A. Customer Choice

What choice will customers have when service quality (which is, in their opinion, what really matters) is inadequate? Under ideal circumstances, customers who receive inadequate service can simply select another service provider. A possible outcome of the RA proposal is that some customers may be left with fewer or no alternative service provider options. For example, the trend in wireless usage is increasing, however, some individuals are not comfortable or satisfied with wireless phone service. On the other hand, the "X-generation" relies heavily on

wireless phone usage with less regard for wireline telephony. Post-auction, end users could potentially be stuck with one telecom carrier and/or delivery mode for the duration of the winning bidder's contract, and reduced customer choice should not be an acceptable outcome.

B. Competition

Under the RA scenario, after a carrier wins the bid to receive the USF support for a given area, it is questionable whether other carriers will continue to serve in that area. It is possible that there would be few or no "unsupported" competitors that continue to operate in a given area and this would adversely impact competition. Without substantive competitive forces, carriers would have less incentive to provide quality service, upgrade networks, invest in new services or control costs. So while RAs may reduce the overall level of high cost support, they may also reduce the level of competition.

VI. MULTIPLE SUPPORT WINNERS

The soundness of allowing multiple support winners in an area could be called into question if it results in confusion regarding service obligations, such as who carries the provider of last resort obligation. Whether there is only one winner or there are multiple winners of high cost support in an area, all supported service providers should be required to satisfy the same service and quality obligations. Further, the contracts or agreements entered into with winning bidders should include clearly delineated and closely monitored obligations.

VII. SELECTION OF WINNING BIDS

The responsibility for administering the bidding process and selecting winning bids would likely rest with the FCC or a third-party administrator. Regardless of the entity that

provides oversight, it is essential that winning bids be chosen based on a bidder's commitment to service and network quality, not simply the "bid price." If the lowest bid for USF support payments is the primary or only consideration when selecting winning bids, investment in infrastructure, service quality and service offerings could potentially suffer.

In many of Oklahoma's rural communities, there is little competition for residential wireline telecommunications service. If the ILECs are forced or choose to lower quality standards in order to achieve a winning bid, the end-users will pay the price. Another potential scenario is that a competitor could win the RA and then receive its "low-bid" high cost support for a period of years while failing to maintain the original standards of quality and service established by the incumbent. So while the ILEC would suffer the consequences of lost support that had traditionally been utilized to provision quality services, the winning competitor would receive a reduced level of support but may be unable, or unwilling, to adequately maintain the existing network and ultimately, the end users bear the greatest risk.

It is possible that there could be no real winners resulting from the RA proposal. A competitor may win a bid but may lack the technical, managerial or financial ability to provide quality service to an area, and may further lack the incentive to launch new technologies in order to remain on par with services offered in urban communities. The losing bidder may be forced to increase rates in an effort to recover lost USF support, while likely losing customers over time to the winning bidder that may be able to offer lower rates. The losing bidder may even be forced to go out of business or file for bankruptcy. Lastly, consumers may be the most adversely affected group if the results prove negative.

VIII. TREATMENT OF INCUMBENTS

In order to create a fair process, incumbents should be required to participate in the reverse auction if and when one occurs. If the incumbent is the losing bidder and there is some requirement to make its network available to the winning bidder, the incumbent should be provided with a means of properly valuing its network investments. The OCC does not support the "taking" of any carrier's assets, but if the RA process places requirements on incumbents to make their networks available to winning bidders, then there should be an opportunity for the incumbent to provide a depreciated value assessment of its assets, and there should be a mechanism to recover stranded investment.

IX. ALTERNATIVE SOLUTIONS

One alternative solution to limit the growth in high cost support would be to increase the threshold that a carrier must exceed in order to receive high cost loop support. Currently, the USF provides support when the cost of service exceeds 115 percent of the National Average Cost Per Line (NACPL). For example, with a NACPL of $324.25, a study area cost per line must exceed $372.89 in order to be eligible for support. Increasing the minimum threshold to 125 percent would mean that the cost per line would have to exceed $405.31 to qualify for support. More significant increases in the threshold support levels would obviously further reduce the overall size of the USF while better targeting support to only the highest-cost carriers.

As a potentially more equitable alternative solution, the FCC could initiate a study to determine by technology (wireline, wireless, VoIP, etc.) the national and "serving area" costs per line. High cost funding could then be based on each carrier's technology-specific cost to provide service as opposed to the current methodology of paying support based on the incumbent's

historic costs. This approach would likely reduce the overall size of the USF but, more importantly, it would better target and calculate support based on carrier-specific costs.

X. CONCLUSION

The reverse auctions model does have the potential to lower consumer USF assessment obligations. However, the Oklahoma Corporation Commission believes that there are far too many unanswered questions and potential unintended consumer consequences for reverse auctions to present a workable solution for controlling the size and growth of the high cost fund. As alternative solutions, the OCC recommends that the FCC contemplate: 1) increasing the "threshold percentages" that must be exceeded in order to receive high cost loop support, and/or 2) determining high cost support based on carrier-specific and technology-specific costs rather than the current methodology of providing support to all ETCs in an area based on the historic costs of the incumbent provider.

Respectfully submitted,

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