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

In the Matter of	)	
	)	
Federal-State Joint Board on Universal Service Seeks Comment on Long-Term, Comprehensive High-Cost Universal Service Reform	)	WC Docket No. 05-337 CC Docket No. 96-45

COMMENTS OF GVNW CONSULTING, INC.

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Executive Summary

The Commission should bear in mind that implementing a reverse auction approach for rural carriers could have unintended consequences, including an inability to raise capital and evolve appropriate levels of service. Rural carrier telecommunications networks necessitate investing large amounts of capital in inherently long-lived plant assets. These investments are possible when lenders have a reasonable certainty of debt repayment and investors/stockholders/cooperative members are afforded an opportunity to receive a compensatory rate-of-return. Reverse auctions create uncertainty and would certainly not provide sufficient incentive for efficient, long-term investment strategies that are prerequisite to infrastructure deployment in low density, high cost to serve areas of the country.

Reverse auctions would create no incentive to invest after the contract, and would be especially acute in the later years of a contract cycle. For example, carriers would be unable to justify investing in long-lived assets in the eighth or ninth year of a ten year contract period when faced with the possible loss of support in year eleven.

With respect to cost modeling, the challenges are exacerbated by the fact that the advances of the last decade require a reexamination of just what is "the" forward-looking technology that should be modeled. In addition, the Synthesis Model was developed under an assumption that competition was not present and thus a wireline network would be built to all locations where service was to be provided. Any new modeling should account for the changed competitive environment, including a review of the level of competition in each area to be modeled and a review of the forward-looking assumptions

as to how many and which locations will be served by the forward-looking network model.

With respect to disaggregation, the record to date contains anecdotal evidence that some lines appear to be reported based on the level of support potentially available to that carrier, as opposed to where the customer resides or maintains an address of record. If the Joint Board was to recommend, and the Commission were to adopt some form of mandatory disaggregation, the impact would be analogous to removing a fist from a bucket of water. Once the fist is removed, there is no evidence that it was ever there. Mandatory disaggregation without attention to where CETCs are reporting lines would have a similar indiscernible impact.

Whatever approach is recommended and ultimately implemented for CETC support should include provisions so that the method is both able to be reviewed or audited by third party reviewers and requires the CETCs to be accountable for the use of any support provided.

Rural carriers stand ready to meet their portion of the broadband challenge. The question that this Joint Board and this and future Commissions are faced with is a simple one: "How much of this broadband cost will be recovered from carrier rates and how much will be left to be recovered from support mechanisms?" We respectfully submit that the solution set may be a bit different in rural, high cost to serve areas with low density that it will be in the heavily populated areas served by AT&T and Verizon.

INTRODUCTION AND BACKGROUND

GVNW Consulting, Inc. (GVNW) is a management consulting firm that provides a wide variety of consulting services, including regulatory and advocacy support on issues such as universal service, intercarrier compensation reform, and strategic planning for communications carriers in rural America.

The purpose of these comments is to respond to the Public Notice concerning a request for input on long term, comprehensive high-cost universal service reform. One of the reasons that universal service is working today is that virtually all customers are accounted for within some eligible carrier's service territory. These "carriers of last resort" (COLR) stand ready to serve even the most remote and isolated customers. But, this universally available service comes with a cost. Specifically for rural carriers, in a rate-of-return regulatory environment, the overarching principle that the Commission should adhere to is that rate-of-return carriers are entitled, as a matter of law, to a full recovery of their costs in providing interstate services.

We applaud the Joint Board for its efforts in addressing these key universal service issues. We respectfully request that as recommendations are formulated for submission to the Federal Communications Commission, that the circumstances present in meeting the needs of customers in high cost to serve rural areas are carefully evaluated and factored into the final decision.

REVERSE AUCTIONS

The Joint Board has requested comments on the reverse auction proposals advocated by parties such as Verizon. It would appear from the data currently in the record that reverse auctions do not constitute the competition that was envisioned in TA 96. One may argue that such competitive bidding is actually anti-competitive per TA 96, at least with respect to a customer's access to competitive alternatives. In the proposed reverse auction approaches, carriers are only on an equal basis once every bidding cycle.

If an existing rural wireline carrier were to be unsuccessful in a reverse auction proceeding, it is unclear as to how the Commission would intend to address confiscation issues.[1]

Reverse Auctions raise significant public policy issues for high cost to serve areas

Implementing a reverse auction approach for rural carriers could have unintended consequences, including an inability to raise capital and evolve appropriate levels of service.

It appears that a key to the success of a reverse auction approach is an exacting statement of work. As with any fixed-price bidding system, the success of the contract will depend entirely upon the quality of the statement of work that forms the basis of the proposal. We anticipate that the Commission would intend to define a static set of supported services. Since any services outside of this definition will not qualify as supported services, the ability to evolve services capabilities is seriously compromised as

[1] While Chairman Martin indicated in his statements to Senator Stevens on September 12, 2006 at the Senate Commerce, Science and Transportation Committee hearing that an adequate transition would be contemplated, it is not clear that the Commission may supersede intrastate depreciation rates in light of the *Louisiana* standard.

the auction winner may have no incentive to spend beyond the proscribed service level. This seems contradictory to the administration's goals and Congressional support present for an evolution to broadband networks.

Reverse auctions would create an uncertainty with respect to capital recovery and retard the deployment of rural infrastructure

Rural carrier telecommunications networks necessitate investing large amounts of capital in inherently long-lived plant assets. These investments are possible when lenders have a reasonable certainty of debt repayment[2] and investors/stockholders/cooperative members are afforded an opportunity to receive a compensatory rate-of-return.

Under the proposed reverse auction scenario, universal service support would not be predictable over the long term. After the contract period expires, support for an area would be re-auctioned. In the subsequent period, the initial bidder, who will have made long-term investments to serve a rural area, would only retain its revenues if it submitted the winning second bid. This type of uncertainty would certainly not provide sufficient incentive for efficient, long-term investment strategies that are prerequisite to infrastructure deployment in low density, high cost to serve areas of the country.

Without adequate network performance standards firmly in place, the Commission will have fired the starting gun for a race to the bottom in terms of service quality

The enforcement of service quality standards could be a difficult task for the Commission. In a competitively bid contract scenario, the purchasing party has the obligation to enforce the terms of the contract upon the bidder. At the same time, the financial incentives for the winning bidder are to perform the work at a lower cost than

[2] Conversely, lenders available to rural carriers will be unwilling to provide new capital if there is significant uncertainty regarding the ability to meet principal and interest obligations.

was bid. In order to prevent this natural incentive to cut costs resulting in a degradation of service, some form of oversight by a regulatory authority would be required.

Reverse auctions would create no incentive to invest after the contract, and would be especially acute in the later years of a contract cycle. For example, carriers would be unable to justify investing in long-lived assets in the eighth or ninth year of a ten year contract period when faced with the possible loss of support in year eleven.

Other important policy questions that the Joint Board and Commission must consider include: How does the Commission propose to monitor the winner's performance and how does the Commission intend to handle the provision of service when carriers exit high cost to serve markets if they are not the successful auction bidder?

In this regard, the Joint Board and Commission must be cautious to recognize the interdependence that wireless carriers have on wireline networks. The mobility provider depends on the wireline provider in its call completion architecture. Current wireless, VoIP, and satellite networks require a connection to land line infrastructure to provide full functionality. This network reality is documented in *Wireless Needs Wires: The Vital Role of Rural Networks in Completing the Call*, published by the Foundation for Rural Service in March, 2006. This paper states in part:

> *Without thoughtful consideration by policymakers of the challenges of providing wireless services in rural America, as well as the dependence of wireless services on wireline networks, portions of the nation are likely to remain underserved . . .Most importantly, one must recognize that without the underlying wireline network, wireless networks could not exist in their current form. In spite of this obvious fact, large wireless carriers and policymakers alike continue to pursue practices and policies that will in fact undermine the critical wireline network. While discussions on how to modify reciprocal compensation, access charges, and universal service continue, attention must be placed on ensuring these mechanisms are capable of maintaining the fiscal health of that wireline network.*

Another question that does not appear to be answered is what are the "costs" from a public policy perspective for reverse auction winners that are ultimately unable to perform? Historically, the "carrier of last resort" (COLR) designation has provided a reasonable assurance that customers in remote regions of the country will have access to communications services. An important part of the COLR package has been the availability of universal service support. The reverse auction proposals do not appear to address an adequate fallback position for customers in rural areas where the "winner" is unable to meet its commitment. This leads to another public policy question that must be answered: How would the Joint Board and Commission propose to mitigate a large carrier from low balling a bid to win the auction, and then ignore the low-density portion of the area? While this may not be important to 90+% of the customers, it is of vital importance to the potentially disenfranchised 10%. We encourage the inclusion of a rural incumbent carrier exemption in any approach to reverse auctions.

From a rural carrier perspective, the first phase is for others

When the Commission considered the reverse auction concept a decade ago, there was no public consensus on how to structure competitive bidding to make it reduce the overall amount of support.[3] And, a decade ago, the decision was made to not pursue reverse auctions. If the current Commission chooses to "reverse" this prior decision, we respectfully submit that carriers other than rural wireline carriers should be the subject of such an experiment. Given the uncertainty regarding such an approach, and the lack of

[3] Recommended Decision, CC Docket No. 96-45 (Federal-State Joint Board on Universal Service), November 6, 1996, paragraph 334.

empirical data as to what constitutes a successful auction scenario, we believe rural carriers are not the proper subset on which to experiment in this regard.

Rural carriers often are the only provider of ubiquitous and high-quality service[4] in a service area.

GIS TECHNOLOGY AND NETWORK COST MODELING

In the initiation of a recent docket, Commissioner McDowell offered a statement that is relevant to this aspect of this proceeding. In his statement accompanying the Notice of Inquiry in WC Docket No. 07-52 (FCC 07-31), the Commissioner states in part: "*But we also must resist the temptation to impose regulations that are based merely on theory*." This is particularly important with respect to any proposed cost modeling.

The criteria for success remain rigid

Cost models that yield accurate and representative results remain costly to build and more importantly maintain. A model must be developed with a requisite level of sophistication so that it is capable of handling the vastly different circumstances between urban and rural service areas. This includes tasks such as properly identifying relevant factors, understanding the relationships amongst and between each factor, and then obtaining sufficient data to appropriately model the network configuration and cost. This type of work is time consuming and time sensitive, as the network continues to evolve.

[4] Rural carriers are measured against the 99.999% standard of reliability, not the "fewest number of dropped calls" as cellular carriers claim in their network and cable television advertisements.

The competitive paradigm is evolving

The modeler is faced with a moving target. The need to achieve accuracy demands granularity, and granularity requires that the modeler capture large amounts of data. These requirements produce a resource intensive scenario, one that is expensive to complete.

These challenges are exacerbated by the fact that the advances of the last decade require a reexamination of just what is "the" forward-looking technology that should be modeled. In addition, the Synthesis Model was developed under an assumption that competition was not present and thus a wireline network would be built to all locations where service was to be provided. Any new modeling should account for the changed competitive environment, including a review of the level of competition in each area to be modeled and a review of the forward-looking assumptions as to how many and which locations will be served by the forward-looking network model.

Roads are not available in some rural, high cost to serve areas

The reference to road-based network modeling indeed merits additional investigation on the part of the Joint Board and the Commission. However, during the pendency of this review, certain facts concerning rural service areas must be kept in mind. One fact is that many rural service areas have no roads. An example of this situation was referenced in our 2006 comments to the Commission on reverse auctions and merits repeating here:

An example of the challenges facing rural carriers serving extremely remote areas is found in an article in US Telecom's *Communications Crossroads* Summer 2006

edition. In the cover story *Going the Distance*, the challenges facing Alaska carriers are documented. In the portion of the article about Cordova Telephone Co-op, the story states:

Cordova lies at sea level, but just one mile away – and 2,500 feet up, atop Heney Ridge – is a key microwave and cellular relay station that enables the co-op to send a microwave signal for nearly 35 miles and cell signals for 20. The relay station is covered by snow seven months a year, winds routinely hit 200 miles an hour and snow sticking to the antenna routinely builds out horizontally as much as 15 feet.

Without very careful consideration of all the implications of applying cost modeling to rural areas, one unintended consequence in rural areas would be to leave many customers as if they were standing near the Cordova antenna - out in the cold.

The geography and math remains the same

The Commission has previously recognized that the costs of rural carriers are higher than non-rural carriers. This was demonstrated empirically in the Rural Task Force's (RTF) White Paper 2,[5] and this research was corroborated in NECA's *Trends in Telecommunications Cost Recovery: The Impact on Rural America* report released in October, 2002.

In *The Rural Difference*, the Rural Task Force quantitatively detailed key differences between urban and rural carriers, including but not limited to differences in costs for switching capacity and various expenses and overheads that were driven by differences in the rate calculation denominator.

Any new model development will need to be validated against such rural circumstances, and inputs to the model would need to be verified as reasonable. History has shown us that this process for the Synthesis Model took roughly 24 months. It is

[5] "The Rural Difference", Rural Task Force White Paper 2, released January 2000.

reasonable to expect a similar time frame, or perhaps an even longer one considering the additional steps now required[6], notwithstanding the shorter timeframe desired by the Joint Board.

DISAGGREGATION OF SUPPORT

The Public Notice poses a series of questions concerning the Commission's disaggregation rules, including but not limited to, whether the Commission should make disaggregation mandatory for subject carriers.

While disaggregation of support has, to some degree, depending on the view of the advocate, served the public policy needs to which it was designed, a mandatory disaggregation approach would miss the mark in several key respects.

First, the rules promulgated at 54.315 provided carriers options due to the variety of circumstances facing carriers subject to Part 54 rules. Carriers facing limited competition or carriers with relatively homogeneous service areas would not benefit from disaggregating their federal universal service support.

Second, there are no questions posed in the Public Notice as to how to provide verification or enforcement that competitive carriers are properly reporting "captured" lines in the proper disaggregation zone. The record to date contains anecdotal evidence that some lines appear to be reported based on the level of support potentially available to that carrier, as opposed to where the customer resides or maintains an address of record. If the Joint Board was to recommend, and the Commission were to adopt some form of mandatory disaggregation, the impact would be analogous to removing a fist from a

[6] With increased competition between network providers, the sensitivity of cost data has increased and it is likely to be more difficult to gather such cost information from non-proprietary sources than it was when the Synthesis Model was developed.

bucket of water. Once the fist is removed, there is no evidence that it was ever there. Mandatory disaggregation without attention to where CETCs are reporting lines would have a similar indiscernible impact.

COMPETITIVE ETC SUPPORT

The Joint Board has posed questions concerning how to calculate support for competitive eligible telecommunications carriers. While the issue is of paramount importance, it is not a new issue. On March 1 of this year, Commissioner Copps testified before the Senate Commerce Committee on the topic of USF reform. In recommending that the identical support rule be eliminated, he stated in part: "…*the time has come to put an end to the irrational and costly system of supporting wireless carriers based on the cost of wireline incumbents*."

Three years ago[7], Commissioner Adelstein addressed USF issues in the following manner: "*A large number of CETCs are wireless carriers. Wireline and wireless carriers provide different types of services and operate under different rules and regulations. Their cost structures are not the same. To allow a wireless CETC to receive the same amount of funding as the wireline carrier, without any reference to their cost structures, is artificial*."

These concerns remain valid in 2007 as the Joint Board seeks to develop its recommendations.

[7] OPASTCO 2004 Annual Winter Convention

Auditability and accountability are key components of any approach

Whatever approach is recommended and ultimately implemented should include provisions so that the method is both able to be reviewed or audited by third party reviewers and requires the CETCs to be accountable for the use of any support provided.

Competitive entry that is motivated only by the possibility of universal service support based on other carriers' costs does not serve the public interest in a prudent manner. The recent rapid rise in CETC support has borne out that the USF is a scarce national resource that should be monitored in order to meet the public interest.

BROADBAND

The fifth topic raised by the Joint Board in the Public Notice regards the important question of how current and future broadband investment will be paid for. Several parties, including FCC Commissioners, have lamented where the United States ranks in terms of broadband penetration rates as compared to other countries, several of which are more densely populated. Key Congressional leaders have called for specific levels of capacity to be available in years such as 2010 and 2015, which would require considerable upgrades to current configurations.

The Commission should continue to support broadband investment

As Chairman Martin offered in his February 1, 2007 written statement to the U.S. Senate Committee on Commerce, Science & Transportation: "Broadband technology is a key driver of economic growth. The ability to share increasing amounts of information, at greater and greater speeds, increases productivity, facilitates interstate commerce, and helps drive innovation."

Rural carriers stand ready to meet their portion of the challenge. The question that this Joint Board and this and future Commissions are faced with is a simple one: "How much of this broadband cost will be recovered from carrier rates and how much will be left to be recovered from support mechanisms?" We respectfully submit that the solution set may be a bit different in rural, high cost to serve areas with low density than it will be in the heavily populated areas served by AT&T and Verizon.

Respectfully submitted

Via ECFS on 5/31/07

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