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

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service	)	WC Docket No. 05-337
Seeks Comment on the Merits of Using	)	
Auctions to Determine High-Cost	)	
Universal Service Support	)	

NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION REPLY COMMENTS

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COOPERATIVE ASSOCIATION

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SUMMARY

In its initial comments in this proceeding, NTCA noted its support for the universal service goals of providing rural and urban consumers comparable rates and services, and curtailing excessive growth of and inefficiency in the high cost universal service fund (USF). However, the implementation of reverse auctions for determining the distribution of universal service in those areas with pre-existing infrastructure and ubiquitous service would be "a serious mistake."[1] As NTCA noted, "[t]he potential downside of reverse auctions for the determination of universal service provision is too great, the risk of an unfavorable outcome too large, and the stakes too high for reverse auctions to be considered a feasible alternative."[2]

The majority of parties commenting in this proceeding agreed with NTCA that reverse auctions are not the answer for determining high cost universal service support. The minority who support reverse auctions were not able to offer any relevant real world examples of reverse auctions successfully utilized in a manner similar to the way they would be utilized for provisioning universal service support. There was virtually no consensus amongst the supporters as to how the reverse auction system would work—there were disagreements in such fundamental elements as geographic areas to be auctioned, time periods between auctions, and the number of winners to be selected. Scant attention was paid to arguably the biggest obstacle of all—the recovery of previously-incurred investments in infrastructure. Taken as a whole, the record leads inevitably to the conclusion that reverse auctions, quite simply, are not the answer.

[1] NTCA Initial Comments, *In the Matter of Federal-State Joint Board on Universal Service Seeks Comment on the Merits of Using Auctions to Determine High-Cost Universal Service Support*, WC Docket No. 05-337, October 10, 2006, p. 2 (NTCA Initial Comments).
[2] *Id.*

NTCA continues to urge the Joint Board to reject the reverse auction concept and to consider and recommend the following alternatives to accomplish the same goals, with much less risk to those both providers who rely on sufficient, reliable universal service support for the provision of affordable communications services and to the consumers who rely on those providers:

1. Apply a meaningful public interest test when considering future ETC designations;
2. Eliminate the identical support rule;
3. Provide alternative cost-based support to rural wireless ETCs; and
4. Expand the base of USF contributors to include all broadband service providers.

Implementing these four changes to the existing universal service rules will enable the Commission to ensure comparable rates and services for rural and urban consumers and rein in the excessive growth of and inefficiency in the high cost universal service fund associated with the identical support rule.[3] The proposed changes will also ensure that multiple ETCs in any given high-cost area in fact are necessary for providing rural consumers with affordable and comparable services. Expanding the base of contributors to include all broadband service providers will ensure sufficient, predictable and sustainable universal service support that will evolve with the future public communications network that will inevitably rely on IP-based transmission services.

[3] 47 C.F.R. § 54.307.

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NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION REPLY COMMENTS

The National Telecommunications Cooperative Association (NTCA)[4] hereby submits these reply comments in response to the Federal Communications Commission's (Commission's or FCC's) Public Notice in the above referenced proceeding (Notice).[5] In this Notice, the Federal-State Joint Board on Universal Service (Joint Board) seeks comment on the use of reverse auctions (competitive low bidding) to determine high-cost universal service support funding to eligible telecommunications carriers (ETCs) pursuant to Section 254 of the Communications Act of 1934, as amended (the Act).

[4] NTCA is the premier industry association representing rural telecommunications providers. Established in 1954 by eight rural telephone companies, today NTCA represents more than 572 rural rate-of-return regulated telecommunications providers. All of NTCA's members are full service incumbent local exchange carriers (ILECs) and many of its members provide wireless, cable, Internet, satellite and long distance services to their communities. Each member is a "rural telephone company" as defined in the Communications Act of 1934, as amended (Act). NTCA's members are dedicated to providing competitive modern telecommunications services and ensuring the economic future of their rural communities.

[5] *Federal-State Joint Board on Universal Service Seeks Comment on Certain of the Commission's Rules Relating to High-Cost Universal Service Support*, Public Notice, WC Docket No. 05-337, CC Docket No. 96-45 (rel. August 11, 2006) ("Notice").

I. INTRODUCTION

In its initial comments in this proceeding, NTCA noted its support for the universal service goals of providing rural and urban consumers comparable rates and services, and curtailing excessive growth of and inefficiency in the high cost universal service fund (USF). However, the implementation of reverse auctions for determining the distribution of universal service in those areas with pre-existing infrastructure and ubiquitous service would be "a serious mistake."[6] As NTCA noted, "[t]he potential downside of reverse auctions for the determination of universal service provision is too great, the risk of an unfavorable outcome too large, and the stakes too high for reverse auctions to be considered a feasible alternative."[7]

II. THE DISAGREEMENT AMONG COMMENTERS SERVES TO ILLUSTRATE THE COMPLEXITY AND INHERENT DANGER TO THE USE OF REVERSE AUCTIONS FOR DETERMINING HIGH COST UNIVERSAL SERVICE SUPPORT DISBURSEMENT.

There was relatively little support for reverse auctions among initial commenters. Those opposed far outnumbered those who thought that reverse auctions could be a potentially viable solution to limiting the growth in the fund. Even among the minority who stand in favor of reverse auctions, there is a wide range of opinions about how successful the auctions could be, and how they should be run. If there is any mandate at all, it is that reverse auctions simply will not work.

[6] NTCA Initial Comments, p. 2.
[7] *Id.*

A. Even within those industry groups with certain parties indicating support for reverse auctions, there are one or more parties on the other side.

A review of the initial comments filed in this proceeding show a number of industry groups are unanimous in their opposition to reverse auctions: commenter representing small ILECs[8], think tanks[9], and financial groups.[10] Among each of the industry segments where there is some support for reverse auctions, there is also opposition. Of the big ILEC filers, AT&T and Qwest are in favor, CenturyTel, Inc. and Frontier Communications are opposed, and Alaska Communications System is neutral. Of the CLECs, General Communication, Inc. is in favor while RICA is opposed. Of the state commissions, the New Jersey Board of Public Utilities is in favor, while the Oklahoma Corporation Commission, Missouri Public Service Commission, and Iowa Utilities Board are opposed. Finally, among consumer advocates, the American Association of People with Disabilities and the Seniors Coalition are in favor, while the National Association of State Utility Consumer Advocates is opposed. If there is this much dissent within the various industry groups, how can there possibly be agreement between them?

Several of the wireless carriers argue that while there are more wireless subscribers than wireline, most universal service funding goes to ILECs.[11] Aside from

[8] *See*, initial comments of FairPoint Communications, Western Telecommunications Alliance, Rural Iowa Independent Telephone Association, The South Dakota Telecommunications Association, Texas Statewide Telephone Cooperative, Inc., John Staurulakis, Inc., Montana Independent Telecommunications Systems, Oregon-Idaho Utilities Inc./Humboldt Telephone Company, NECA, Oklahoma Carriers, ICORE, OPASTCO, Louisiana Telecommunications Association, Alaska Telephone Association, and the Northwest Associations.
[9] *See*, initial comments of TCA, Inc., Alexicon Telecommunications Consulting, and GVNW Consulting.
[10] *See*, initial comments of Rural Telephone Finance Cooperative and CoBank.
[11] *See*, for example, CTIA Initial Comments, p. iii, Corr Wireless Telecommunications Initial Comments, p. 2, Verizon and Verizon Wireless Initial Comments, p. 5.

the fact that wireless subscribers are individuals while wireline subscribers are households, these commenters fail to address the basic question of what exactly is universal service as applied to wireless carriers. Does it mean that every resident can receive a usable wireless signal at their home? Does it mean that a wireless subscriber can receive a usable signal on every mile of improved roads? Or both? Or what? What is the wireless service that is to be available throughout the designated service territory? What is a usable signal? Voice only, or a minimal speed for access to the Internet, video and other requirements? Unless and until these questions are answered, wireless carriers' ability to serve as a carrier of last resort is uncertain.

There is considerable disagreement as to the number of winning bidders that should be selected—one, two, or more. Many commenters appear to be operating under the mistaken assumption that adding additional carriers is costless. Professor Dale Lehman, in his paper that accompanied NTCA's initial comments, cites evidence that decreasing a carrier's market share by one-half increases unit costs by 52%.[12] This is due to the fact that, particularly in sparsely populated areas, investment is determined more by the size of the area covered than by the number of customers served.

In a new paper accompanying these comments, Lehman presents a simplified quantitative example where he illustrates precisely how the awarding of support to an additional provider increases overall support levels.[13] As this example clearly shows, it

[12] Dale E. Lehman, *The Use of Reverse Auctions for Provision of Universal Service*, October 10, 2006, p. 9 ("Lehman 10/10/06"). Dale E. Lehman is Director of the Executive MBA in Information and Communication Technology at Alaska Pacific University. He has taught at a dozen universities, and held positions of Senior Economist at Southwestern Bell Telephone Company and Member of Technical Staff at Bellcore. He has a B.A. in Economics from SUNY at Stony Brook, and M.A. and Ph.D. degrees in Economics from the University of Rochester. He has published widely in the area of telecommunications economics and policy, including a number of previous papers on behalf of NTCA.

[13] Dale E. Lehman, *Reply to Reverse Auction Comments*, November 8, 2006, pp. 11-12 ("Lehman 11/8/06"). Appended to these reply comments as Attachment A.

must be determined whether the secondary goal of universal service is reducing the overall size of the fund or increasing competition, as these could very well be mutually exclusive.[14]

In addition, the awarding of multiple winners could change the dynamics of the auction itself. As NASUCA points out

> The possibility of multiple winners would obviously have a significant influence on the amounts bid. A carrier that expected to receive all of the support in an area would bid differently from a carrier that expected to have to share the support. This would make the bidding process fraught with a greater than usual level of uncertainty.[15]

Any increase in uncertainty will raise the cost of capital, and/or limit its availability.[16] Either outcome would ultimately increase the amount of universal service support needed.

General Communication, Inc. (GCI) recommends that the Commission freeze per-line universal service support at current levels. NTCA maintains that any freeze on high cost universal service support is incompatible with the Act's mandate of sufficient universal service support. Further, a per-line freeze would likely result in cherry-picking, whereby competitors would enter the market to serve only what they perceive to be the most profitable customers—hardly in the spirit of "universal service."

GCI also talks about their commendable efforts making "advanced services available…in some of the smallest villages in Alaska."[17] It is noteworthy, however, that while the total population in Alaska is small, it tends to be relatively clustered. According to Census Department data, Alaska ranks fifth in the nation in the percentage

[14] *See, Id.*, p. 7.
[15] National Association of State Utility Consumer Advocates Initial Comments, p. 9.
[16] *See,* CoBank Initial Comments, pp. 3-4.
[17] GCI Initial Comments, p. 6.

of overall population living in clustered "places."[18] The key point is that GCI is serving "villages." These villages are small and are scattered, but they are clusters of population. In contrast, many of NTCA's member companies provide carrier of last resort service to areas that are not even towns or villages. The very heart of universal service is providing affordable comparable services to a geographically dispersed customer base. It is extremely impressive that the United States has attained the goal of universal service. It is a credit to the foresight and pioneering spirit of an earlier generation of regulators, legislators and community-based companies that this goal has been reached. It was tremendously challenging and expensive and it took decades to accomplish. Absent sufficient, predictable and sustainable universal service support, in many instances it simply wouldn't happen. GCI claims that their service stands as evidence that "no market is 'too small' for competition."[19] History says otherwise. It is commendable that GCI is offering advanced services in these villages, but it is entirely another matter to bring the same services to areas outside villages and towns. Is GCI willing to offer service in rural areas in the rest of the U.S.? Would the incumbent LEC offer service without support?

NTCA has long asserted that artificially induced competition—competition subsidized in places where it would not otherwise exist—can actually result in a lower quality of service than would otherwise exist. Either the total amount of support must increase to provide sufficient funds to have multiple providers or the quality of service will necessarily diminish over time.

[18] U.S. Census Bureau, Census 2000 Summary File 1.
[19] GCI Initial Comments, p. 6.

Professor Dale Lehman sums up the uncertainty quite nicely when he notes that in their initial comments, proponents of reverse auctions "do not converge on any significant dimension for such auctions—not the number of winners, the size of areas to be auctioned, the time periods for 'licenses' to be held, and not on the impacts on the overall size of the high cost fund."[20] Uncertainty is the enemy of universal service; reverse auctions would open the floodgates to uncertainty of all types.

B. No commenter was able to provide a comparable real-world example of reverse auctions being successfully utilized.

Several commenters noted that reverse auctions, *if properly implemented*, could help solve the problem of excessive growth of the high cost universal service fund.[21] Yet none was able to provide a comparable example of the successful real-world use of such a regime. Verizon offered examples of setting timber prices in British Columbia and establishing stranded electricity investment costs in Texas.[22] Yet these specific instances are very dissimilar to the matter at hand. As NTCA pointed out in its initial comments, "[a]uctions tend to work well in those cases where the bid being made is easily quantifiable, where the service put out for auction is easily defined, the parameters of the service are relatively static, and progress and ultimate results can be easily measured."[23] While the British Columbia and Texas examples cited by Verizon may fit these criteria, the use of auctions for determining universal service support certainly does not, as it "will require that non-quantifiable factors be taken into account, as well."[24] Other proposed

[20] Lehman 11/8/06, p. 7.
[21] *See,* for example, GCI Initial Comments, p. 2, NCTA Initial Comments, p. 4, AT&T Initial Comments, p. 2 and p. 4, Dobson Cellular Systems Initial Comments, p. 3. Virtually all pro-reverse auction commenters included this caveat.
[22] *See*, Verizon Initial Comments, pp. 15-16.
[23] NTCA Initial Comments, p. 6.
[24] *Id.*

examples—the awarding of government and private business contracts,[25] or the provision of telecommunications services in unserved areas in developing countries,[26] are similarly flawed. As Lehman points out, "[these examples] work precisely because the circumstances under which they are utilized differ from the conditions under which universal service must be provided."[27]

Verizon, CTIA, Qwest and others cited the FCC's spectrum auctions as evidence that universal service auctions could be successful.[28] To the contrary, the spectrum auctions illustrate the dangers inherent to auctions. Despite the fact that the spectrum auctions are relatively straightforward, with a discreet and readily defined good being bid upon, the Commission still ran into serious problems, such as non-performing winning bidders. A more complex auction process, such as that proposed by the proponents of reverse auctions for universal service support, would pose even greater potential risks.

Further, as Lehman points out, spectrum auctions have not resulted in universal service, but in "deployment of services in urban and suburban markets with relatively less build-out in rural areas."[29] Bidders' freedom to do just that is what leads them to bid at auction in the first place. On the other hand, "[u]niversal service requires different considerations—ubiquity, quality, and comparability. There is no evidence that spectrum auctions have been able to provide these features."[30] As with the other examples provided by commenters, the spectrum auction example cannot be directly applied to the matter at hand.

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[25] TracPhone Initial Comments, pp. 10-11.
[26] Satellite Industry Association Comments, pp. 4-5. The examples cited refer to previously unserved areas or significant upgrades to the existing infrastructure within these areas.
[27] Lehman 11/8/06, p. 1.
[28] *See*, Verizon Initial Comments, pp. 13-15, CTIA Initial Comments, p. 5, Qwest Initial Comments, p. 2.
[29] Lehman 11/8/06, p. 6.
[30] *Id.*

C. Groups representing those areas in need of universal service support are in unanimous agreement—reverse auctions are unworkable.

Commenting parties representing those providers serving the rural consumers who rely on universal service support for the receipt of telecommunications services were virtually unanimous in their opposition to reverse auctions. These groups are innately familiar with the challenges inherent to serving rural customers, and the risks posed by threats to continued sufficient, predictable and sustainable universal service support.

The lack of a proven track record for reverse auctions, coupled with the other evidence presented in the round of initial comments, underscores NTCA's concerns about "[t]he difficulties and dangers inherent in applying reverse auctions in areas with existing communications infrastructure and ubiquitous service[.]"[31]

III. NTCA'S FOUR ALTERNATIVES ARE THE MOST EFFECTIVE AND LEAST RISKY MEANS OF CURBING EXCESSIVE GROWTH IN THE HIGH-COST FUND.

As NTCA pointed out in its initial comments, while "an appealing theoretical construct, in reality [reverse auctions] are fraught with uncertainty and risk."[32] While the overall goal here—reducing the excessive growth in the high cost universal service fund—is undeniably important, NTCA believes that it can be achieved more efficiently and with much less overall risk through the following four steps:

1. Apply a meaningful public interest test when considering future ETC designations;
2. Eliminate the identical support rule;
3. Provide alternative cost based support to rural wireless ETCs, and
4. Expand the base of USF contributors to include all broadband service providers.

[31] NTCA Initial Comments, p. 2.
[32] *Id*, p. 4.

NTCA advocates a public interest test that focuses not on the impact support will have on overall levels of competition, but on "whether universal service is being maintained and preserved in accordance with the principles of Section 254."[33] NTCA believes that "a meaningful public interest test should…look beyond the short term and consider the long-term impact of multiple ETCs within a single designated area on evolving services that are likely to be deployed widely in urban areas, namely broadband services."[34]

A substantial number of commenters joined NTCA in recommending the elimination of the identical support rule—except for the idea that the current system is flawed and must be fixed, this was the most agreed upon point by the various commenters. Even a cursory review of the numbers shows where the real growth in the fund is coming from: between 2003 and 2006, CETC support has grown 870%, from $106 million to $1.03 billion. Over that same period, ILEC high-cost support has remained unchanged at $3.17 billion.[35] Requiring competitors to only receive support based on their own costs, rather than the incumbent's (which may have no resemblance whatsoever to the competitor's actual costs), would be a giant step in the direction of curbing the unnecessary growth in the fund.

In its initial comments, NTCA highlighted several steps that should be taken to correct the problems associated with the identical support rule, including: applying a similar size criteria in the statutory definition of a "rural telephone company" to determine whether a wireless CETC should be treated like a "rural telephone company";

[33] *Id.*, p. 19.
[34] *Id.*
[35] *See*, Universal Service Administrative Company (USAC) filings with the FCC: USAC 1Q2003 HC01 and USAC 2Q2006 HC01.

allow all wireless CETCs that meet this criteria the option of receiving per-line support based on a reasonable small rural wireless carrier proxy mechanism or demonstrate their wireless costs; and that all wireless CETCs that do not meet the criteria should be allowed the option of receiving support based on the non-rural high-cost proxy mechanism for that state or demonstrate their wireless costs. As previously noted, NTCA believes this change "would enable the FCC to more effectively manage the future growth of the high-cost fund while at the same time provide affordable and comparable rates and services to consumers."[36]

Finally, NTCA urges the Joint Board to recommend to the Commission that all cable, wireline, wireless, electric, and satellite broadband Internet access providers be required to contribute to the universal service fund. Doing so is within the bounds of the Commission's authority under Section 254(d), and would ensure sufficient universal service support and will ensure long-term stability of the USF.

[36] NTCA Initial Comments, p. 23.

IV. CONCLUSION

For the reasons stated above, the Joint Board should reject the reverse auction concept and consider and recommend NTCA's four alternatives to accomplish the same goals, with considerably less risk to service providers and consumers alike.

Respectfully submitted,

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November 8, 2006

CERTIFICATE OF SERVICE

I, Rita H. Bolden, certify that a copy of the foregoing Reply Comments of the National Telecommunications Cooperative Association in WC Docket No. 05-337, FCC 06J-1 was served on this 8th day of November 2006 by first-class, United States mail, postage prepaid, or via electronic mail to the following persons:

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