



**TABLE OF CONTENTS**

Summary.....ii

INITIAL COMMENTS OF THE WESTERN ALLIANCE.....1

I. The Western Telecommunications Alliance.....2

II. Conceptual Framework.....4

    Purpose of USF.....4

    Future of the Public Network.....5

    USF Capabilities and Constraints.....7

III. Evaluation of Reverse Auction Option.....11

    Type of Auction.....13

    Term of Auction.....14

    Size of Auction Area.....16

    Services Covered.....19

    Conclusion.....21

IV. Evaluation of Disaggregation Option.....22

V. Evaluation of CETC Support.....22

VI. Conclusion.....24

**SUMMARY**

The Western Telecommunications Alliance (“WTA”) agrees that the size and growth of the Universal Service Fund (“USF”) must be controlled in the short run and the long run. In the short term, WTA supports the Joint Board’s proposed interim cap on CETC support because this is the sector where present and future USF disbursements are mushrooming out of control.

In the long term, WTA supports the elimination of the “identical support” rule. However, WTA has questions and reservations regarding the ability to design reverse auctions that can function effectively and equitably in non-greenfield situations without destroying rural infrastructure investment incentives and financing, or adversely impacting statutory universal service goals.

When evaluating various USF options, regulators should consider: (a) the purpose of the USF; (b) the nature and likely evolution of the existing public network; and (c) the reasonable capabilities and constraints of the USF. This conceptual framework includes: (1) the past successes and critical future import of the USF revenue stream in facilitating investment by small rural carriers in essential rural telecommunications infrastructure; (2) the long-term dependence of business and residential users, as well as wireless and Voice over Internet Protocol (“VoIP”) service providers, upon wireline networks; and (3) the costs and benefits of providing USF support to other segments of the telecommunications industry.

Reverse auctions have been used in some other countries to select carriers to provide defined packages of new telecommunications services to unserved areas. However, it remains unclear and unproven whether and how reverse auctions can be designed and superimposed upon

the existing rural telecommunications industry with its variety of diverse and existing networks, technologies, services, packages, rate structures, quality standards, service areas and carrier sizes. The various types of auctions (winner gets more, winner takes all, and everybody wins) each impose their own uncertainties and disincentives upon investment. Shorter auction terms will wreak havoc upon investment in fiber optic facilities and other expensive equipment having long depreciation lives, while longer auction terms will freeze technology while also dampening investment during the later stages of the term. Small auction areas (e.g. wire centers) will disrupt networks and operations, while both small and large auction areas can be readily used in different ways by national and regional carriers to defeat smaller local carriers or deprive them of critical USF support. Finally, varying services and regulatory costs will further complicate the auction selection process.

While WTA is still exploring long term solutions, it believes that it is time for the Joint Board and Commission to re-examine the assumption that wireless ETCs compete directly and significantly with ILECs, and to eliminate the “identical support” rule that is providing windfall USF dollars to many wireless CETCs. Given that wireline and wireless services are primarily complementary or supplementary services, wireless CETCs should be required to open their books and demonstrate their own actual costs as a condition of receiving USF on the basis of such costs.

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

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

TO: Federal-State Joint Board on Universal Service

**INITIAL COMMENTS OF  
THE WESTERN TELECOMMUNICATIONS ALLIANCE**

The Western Telecommunications Alliance (“WTA”) submits its initial comments in response to the Public Notice (*Federal-State Joint Board on Universal Service Seeks Comment on Long Term, Comprehensive High-Cost Universal Service Reform*), FCC 07J-2, released May 1, 2007.

WTA understands that the recent rapid growth of the Universal Service Fund (“USF”) endangers the stability, sufficiency and future existence of Universal Service programs that have brought essential telecommunications infrastructure and critical economic development opportunities to many rural areas. As demonstrated in Appendix A to the Joint Board’s recent Recommended Decision,<sup>1</sup> this growth has been concentrated in the competitive ETC (“CETC”) sector, and is primarily the result of the gold rush by wireless CETCs for portable “identical support rule” dollars. In stark contrast, USF distributions to incumbent local exchange carriers (“ILECs”) have been flat or declining during recent years.

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<sup>1</sup> Recommended Decision (*In the Matter High-Cost Universal Service Support and Federal-State Joint Board on Universal Service*), WC Docket No. 05-337 and CC Docket No. 96-45, FCC 07J-1, released May 1, 2007

WTA agrees that the size and growth of the USF must be controlled in both the short term and the long term. For the short run, WTA supports the Joint Board's recently proposed interim cap on high-cost support for CETCs because this is the program sector where USF disbursements have been careening out of control. The Joint Board and Commission must stanch the bleeding from this gaping wound before they can examine and address the USF's long-term health issues.

With respect to the long term, WTA has been expending substantial time and effort, both internally and in conjunction with other entities, in the consideration and evaluation of various options for the operation and stabilization of the USF. As of the present date, WTA is still engaged in this process, and does not yet have a comprehensive long-term proposal to offer the Joint Board. For now, WTA wishes to present some thoughts and questions regarding certain USF distribution options listed in the Public Notice – specifically, reverse auctions, disaggregation, and CETC support. WTA will continue to focus upon USF matters, and hopes to be able to present (or to join with others in the presentation of) a long-term plan for USF distribution within the foreseeable future.

## I

### The Western Telecommunications Alliance

The Western Telecommunications Alliance is a trade association that represents approximately 250 rural telephone companies operating west of the Mississippi River.

WTA members are generally small ILECs serving sparsely populated rural areas. Most members serve fewer than 3,000 access lines in the aggregate, and fewer than 500 access lines per exchange. Most members also generate revenues much smaller than the

national telephone industry average, and presently rely upon federal USF dollars for approximately 25-to-50 percent of their revenues.

WTA members serve remote and rugged areas where loop, transport and switching costs per customer are much higher than in urban and suburban America. Their primary service areas are comprised of sparsely populated farming and ranching regions, isolated mountain and desert communities, and Native American reservations. In many of these areas, the WTA member not only is the Carrier of Last Resort, but also is often the sole telecommunications provider that has shown a sustained commitment to invest in and serve the area. WTA members have made significant progress installing broadband facilities and making advanced services available to their rural customers, but still have a long way to go to achieve the goal of ubiquitous broadband availability (particularly as bandwidth demand continues to increase).

WTA members are highly diverse. They did not develop along a common Bell System model, but rather employ a variety of network designs, equipment types and organizational structures. They must construct, operate and maintain their networks under conditions of climate and terrain ranging from the deserts of Arizona to the rain forests of Hawaii to the frozen tundra of Alaska, and from the valleys of Oregon to the plains of Kansas to the mountains of Wyoming.

Predictable and sufficient revenue streams and cost recovery are essential to WTA members if they are to continue investing in and operating essential telecommunications facilities in high-cost rural areas, while providing their rural communities and customers with quality and affordable services reasonably comparable to those available in urban

areas. Therefore, WTA has found it necessary to participate in this and other proceedings that may affect federal high cost support and the economic development of rural areas.

## II

### Conceptual Framework

In evaluating various proposals and options for the long-term design and operation of the USF, the Joint Board and Commission should keep in mind: (a) the purpose of the USF; (b) the nature of the existing public telecommunications network and its likely evolution during the foreseeable future; and (c) the reasonable capabilities and constraints of the USF.

**Purpose of USF.** WTA believes that the critical and overriding purpose of the USF is the encouragement and facilitation of investment in essential rural telecommunications infrastructure. This, and not the promotion and underwriting of competition, is the USF goal that is most congruent and consistent with the governing statute.

The Communications Act sets forth the relevant Universal Service principles and obligations as: (a) quality services at affordable rates [47 U.S.C. §254(b)(1)]; (b) access to advanced telecommunications and information services in all regions [47 U.S.C. §254(b)(2)]; (c) reasonable comparability of rural services and rates vis-à-vis those in urban areas [47 U.S.C. §254(b)(3)]; and (d) specific, predictable and sufficient universal service support [47 U.S.C. §§254(b)(5) and 254(d)].

Investment in essential telecommunications infrastructure for high-cost areas is the keystone that links and satisfies all four of these statutory requirements. State-of-the-art infrastructure is necessary to provide quality traditional and advanced services to rural

residents and businesses that are reasonably comparable to the telecommunications and information services available in urban areas. A specific, predictable and sufficient federal USF provides the assurances of investment cost recovery and loan repayment necessary to convince lenders, investors, directors and owners to approve rural infrastructure investments, and enables investment and related operating costs to be recovered while keeping the local service rates of rural customers affordable and reasonably comparable with urban rates.

In contrast, the Communications Act does not explicitly or implicitly require or authorize the USF to promote competition, particularly in places where it does not arise naturally in response to normal market forces. Whereas the Joint Board and Commission saw fit to supplement the statutory Section 254(b) universal service principles with an additional principle of “competitive neutrality,” the adoption of a policy that the USF should not unreasonably favor particular carriers or technologies does not mean that it must encourage and underwrite artificial competition by offering large amounts of portable “identical support” to multiple CETCs unrelated to their costs (and, very probably, in excess of them) if they enter various rural areas.

**Future of the Public Network.** Notwithstanding claims of changing technologies and cavalier dismissals of “legacy” networks, the future as well as the past of the public telecommunications network and the Internet will continue to be dependent upon wireline networks connecting communities and customers. Digital switches are likely to be increasingly replaced by soft switches and routers as packet technology replaces circuit switched technology, but the transmission lines of wireline networks will still be needed to connect the originating and terminating points of voice, data, and video

messages, as well as to route them through a variety of intermediate points. A substantial portion of existing wireline trunks and loops are already fiber optic facilities, and fiber will continue to be installed closer and closer to the home as bandwidth needs increase.

ILECs will be joined in some markets by cable television companies and wireline competitive local exchange carriers (“CLECs”), but wireline telecommunications networks and services are not going to disappear within the foreseeable future. Existing wireline telecommunications and Internet access services are not only used regularly on a daily basis by a substantial majority of American businesses and residences, but also remain the most reliable communications systems in times of local, regional and national emergency. Moreover, wireline facilities are used extensively by wireless carriers to: (a) connect their cell sites with each other and with their mobile telephone switching offices (“MTSOs”); and (b) to connect their customers with wireline and wireless phones throughout the nation and the world via the public telecommunications network. Likewise, Vonage and other Voice over Internet Protocol (“VoIP”) providers have not been constructing their own networks, but rather depend heavily upon existing wireline networks and facilities to route and connect substantial amounts of their traffic.

Wireless services provide a significant mobility element for many end users, but are not likely to drive out or substantially replace wireline services in most business and residential markets. Rather, wireline and wireless services are predominately complementary or supplementary services, with substantial majorities of businesses and residences still subscribing to both services and likely to do so for many years to come. Whereas the media has published stories about people “cutting the cord,” the majority of such individuals are students and young professionals who are likely to return to the

wireline fold as they become more settled in their careers and family situations. Likewise, while CTIA brags about the growth of the number of wireless phones vis-à-vis wireline phones, a great deal of this pattern is explained by the fact that digital subscriber line (“DSL”) and fiber connections allow an increasing portion of households to be served by a single wire line, whereas the multiple residents of such households often each have their own wireless phones.

It is not clear at this time whether VoIP providers will survive as separate, add-on service providers, or whether VoIP communications services will be furnished primarily by ILECs, CLECs, wireless carriers and cable telephone companies over their own networks. To date, the pure VoIP providers do not appear to have invested significantly in their own infrastructure, and appear likely to remain dependent upon wireline and wireless networks to carry substantial amounts of their traffic for the foreseeable future. To the extent that VoIP becomes the technology of choice for existing wireline and wireless carriers, it will have some of the same general characteristics as existing circuit-switched technology – for example, that costs will be lower in populous urban and suburban areas where packet-mode efficiencies can be more readily realized and higher in sparsely populated rural areas where potential packet efficiency savings are much smaller.

**USF Capabilities and Constraints.** Since its origin in the 1930’s as an implicit mechanism and its establishment in the mid-1980s as an explicit fund, the USF has been very successful in encouraging and enabling small wireline carriers with limited financial resources to invest in essential rural telecommunications infrastructure. The USF may also be used to stimulate increased rural infrastructure investment by large and small

wireless carriers, and/or by the Regional Bell Operating Companies (“RBOCs”) and other large wireline carriers. However, as indicated by the large recent and pending increases in wireless CETC distributions, these additional undertakings are likely to require very substantial expansions in the size of the USF. In addition, they may require separate distribution mechanisms and procedures to address complexities such as the determination of how many competing wireless CETCs should receive USF support in a particular service area without depleting the USF or adversely impacting wireless competition.

The rural ILEC high-cost support program is a major success story that has helped small carriers with limited financial resources and limited access to capital markets to bring quality and affordable telecommunications and information services to their rural service areas, and to sustain and stimulate the economic development of such areas. USF support has helped WTA members and other rural ILECs to upgrade their networks to install digital switches and soft switches, to implement Signaling System 7, to install fiber optic cable and DSL capabilities, to bury lines to limit weather damage and outages, to provide local or centralized equal access, to offer custom calling options, to comply with Emergency 911 (“E911”) and Communications Assistance for Law Enforcement (“CALEA”) responsibilities, and to provide access to the Internet and information services.

However, the job is far from being completed. Whereas many rural ILECs have made impressive starts in upgrading their networks to offer access to advanced services to more and more customers, much more investment will be necessary to further extend and improve rural ILEC networks (*e.g.*, to install fiber optic facilities closer and closer to

customers) in order to achieve ubiquitous or near-ubiquitous access to advanced services, particularly as bandwidth requirements continue to increase.

During the foreseeable future, rural ILECs will need a predictable and sufficient USF revenue stream to continue making these investments, and to repay the loans incurred to make their existing and future investments. As a substantial portion of the former access revenue stream has been transferred into USF mechanisms through the CALLS and MAG orders,<sup>2</sup> the federal USF has become the primary revenue stream for many rural ILECs, and now comprises 25-to-50 percent of the revenues of the typical WTA member. If arbitrage schemes, phantom traffic, regulatory exemptions, toll migration and/or intercarrier compensation reform continue to reduce interstate and intrastate access revenues, rural ILECs will be forced to depend more and more upon the USF. Whereas WTA members and other rural ILECs would prefer to rely much more extensively or predominately upon customer revenues from existing and new services, there are simply not enough such potential additional customer revenues in many high-cost rural areas, particularly if local rates continue to be required to be maintained at affordable and reasonably comparable levels.

WTA recognizes that all existing and potential USF recipients may be called upon to make compromises and accept changes in order to achieve a sustainable USF in the long term. However, it cautions the Joint Board and Commission to be careful in tinkering with rural ILEC programs that have been very successful in achieving universal service goals, that have long been capped in significant part, and that have not been responsible for the recent burgeoning growth of the USF.

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<sup>2</sup> *Access Charge Reform*, 15 FCC Rcd 12962 (2000) ("CALLS Order"); *Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, 16 FCC Rcd 11244 (2001) ("MAG Order").

WTA does not oppose the provision of USF support to qualified wireline and wireless CETCs. The principal long-term issues to be resolved are: (1) the number of CETCs that should be supported in each rural service area; and (2) the basis upon which these CETCs should receive USF support (both in terms of level of support and of CETC eligibility requirements).

The “number of supported CETCs per service area” issue is predominately a “wireless CETC versus wireless CETC” issue, and will be difficult to resolve reasonably and equitably. Given that wireline and wireless services are primarily complementary and supplementary rather than competitive, it is the ability to offer mobility (rather than the receipt or non-receipt of portable USF support) that predominately impacts the ability of wireless carriers to convince wireline customers to subscribe (usually, also) to wireless service. What the receipt or non-receipt of USF support does impact is wireless-to-wireless competition, for the receipt of portable “identical USF support” by one or more wireless carriers in a market will give rise to significant competitive advantages over any wireless competitors that do not receive windfall USF dollars.

At the same time, requests by multiple wireless CETCs for existing “per-line” ILEC support in an increasing number of markets is placing increasing strain upon the USF. At least part of this problem can be alleviated by eliminating the “identical support rule” for portable USF support, and determining instead the USF support provided to CETCs on the basis of their own actual costs. Distributing high-cost USF support to CETCs on the basis of an ILEC’s costs makes no more sense than requiring taxes to be calculated and paid by one entity on the basis of another entity’s income, or providing

medical treatment to one person on the basis of another person's medical history and test results.

WTA also does not oppose the provision of additional USF support to AT&T, Verizon, Qwest and other "non-rural" carriers. Unlike small rural ILECs that lack financial resources and access to capital markets, large and publicly traded non-rural carriers have very substantial financial resources. However, they appear to be constrained by the stock and bond markets from investing in rural infrastructure upgrades that do not promise returns comparable to other investment options. As a result, some rural service areas of some non-rural carriers do not have state-of-the-art telecommunications infrastructure, and do not offer services and service quality reasonably comparable to those in urban areas. The problem faced by the Joint Board and Commission is to determine how much additional USF support can and should be given to non-rural carriers to upgrade their lagging service areas, how much this additional non-rural carrier support will increase the aggregate size of the USF, and how the USF (both existing and increased requirements) can be funded in a sustainable manner.

### III

#### **Evaluation of Reverse Auction Option**

WTA is aware that Chairman Martin and others are interested in exploring the advantages and disadvantages of reverse auctions as a potential USF distribution device. Subsidy auctions have been used in some "green field" situations, primarily in Latin America, to select individual carriers to provide defined packages of payphone or other telecommunications services to previously unserved areas.

WTA has been trying to understand how reverse USF auctions would be designed and conducted, and how they would be likely to impact Universal Service goals and programs. It has serious questions and concerns as to how reverse auctions would affect rural infrastructure investment decisions, financing and cost recovery. It also has major questions and concerns as to how reverse auctions can be effectively and equitably designed and superimposed upon “non-green field” situations consisting of a variety of diverse and existing networks, technologies, services, packages, rate structures, quality standards, service areas and carrier sizes. WTA notes that it is not inalterably opposed to reverse auctions *per se*, but rather that it has not yet been able to see how reverse auctions can effectively and equitably control the growth of the USF while satisfying the Universal Service principles and requirements of Section 254.

WTA has reviewed the Verizon,<sup>3</sup> CTIA<sup>4</sup> and Alltel<sup>5</sup> reverse auction proposals referenced in the Public Notice, and will present its concerns in terms of the following design topics: (a) type of auction; (b) term of auction; (c) size of auction area; and (d) services covered. Its general observation is that the existing structures and circumstances of the U.S. telecommunications industry make reverse auction design extremely complex and volatile, and that virtually any combination of design options will create risks and uncertainties likely to discourage rural infrastructure investment as well as to have other foreseen and unforeseen consequences.

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<sup>3</sup> Letter from Kathleen Grillo, Vice President Federal Regulatory, Verizon, to Deborah Taylor Tate, Federal Chair, and Ray Baum, State Chair, Federal-State Joint Board on Universal Service, WC Docket No. 05-337 and CC Docket No. 96-45 (February 9, 2007).

<sup>4</sup> CTIA Reply Comments in WC Docket No. 05-337 and CC Docket No. 96-45, filed November 8, 2006, Appendix (*Controlling Universal Service Funding and Promoting Competition Through Reverse Auctions* by James Stegeman, Dr. Steve Parsons, Robert Frieden and Mike Wilson).

<sup>5</sup> Letter from Gene DeJordy, Vice President, Regulatory Affairs, Alltel Wireless *et al.* to Deborah Taylor Tate, Federal Chair, and Ray Baum, State Chair, Federal-State Joint Board on Universal Service, WC Docket No. 05-337 and CC Docket No. 96-45 (February 16, 2007).

**Type of Auction.** CTIA proposes a “winner gets more” auction mechanism (in which higher bidders get a lower percentage of the winning USF bid), as opposed to “winner takes all” (only the low bidder gets USF during the auction term) and “everybody wins” (all participating carriers get the same USF as the low bidder) options. The problem with all three options is that they introduce major uncertainties and risks into a rural investment environment where certainty and stability are necessary if small rural carriers are to be able to repay their existing investment loans, and to obtain future investment financing at affordable rates and terms.

The “winner takes more” format is likely to produce a “race to the bottom,” as bidders minimize their planned investment expenditures and service quality costs in order to make the winning bid, and avoid the additional support deductions imposed upon losing bidders. Whether a rural carrier “wins” or “loses” the auction, it is quite possible that it will receive a smaller USF revenue stream than it needs to repay its existing investment loans, much less to convince lenders to approve substantial future investment projects. In fact, even if a future auction does not actually result in a smaller USF revenue stream, the very possibility that it might do so will have an adverse impact upon investment plans and financing.

The “winner takes all” option is even more de-stabilizing for investment (as well as destructive for potential competition), for it presents a steeper “race to the bottom” for a winning bidder that seeks to salvage some USF support rather than nothing, and deprives the losing bidders of all USF support for the designated area during the specified term of the auction. For a rural ILEC receiving 25-to-50 percent or so of its revenues from the USF, the loss of all of its USF support for much or all of its service area in a

“winner takes all” action is a ticket to bankruptcy court for a Chapter 7 dissolution or Chapter 13 reorganization. If the term during which the auction remains effective is moderately long (say, 5 or 10 years), it is quite likely that many losing rural ILECs (as well as other losing CETCs) will no longer be serving the area when the next auction rolls around. Even if a rural ILEC or other small carrier manages to “win” a reverse auction, the possibility that it may lose the next “winner takes all” auction will deter its owners and lenders from making investments having cost recovery and loan repayment periods longer than the remaining auction term.

Even an “everybody wins” auction may adversely impact investment plans and financing. For example, the possibility that an auction participant can bid USF support amount down to an unreasonably low level during a future auction (to gain a competitive advantage or to weaken or drive out a competitor) may create enough risk and uncertainty to discourage certain investment projects and/or render investment financing less available or more expensive.

**Term of Auction.** In addition to the general adverse impacts of auction risk and uncertainty upon investment, the incongruity between the lengthy depreciable lives of telecommunications equipment and the likely effective periods of reverse auctions will wreak havoc upon rural infrastructure investment financing, incentives and cycles.

CTIA suggests an initial 3-to-6 year transition period, and subsequent 5-year auction terms, while Verizon and Alltel leave the critical question of auction terms unaddressed. The critical defect of a short auction term is that most telecommunications equipment is expensive, durable and depreciated over substantial time periods. In CC Docket No. 98-137, the Commission mandated depreciation ranges for large ILECs for

various telecommunications network facilities, including digital switches (12 to 18 years), digital circuit equipment (11 to 13 years), fiber cable (25 to 30 years), metallic aerial or buried cable (20 to 26 years), and metallic underground cable (25 to 30 years).<sup>6</sup>

If a reverse auction designates USF recipients and/or support for a relatively “short” period (e.g., CTIA’s 3, 5 or 6 years), winning bidders will have little or no incentive or financing to invest in facilities and equipment having significantly longer depreciation periods. Since fiber optic lines and virtually all other substantial elements of the telecommunications infrastructure have depreciation lives greater than 6 years (with most having much longer cost recovery periods), a “short” auction term will have a very negative impact upon investment in rural infrastructure upgrades.

Moreover, even if reverse auctions were to designate USF recipients and/or support for a relatively “long” period (e.g., 10-to-20 years), investment cycles will still be disrupted and adversely impacted. First, fiber optic cable (25-to-30 years) and other critical elements of rural networks have even longer depreciation periods. Second, investment incentives and financing options will decrease as the time remaining until the next auction grows shorter (e.g., a carrier will become increasingly reluctant or unable to invest in equipment with a 10-year depreciation period after Year 5 of a 15-year auction term). Third, once a winning bidder has invested in the facilities and services that it promised at the time of the auction (and upon which costs it based the amount its bid), federal and state regulators would have little or no ability to require the bidder to invest in new and improved technologies and services during the remainder of the auction term.

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<sup>6</sup> 1998 Biennial Regulatory Review – Review of Depreciation Requirements for Incumbent Local Exchange Carriers, Report and Order in CC Docket No. 98-137, Memorandum Opinion and Order in ASD 98-91, FCC 99-397, released December 30, 1999, at Appendix B. Whereas smaller ILECs are not subject to the Commission’s depreciation prescription process, they generally use comparable depreciation lives.

In sum, the setting of effective terms for reverse auctions appears to be a “lose-lose” choice between: (a) relatively “short” terms that will discourage investment in virtually all telecommunications infrastructure; and (b) relatively “long” terms that will freeze technology and increasingly discourage investment as the remaining length of the term decreases.

**Size of Auction Area.** Reverse auction design is further complicated by the fact that the service providers likely to participate in such auctions serve existing networks of very different sizes that generally overlap only partially with one another, and that are subject to very different types and amounts of regulation. Rural and non-rural ILEC networks serve study areas that vary in size from a single exchange to most of a state, and that are subject to substantial federal and state regulation (including, rate, accounting, service quality, and Carrier of Last Resort regulation). Wireless networks serve a variety of large and small regions that may or may not cross state boundaries such as Metropolitan Statistical Areas (“MSAs”), Rural Service Areas (“RSAs”), Major Trading Areas (“MTAs”) and Basic Trading Areas (“BTAs”), and have very little regulation beyond federal licensing and radio propagation requirements, CALEA, and some limited federal and state consumer protection rules. Satellite networks can have footprints that include much or all of the Continental United States or Alaska or Hawaii, and that are subject to federal licensing and radio propagation requirements but little rate and service regulation. Cable networks have local franchise areas that may or may not be combined with other local franchise areas by a common headend, but presently are not common carriers or subject to common carrier regulation. VoIP providers claim the worldwide Internet as their service area, and are subject only to very limited federal Title I

regulation. CLECs have substantial discretion to select and design their own networks and service areas, and are subject to minimal federal or state regulation beyond caps on their interstate access charges.

The key fact is that virtually all likely or potential reverse auction participants have developed and serve their own existing networks. The proposals of Verizon that auctions be held for wire centers, and of Alltel that auctions be held for ZIP codes, make little sense because existing networks are of significantly different sizes and shapes. All but the smallest rural ILEC networks serve multiple wire centers, while the national and regional networks of Verizon and other large wireline and wireless carriers encompass hundreds or thousands of wire centers. Likewise, all but the smallest rural ILEC networks serve multiple ZIP codes or portions of ZIP codes (which postal areas have little or no relationship to telecommunications networks), while the networks of Alltel and other large wireline and wireless carriers may include all or part of hundreds or thousands of ZIP codes.

In the reverse auction context, small auction areas like wire centers and ZIP codes will permit large ILECs like Verizon to qualify for substantially greater USF distributions. Whereas the higher costs of their rural wire centers are currently “averaged down” when included in study area calculations dominated by their urban and suburban wire centers, determining USF eligibility on a wire center-by-wire center basis will permit Verizon and other large ILECs to qualify for USF support in hundreds or thousands of additional wire centers located in study areas where they do not presently qualify for such support.

From a rural ILEC standpoint, the use of wire centers or ZIP codes as auction areas would be extremely disruptive. Because most rural ILEC networks encompass multiple wire centers and ZIP codes, it would be likely that some (and perhaps many) rural ILECs would receive different amounts of USF support (including no support at all) for different portions of the same network. This would wreak havoc with investment and pricing decisions, with the likely end result being degradation of entire rural ILEC networks.

At the same time, the use of small auction areas like wire centers or ZIP codes will give national and regional wireless CETCs like Verizon and Alltel that serve hundreds or thousands of such areas very substantial bidding advantages over rural ILECs and small wireless carriers that serve much smaller numbers of areas. The large carriers can afford to make “low-ball” bids for particular wire centers (*e.g.*, where they have substantial competition or want to cripple existing or potential competitors), and then internally cross-subsidize such wire centers from the revenues and USF support they receive throughout the numerous other wire centers in their networks.

In contrast, the designation of large auction areas such as Economic Areas, MSAs, MTAs and BTAs would ensure domination of reverse auctions by the large national or regional ILECs and wireless CETCs that would likely be the only entities capable of serving most or all of such areas. The likely result would be very similar to the current service patterns of the large wireline and wireless carriers – excellent service in urban and suburban areas, with declining service and quality as population density decreases and distances and costs increase.

Finally, combinatorial bidding does not appear capable of solving auction area problems. While it would allow individual service providers to group and bid for auction areas in a manner more closely approximating their own networks, it would turn auctions into incomprehensible free-for-alls in which participants would bid for differently shaped and sized areas that overlap, in part, one or more of the areas bid for by one or more of other participants. It is not clear how the Commission could reliably and lawfully determine the winning bidders of such “apples, oranges, grapefruits and bananas” jumbles.

**Services Covered.** Prospective reverse auction participants provide very different types, qualities and packages of services pursuant to different prices and pricing plans. WTA does not see any viable way for the Joint Board and Commission to superimpose equitable auction bid evaluation standards upon this existing market place.

The Joint Board and Commission could allow each bidder to propose a level of USF support for its own unique existing configuration of services, quality and rates, and then try to make a reasonable and legally sustainable choice among the resulting different bids for different configurations. The end result would be likely to resemble the subjective “beauty contests” that used to be employed to select the initial winners of comparative broadcast and comparative cellular hearings, and would almost certainly end up in appellate court with equal frequency.

In the alternative, the Joint Board and Commission could specify a common set of services and rates which the winning bidder would be required to offer. This set of services could be: (a) an ideal set of desired services; (b) a “best practices” set of services; (c) an averaged set of services; or (d) a lowest common denominator set of

services. It could be determined on a national, state or local basis. This approach would enable reverse auctions to function more like eBay and spectrum auctions where all bidders are valuing and bidding for the same item (although this would also require the problem of differing service areas to be resolved). However, it would force the Commission or state commissions to involve themselves extensively in service, marketing and pricing oversight from which they have been trying to withdraw. It could also encounter substantial consumer resistance and complaints, particularly if winning bidders were required to modify their existing rates, rate plans and/or service packages.

Bidding for service configurations is also complicated by the fact that ILECs have significantly higher costs because they are forced to comply with more onerous and expensive regulatory requirements. For example, Carrier of Last Resort obligations have long saddled ILECs with higher costs than CLECs and wireless carriers by requiring them to serve high-cost, low-revenue customers and communities that would not be likely to be served if ILECs were free to make purely economic investment and service decisions. In contrast, CLECs can design their own service areas, while cellular and PCS build-out requirements permit wireless carriers to leave many sparsely populated and high-cost portions of their license areas unserved. ILECs must also comply with many other federal and state regulatory requirements not applicable to CLECs and wireless carriers, including rate regulation, accounting and recordkeeping requirements, and reporting obligations.

Finally, the possibility that broadband services will become supported universal services adds further levels of complexity. WTA is well aware that many legislators and regulators are very interested in expanding broadband deployment, and understands that

this may require very large increases in USF dollars at a time when the sustainability of the USF is already in question. Moreover, whereas the term “broadband” is regularly bandied about, it is carefully and specifically defined with much less frequency.

WTA is very interested in exploring the implications and costs of adding “broadband” to universal service. It believes that the Joint Board and Commission need, at an early point, to define what bandwidth or bandwidths constitute “broadband” in a universal service context and to determine whether there is sufficient demand and/or market share for such bandwidth(s) to justify classification of “broadband” as a universal service. However, even if the Joint Board and Commission are able to determine a reasonable bandwidth definition for broadband for initial reverse auction purposes, the rapidly changing nature of broadband technologies and services pose serious dangers that such definition will be outmoded long before the end of the initial auction term.

**Conclusion.** WTA is aware that the Verizon and Alltel proposals contemplate experimentation with reverse auctions initially, particularly in situations where multiple wireless CETCs are seeking or receiving USF support in the same area. Whether or not such limited “all-wireless” reverse auctions would be effective and equitable, there would remain very complex design issues to be resolved before reverse auctions could be extended generally to an intermodal environment including participants with differing services, service packages, rate and cost structures, networks, equipment, depreciation lives, service areas and regulatory obligations. Given these design issues, as well as the risk of significant disruption and disincentive for critical rural infrastructure investment, WTA believes that the reverse auction option should not be selected or implemented before less disruptive options are fully considered.

## IV

**Evaluation of Disaggregation Option**

Disaggregation has been an option for rural ILECs since the implementation of the Rural Task Force proposals. Some WTA members have elected to disaggregate their study areas into higher-cost and lower-cost zones, while others have elected not to exercise the option.

The primary purpose and impact of disaggregation have been to discourage wireless CETCs from gaming the “identical support” rule by serving the more densely populated and lower-cost areas of rural ILEC study areas while claiming the averaged per-line portable support for the entire study area. As discussed below, this problem can be resolved more effectively and equitably by eliminating the “identical support” rule and requiring all USF recipients to receive support on the basis of their own costs.

## V

**Evaluation of CETC Support**

The “identical support” rule was adopted and rationalized by previous Commissions as promoting “competitive neutrality.” However, it has never been explained satisfactorily why any ETC should receive USF support in amounts that do not bear (or even purport to bear) any relationship whatever to its own investments, costs, facilities or services in the affected rural area. This is particularly true where the portable per-line rural ILEC support sought by wireless CETCs is based in significant part upon Carrier of Last Resort and other substantial regulatory costs not incurred by wireless CETCs.

As indicated above, it is time for the Joint Board and the Commission to re-examine the assumption that wireless ETCs compete directly and significantly with ILECs. Notwithstanding some reported instances of “cutting the cord,” substantial majorities of American businesses and households continue to subscribe to both wireline and wireless services. Moreover, although the Commission has long had the authority in Section 3(26) of the Act to classify and regulate Commercial Mobile Radio Service providers as “local exchange carriers,” it has not heretofore exercised its discretion to do so and to treat them as full-fledged competitors of ILECs.<sup>7</sup>

Rather, wireline and wireless services appear to complement or supplement (rather than compete with) each other. Virtually all businesses subscribe to single-line or multi-line wireline service, while many of their employees carry business or personal wireless phones. Likewise, most stable and established residences subscribe to one or two wirelines (increasingly, to a single DSL line) as well as to separate wireless phones for most or all adult and adolescent residents. This latter phenomenon is producing increasing anomalies wherein a rural ILEC receives a specified amount of USF support for serving a rural residence, while a wireless CETC receives two, three or four times that amount in portable “per-line” support for providing separate wireless phones to the separate individuals living at the same address.

WTA recommends that the Joint Board and the Commission terminate the “identical support” rule on the ground that ILECs and wireless ETCs are not predominately competitors, and that neither competitive neutrality nor any other reason justifies the continued distribution to wireless CETCs of the same per-line USF support

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<sup>7</sup> *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, CC Docket No. 96-98, First Report and Order, FCC 96-325 (released August 8, 1996), at par. 1004.

provided to ILECs. Rather, wireless and other CETCs should henceforth receive USF calculated solely on the basis of the actual and properly allocated and depreciated costs of the facilities they construct and install in high-cost rural areas to serve the residents thereof.

The task of developing and adopting USF accounting and allocation standards for CETCs should not be a complicated, onerous or expensive one. CETCs need not be required to adopt the Uniform System of Accounts (“USOA”) in order to maintain the records and accounts necessary to determine and verify their relevant actual costs of providing supported services for USF purposes. WTA believes that the ultimate CETC accounting requirements can and will be very similar to their existing financial and cost accounting systems. It believes that the asserted “difficulty” and “expense” of such accounting requirements is merely a smokescreen by wireless CETCs that do not want to open their books to potential regulatory scrutiny. However, whether their USF accounting and cost substantiation requirements are substantial or minimal, CETCs should be required to accept and implement them as a condition of receiving substantial amounts of federal USF dollars.

## VI

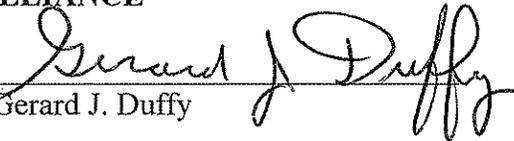
### Conclusion

WTA agrees that the size and growth of the USF must be controlled in both the short term and the long term. In the short run, WTA supports the proposed interim cap on the CETC support that is the primary cause of present USF growth. In the long run, WTA agrees that the time has come to reexamine and eliminate the “identical support”

rule and to require all USF recipients to open their books and receive USF support solely on the basis of their own actual costs.

While trying to keep an open mind on reverse auctions, WTA believes that “the devil is in the details” and that it will be extremely difficult to design reverse auctions that can be superimposed upon the very complex and diverse segments of the existing rural telecommunications industry without discouraging and disrupting infrastructure investment and/or producing other foreseen and unforeseen consequences that violate statutory universal service principles and requirements. WTA believes that the reverse auction option should not be selected or implemented before less risky and disruptive options are fully considered.

Respectfully submitted,  
**WESTERN TELECOMMUNICATIONS  
ALLIANCE**

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