FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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

REPLY COMMENTS OF VERIZON[1] AND VERIZON WIRELESS

I. INTRODUCTION AND SUMMARY.

The Commission should impose an interim cap on the amount of high cost support to competitive eligible telecommunications carriers ("ETCs") until the Commission puts in place comprehensive universal service reform. Capping competitive ETC support on an interim basis would stabilize the high cost fund and ease the increasing demand on consumer contributions to the fund. The interim cap has received strong support from consumer advocates, state commissions, and the industry, and the Commission should move quickly to adopt the Joint Board's recommendation.[2]

Parties opposing the interim cap distort its impacts. Claims that the interim cap would adversely affect wireless voice or wireless broadband services in rural areas are simply not true. The interim cap would not reduce support to competitive ETCs, but rather would maintain such support at 2006 levels. In addition, wireless carriers, including two of the four largest carriers in

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[1] In addition to Verizon Wireless, the Verizon companies participating in this filing are the regulated, wholly owned subsidiaries of Verizon Communications Inc. (collectively "Verizon").

[2] *Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Recommended Decision, FCC 07J-1 (Fed.-State Jt. Bd., rel. May 1, 2007) ("*Recommended Decision*").

the vast majority of their service areas, have been able to serve customers in rural areas without subsidies, and all carriers will continue to have the incentive to offer quality wireless services as a matter of competitive necessity, regardless of whether high cost support is capped. Moreover, under the current system ETCs enjoy a significant advantage by basing support on the incumbent LEC's costs and by allowing recovery of support for multiple handsets to the same customer. The interim cap would help correct this.

The Commission has broad discretion to adopt caps on universal service funding, and an interim cap on competitive ETC support would not violate the Telecommunications Act of 1996 ("Act"), notwithstanding claims to the contrary. The interim cap is competitively neutral because it merely places temporary constraints on funding to competitive ETCs, similar to the limits in place for incumbent local exchange carriers ("LECs"). The interim cap would not give incumbent LECs a competitive advantage, particularly when competitive ETCs receive support based on the incumbent LEC's costs and for multiple handsets to a customer, allowing competitive ETCs to receive subsidies well in excess of their costs.

The Joint Board's recommendation is a necessary step on the path to long term reform. Such a cap will stabilize the fund over the short term and allow the Joint Board and the Commission the time and the opportunity needed to adopt real, comprehensive reform. The Commission should act quickly in adopting and implementing the Joint Board's recommendation.

II. THE INTERIM CAP WILL BENEFIT CONSUMERS.

A. Capping Support To Competitive ETCs On An Interim Basis Is Widely Supported In The Industry.

Numerous commenters have endorsed an interim cap on support to competitive ETCs. Supporters of such a cap include the National Association of State Utility Consumer Advocates;[3] state public service commissions in California, Iowa, New Jersey, New York, Nebraska, and Ohio;[4] wireless carriers;[5] wireline carriers;[6] and numerous trade associations.[7] While certain of

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[3] Comments of the National Association of State Utility Consumer Advocates at 1-2 & 12 ("NASUCA Comments") (supporting the *Recommended Decision*, noting that the "Commission cannot stand by as consumers continue to pay ever-increasing amounts into the USF . . .").

[4] Comments of California and California Public Utilities Commission at 2 (noting that "without the cap, California ratepayers will be burdened with paying for a federal fund that may continue to grow unfettered"); Comments of Iowa Utilities Board at 1; Comments of New Jersey Board of Public Utilities at 3-4; Comments of New York State Department of Public Service at 2; Comments of Nebraska Public Service Commission at 1 (interim cap "would stem the growth of the federal fund"); Comments of Public Utilities Commission of Ohio at 4 (noting that "attempting to reform the USF High-Cost Fund without imposing an interim "freeze" to cap CETC High-Cost support would allow the problem to worsen, even as parties work to resolve it").

[5] Comments of AT&T at 1-2 ("AT&T Comments"); Comments of Corr Wireless at 1-2 ("A cap is a quick and efficient way to stop growth in USF revenue requirements while maintaining something like the status quo"); Comments of TracFone Wireless, Inc. at 1; Comments of Verizon and Verizon Wireless at 1-6 ("Verizon Comments").

[6] Comments of the Blackfoot Telecommunications Group at 5-6; Comments of CenturyTel, Inc. at 2; Comments of Comcast Corporation at 2; Comments of Embarq Corporation at 1 ("Embarq Comments"); Comments of Frontier Communications at 2-3; Comments of Mid-Rivers Telephone Cooperative at 6-8; Comments of TDS Telecommunications Corporation at 1; Comments of Windstream Communications at 1-2; Comments of Totah Communications, Inc., et al., at 2-3; Comments of Valley Telephone Cooperative, Inc. at 3-4.

[7] Comments of Alaska Telephone Association at 2-3; Comments of Iowa Telecommunications Association at 2-3; Comments of Independent Telephone and Telecommunications Alliance at 2-3; Comments of Minnesota Independent Coalition at 1-2; Comments of National Telecommunications Cooperative Association at 1; Comments of Nebraska Rural Independent Companies & South Dakota Telecommunications Association at 2; Comments of the National Exchange Carrier Association, Inc. at 2; Comments of the Organization for the Promotion and Advancement of Small Telecommunications Companies at 2-5.; Comments of Rural Independent Competitive Alliance at l; Comments of Rural Telecommunications Group at 3; Comments of State Independent Telephone Association of Kansas and the Independent Telecommunications Group at 2; Comments of Telecommunications Association of Michigan at 1; Comments of Telephone Association of Maine at 1; Comments of Texas Statewide Telephone Cooperative, Inc. at 1-2; Comments of the United States Telecom

these commenters propose modifications to the interim cap recommended by the Joint Board, there is considerable support for capping competitive ETC support on an interim basis in order to stabilize the high cost fund.

B. The Interim Cap Will Stabilize The High Cost Fund And Ease Demands On Consumers.

The universal service fund is intended to ensure that consumers have access to telecommunications services at affordable rates. Increased demands on the high cost fund – driven primarily by increased support to competitive ETCs – threatens such access as consumers face escalating universal service surcharges on their monthly bills. This trend shows no sign of slowing absent Commission action. The cap on competitive ETC support is a reasonable cost control measure that is well within the Commission's discretion and will ensure that consumers have continued access to affordable telecommunications services.

As the Joint Board correctly observed, high cost support has nearly doubled since 2001, ballooning from $2.6 billion to approximately $4 billion.[8] And the source of this dramatic growth is clear – "increased support provided to competitive ETCs ...." *Recommended Decision*, ¶ 4. While support to incumbent LECs has been "flat or even declining since 2003," support to competitive ETCs "grew from $15 million *to almost $1 billion*" between 2001 and 2006. *Id.* ¶ 4 (emphasis added). This growth in the high cost fund threatens the affordability of telecommunications services – an issue few commenters opposing the interim cap bother to address.

Association at 1-3; Comments of Western Telecommunications Alliance at 1; Comments of Wisconsin State Telecommunications Association at 3-4.

[8] *Recommended Decision*, ¶ 4 (citing *Universal Service Monitoring Report*, CC Docket No. 98-202, Prepared by the Federal and State Staff for the Federal-State Joint Board on Universal Service in CC Docket No. 96-45, Table 3.2 (2006)).

Alltel disputes the notion that increased support to competitive ETCs is the cause of growth in the high cost fund, claiming that the Joint Board's conclusions concerning the levels of current and predicted competitive ETC subsidies are "unsupported."[9] But other parties, including CTIA, concede that high cost support to competitive ETCs has increased dramatically in recent years and that the amount of such support was approximately $1 billion in 2006.[10] And even Alltel has acknowledged receiving more support in 2007 than it received in 2006. Indeed, just two months ago, Alltel told investors that it received $80 million in universal service support in the first quarter of 2007; this amount represented an increase of more than 32 percent from the approximately $54 million in net universal service funding that Alltel received in the first quarter of 2006.[11] Thus, there is no question that the support paid to Alltel and other competitive ETCs will continue to spiral in 2007 and beyond absent Commission action.

Sprint Nextel identifies other potential areas of reform that the Joint Board could have recommended which, according to Sprint Nextel, would be as effective "at controlling the high-cost fund as would the proposed CETC cap."[12] While there are serious problems confronting

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9 Comments of Alltel at 5 ("Alltel Comments").

10 *See* Comments of Sprint Nextel Corporation at 5 (not disputing "that CETC receipts from the high-cost fund have increased over the past few years") ("Sprint Nextel Comments"); Comments of CTIA – The Wireless Association at 3 (noting that "[o]ver the past five years, annual high-cost universal service support for wireless ETCs has increased to about $1 billion") ("CTIA Comments"); *see also* Embarq Comments at 4 (conducting analysis suggesting that high cost support could grow by $150 million annually if the Commission were to grant all pending ETC applications).

11 *Compare* Alltel Corporation Form 10-Q for the Quarterly Period ended March 31, 2007, at 26, *with* Alltel Corporation Form 10-Q for the Quarterly Period ended March 31, 2006, at 34.

12 Sprint Nextel Comments at 3-4 (noting that the Joint Board could have recommended: (i) using forward-looking costs rather than embedded costs to determine rural LEC high cost support; (ii) revising the rule which bases rural LEC support on a comparison of each rural LEC's revenue requirement per line with a nationwide benchmark; (iii) limiting high cost support to those incumbent LECs that charge a minimum prescribed rate for basic local service; and (iv) reducing explicit support to incumbent LECs that "earn supra-competitive rates of return").

the high cost fund – some of which the interim cap on competitive ETC support would not solve – the interim cap is a critical and necessary first step in stabilizing the fund while the Joint Board and the Commission consider comprehensive reform. Keeping the interim cap in place until the Commission adopts such reform would benefit consumers by protecting them from the risk that the high cost fund will continue to grow out of control before real change is in place. An interim cap on competitive ETC support pending comprehensive reform is logical and reasonable because it responds to the immediate threat to the sustainability of the high cost fund and benefits consumers in the interim.[13]

III. PARTIES OPPOSING THE INTERIM CAP DISTORT ITS IMPACTS.

A. The Interim Cap Will Not Have a Detrimental Impact On Wireless Service In Rural Areas.

In opposing the interim cap, some commenters make apocalyptic predictions about the demise of wireless service in rural areas unless universal subsidies to competitive ETCs continue unabated.[14] Such rhetoric is simply not credible.

First, the suggestion that the interim cap would prevent wireless carriers from building out their networks to serve rural areas with few customers is inaccurate. Alltel Comments at 19-20. The fund, as currently structured, is not targeted to promote build-out to areas where wireless services are not available today. Instead, rather than expanding coverage, the current system rewards wireless carriers for selling additional handsets in the subsidized area, which

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[13] While the interim cap will not solve inefficiencies in the current high cost program, it also will not encourage incumbent LECs to inflate their costs, as CTIA asserts. CTIA Comments at 6. This assertion ignores that many forms of high cost support to incumbent LECs are already capped; thus even assuming that incumbent LECs had the "incentive" to "overstate costs," they do not have the ability to do so by virtue of the caps.

[14] CTIA Comments at iii (alleging that "in many, many areas, facilities will not be deployed, service quality will not improve, public safety will suffer, and rural communities will be bypassed"); Alltel Comments at 18-19 (the interim cap "would substantially reduce incentives for wireless carriers to invest in improving service in high-cost areas, and would degrade wireless service ...").

they do "by investing in more retail outlets, a bigger advertising budget, or other marketing activities."[15] To the extent wireless carriers are deploying such facilities in remote areas, they are doing so consistent with their own business plans, not because of the availability of universal service subsidies.[16] Indeed, a recent study by Kavin Caves and Jeffrey Eisenach of Criterion Economics reveals through regression analysis that "subsidies do not appear to result in significantly greater wireless coverage or choice."[17]

In the more than 800 study areas where there is a subsidized wireless carrier, there are only 329 study areas in which a subsidized wireless carrier provides coverage to populations not served by an unsubsidized wireless carrier.[18] Alltel, for example, received approximately $228 million in CETC subsidies in 2006.[19] In 187 of its subsidized study areas, Alltel provides zero incremental coverage compared with unsubsidized carriers while still drawing $91.8 million from the fund to provide service in those areas.[20] Again, this is what the fund currently incents – duplicative subsidies (often several times over) in areas where market conditions are themselves sufficient to encourage wireless carriers to offer service without subsidies. In fact, of Alltel's approximately 700 retail stores, "only 28 of these stores are in areas where Alltel is subsidized

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15 *The Effects of Providing Universal Service Subsidies to Wireless Carriers*, Criterion Economics, L.L.C., Kevin W. Caves & Jeffrey A. Eisenach, 29 ("Caves & Eisenach").

16 *See* NASUCA Comments at 6 (noting that "while it is likely that the receipt of universal service funds eases wireless carriers' deployment of services in rural areas, many carriers were and have been deploying wireless facilities without such support").

17 Caves & Eisenach at 42.

18 *The Availability of Unsubsidized Wireless and Wireline Competition in Areas Receiving Universal Service Funds*, Criterion Economics, L.L.C., Nicholas Vantzelfde, 15 ("Vantzelfde").

19 *Id.* at 18.

20 *Id.*

and provides unique wireless coverage."[21] This lack of proper targeting is something that should be addressed as a part of long-term reform. But in the meantime, it is not the case that capping support would have a dramatic effect on build-out during the interim period.[22]

Second, many wireless carriers have more generally been able to deploy facilities and provide quality wireless service in areas across the country, including rural areas, with little or no universal service subsidies. For example, two of the four largest wireless carriers – Verizon Wireless and T-Mobile – currently provide service to much of the country without high cost support in the vast majority of their service areas. Indeed, unsubsidized carriers actually do a better job of providing service in these areas than subsidized carriers. *Unsubsidized* wireless carriers today provide coverage to 97.3 percent of the population in study areas where wireless ETCs receive USF subsidies, while the subsidized carriers provide service to only 70 percent of the population in those study areas.[23] In addition, "of the 103.7 million pops covered by wireless CETCs, only 3.2 million people, or roughly 1.5 million households, receive coverage from subsidized carriers that is not duplicated by at least one unsubsidized carrier."[24] Clearly, wireless providers are able to provide service in these areas without additional subsidies.

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21 *Id.* at 19.

22 *See* Comments of the Maine Public Utilities Commission at 2. To the extent there are areas where the interim cap would truly jeopardize "the public health and safety," *id.*, or prevent the offering of service in sparsely-populated or unserved areas, Comments of DialToneServices, L.P., a state or affected ETC could seek a waiver of the cap. *See* 47 C.F.R. § 1.3 (general waiver provision of Commission rules); *Federal-State Joint Board on Universal Service; Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, Transport Rate Structure and Pricing, End User Common Line Charge*, Fourth Order on Reconsideration in CC Docket No. 96-45, Report and Order in CC Docket Nos. 96-45, 96-262, 94-1, 91-213, 95-72, 13 FCC Rcd 5318, ¶ 38 (1997) (providing for waiver of indexed cap on growth in high cost loop fund).

23 Vantzelfde at 10.

24 *Id.* at 15.

This certainly has been the case with Cingular, now AT&T Mobility, which historically has provided wireless service in the vast majority of areas it serves without high cost subsidies. However, AT&T is seeking ETC designations and high cost support in several states.[25] The high cost fund would be further strained if AT&T's ETC petitions are granted. Competitive pressures could also force those carriers that do not now draw high cost subsidies to seek ETC designations in the future, putting additional pressure on the fund.

Third, the interim cap on competitive ETC support would not impact the provision of wireless service in many rural areas. As the Joint Board explained, in states where the uncapped amount is less than the capped amount, support to competitive ETCs would not be reduced. *Recommended Decision* ¶ 11. Similarly, in rural areas with only one competitive ETC, the interim cap would not reduce the support that carrier receives but would only maintain the amount of that support at 2006 levels.

Fourth, the interim cap would not adversely impact wireless service in those states where competitive ETCs currently do not receive high cost support. For example, Alltel claims that the interim cap would prevent it from receiving support in South Carolina "where Alltel operates and seeks to provide service in high-cost areas but has been unable to obtain ETC status to date." Alltel Comments at 17-18. However, Alltel already offers service throughout the entire state of South Carolina, in both urban and rural areas, and obviously can do so without universal service subsidies.[26] Furthermore, there are 12 wireless carriers providing service in South Carolina, and all counties in South Carolina have at least two wireless providers.[27]

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[25] Verizon Comments at 4, n.6.

[26] Alltel National Freedom ® coverage map (available at http://www.alltel.com/personal/wireless/plans/nf_coverage_map.html).

[27] *Implementation of Section 6002(d) of the Omnibus Budget Reconciliation Act of 1993*, Eleventh Report, WT Docket No. 06-17, at 97 (Table 2 - FCC's Semi-Annual Local Telephone

The vibrant wireless competition in South Carolina and other states that do not receive high cost support belies CTIA's suggestion that the "explosive and dramatic" growth in wireless subscribership and minutes of use has been driven by the "growth of wireless carrier high-cost universal [service] funding ...." CTIA Comments at 3. Wireless service has been successful because of its mobility, quality, and attractive pricing, not because of universal service subsidies. Indeed, the significant growth in wireless subscribership and minutes of use has been driven in large measure by the four national wireless carriers, two of which currently receive no high cost support in the vast majority of their service areas.

C. The Interim Cap Will Not Have An Adverse Affect On Broadband Deployment.

There is no merit to the claim that the interim cap "would inhibit the deployment of broadband services to rural America."[28] Wireless carriers are committed to deploying new and innovative broadband services – the roll-out of which does not rely upon or require universal service subsidies. As the Commission correctly observed, "market forces have encouraged the deployment of advanced and high-services on a reasonable and timely basis."[29] These market forces have led Verizon Wireless to deploy its EV-DO (Evolution-Data Optimized) service,

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Competition Survey: Mobile Telephone Subscribership) & 109 (Map 1 – Mobile Telephone Operator Coverage Estimated by County) (Sept. 26, 2006) (*"Eleventh Report"*). The same is true for other states in which competitive ETCs did not receive high cost support in 2006. *See* Sprint Nextel Comments at 11 (claiming that "[a]doption of the proposed cap will penalize the many states with little or no 2006 CETC distributions ..."). For example, nearly every county in Connecticut, D.C, Delaware, Illinois, Maryland, Massachusetts, New Jersey, Ohio, and Rhode Island has at least four wireless providers, and there are no counties in any of these states without at least two wireless providers. *Eleventh Report* at 97 & 109.

28 CTIA Comments at 6-9; *see also* Alltel Comments at 19.

29 *Eleventh Report*, ¶ 10, n.20.

which provides wireless broadband to more than 150 million Americans across the country, and many other broadband services and technologies.[30]

These same market forces are fueling increased demand for spectrum. The Commission's upcoming 700 MHz spectrum auction is expected to be extremely competitive as providers vie to offer the latest and most advanced wireless broadband services. The interim cap would have no impact on demand for spectrum or the competitive necessity for providers to satisfy the explosive growth in the demand for wireless broadband services.

Moreover, Verizon's proposal to distribute high cost subsidies using reverse auctions for a flat amount of subsidy would encourage broadband deployment without need to add broadband to the fund directly as a supported service.[31] In preparing to bid in auctions for high cost subsidies, carriers will consider all of their services and potential revenue sources that make up their business plans – regardless of whether such services are explicitly supported by the fund. Flat payments to ETCs that win the bid to provide supported services in high cost areas, under Verizon's proposal, would then help those ETCs implement all parts of their business plans. In that way competitive bidding would encourage broadband deployment in a market-driven manner without impacting the size of the fund.

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[30] Verizon Wireless Press Kit (available at http://news.vzw.com/pdf/Verizon_Wireless_Press_Kit.pdf).

[31] *See* Comments of Verizon and Verizon Wireless, WC Docket No. 05-337 (filed May 31, 2007).

IV. THE COMMISSION HAS BROAD DISCRETION TO ADOPT USF CAPS, AND AN INTERIM CAP ON COMPETITIVE ETC SUPPORT WOULD NOT VIOLATE THE ACT.

A. The Commission Has Broad Discretion To Adopt Caps on Universal Service Support.

Various commenters argue that the interim cap on support to competitive ETCs would be unlawful.[32] However, such arguments are impossible to reconcile with *Alenco Communications, Inc. v. FCC,* 201 F.3d 608, 620 (5th Cir. 2000), in which the Fifth Circuit upheld the cap on incumbent LEC high cost loop support and in so doing recognized the Commission's "broad discretion" to establish caps or other "cost controls" to curtail the growth of the USF. In fact, many of the commenters opposing the interim cap cite *Alenco*, but do not bother to mention, let alone seek to distinguish, the central holding of the case.

Alltel asserts that the interim cap on competitive ETC support "would cap CETC funding twice," because, according to Alltel, the limits on growth in incumbent LEC support per line "impose identical limits on the growth of CETC support." Alltel Comments at 10. This assertion is misguided. First, competitive ETCs are not included in the cap on high cost loop support to which incumbent LECs are subject.[33] As the incumbent LEC loses lines while its fixed costs remain roughly the same, the competitive ETC would be entitled to higher support per line for every line that it takes from the incumbent without limitation. Second, because the current system counts every line and handset the same based on the incumbent's LEC's costs, the

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[32] *See, e.g.,* Sprint Nextel Comments at 6-7; Alltel Comments at 2-8; Comments of COMPTEL at 2.

[33] *See Federal-State Joint Board on Universal Service, Multi-Association Group (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Fourteenth Report and Order, Twenty-Second Order on Reconsideration, and Further Notice of Proposed Rulemaking in CC Docket No. 96-45, and Report and Order in CC Docket No. 00-256, 16 FCC Rcd 11244, ¶ 209 (2001) (noting that the indexed cap on high cost loop support "would not check" excessive growth in the fund "because support received by competitive carriers currently is not included within the cap").

support received by wireless ETCs is inflated. Thus, there currently exist no effective limits on competitive ETC support, which readily explains the unchecked growth in the high cost fund.

B. The Interim Cap On Competitive ETC Support Would Not Run Afoul Of The Principle Of Competitive Neutrality.

While various commenters complain that an interim cap on competitive ETC would not be "competitively neutral," such complaints misconstrue the competitive neutrality principle. There is no legal authority for the proposition, and commenters cite none, that competitive neutrality requires that incumbent LECs and competitive ETCs "receive the same amount of support, per line ...." Comments of the Corporation Commission of the State of Kansas, at 3. In fact, the law is the contrary. As the Court of Appeals for the Second Circuit held, competitive neutrality "does not require precise parity of treatment."[34] Thus, the interim cap on competitive ETCs does not violate the competitive neutrality principle merely because it may impact differently the amount of support received by competitive ETCs as compared to incumbent LECs.

The cases cited by Sprint Nextel and Alltel in support of their competitive neutrality theory are readily distinguishable. For example, Sprint Nextel cites *Silver Star Telephone Co., Inc. Petition for Preemption and Declaratory Ruling,* 12 FCC Rcd 15639 (1997), for the proposition that "disparity in the treatment of classes of providers violates the requirement of competitive neutrality ...." Sprint Nextel Comments at 6-7, n.11. However, the "disparity" to

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[34] *TCG New York, Inc. v. City of White Plains*, 305 F.3d 67, 80 (2d Cir. 2002); *see also Qwest Communications International v. FCC*, 398 F.3d 1222, 1233 (10th Cir. 2005) (section 254 "does not impose a requirement of parity with respect to . . . the distribution of funds between and among carriers") ("*Qwest II*"). While the quoted language in *Qwest II* was made in the context of contribution obligations, as CTIA correctly points out, CTIA Comments at 18, n. 45, the court was addressing the "disproportionate and inequitable share of the burden" that a single carrier may be forced to bear in supporting its own high cost consumers – a burden that necessarily takes into account both contributions to and distributions from the high cost fund. *Id.* Thus, the Tenth Circuit's statement that "parity" is not required with respect to "the distribution of funds between and among carriers" is fatal to CTIA's view of competitive neutrality.

which the Commission was referring in that case was a rural incumbent protection provision under state law that allowed incumbent LECs "to determine if and when they will face competition" and saddled "potential new entrants with the ultimate competitive disadvantage – an insurmountable barrier to entry." 12 FCC Rcd at 15658, ¶ 42. *Silver Star Telephone* had nothing to do with universal service or levels of universal service subsidies.

Sprint also cites the Commission's *Western Wireless Order,*[35] which involved a state universal service program that limited eligibility for funding to incumbent LECs. Because denying universal service funding to competitive carriers "may give ILECs a substantial unfair price advantage in competing for customers," the Commission expressed doubt that such a program "could be considered competitively neutral." 15 FCC Rcd. at 16232, ¶ 10. The case did not address, and certainly does not hold that incumbent LECs and competitive ETCs must receive the same levels of universal service support as a matter of competitive neutrality or that the Commission cannot establish interim limits on competitive ETC support as it has done for incumbent LEC support.

In the *South Dakota Declaratory Ruling* cited by Alltel,[36] the Commission addressed a state law requirement that a new entrant provide service throughout a service area before being designated as a competitive ETC. The Commission found that such a requirement was not competitively neutral because it would have "the effect of prohibiting the ability of the new entrant to provide intrastate or interstate telecommunications service, in violation of section 253(a)." 15 FCC Rcd at 15172, ¶ 10. Again, the *South Dakota Declaratory Ruling* does not hold

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[35] Sprint Nextel Comments at 9 (citing *Western Wireless Corp. Petition for Preemption of Statutes and Rules Regarding the Kansas State Universal Service Fund Pursuant to Section 253 of the Communications Act of 1934,* 15 FCC Rcd 16227 (2000) ("*Western Wireless Order*")).

[36] Alltel Comments at 17 (citing *Federal-State Joint Board on Universal Service; Western Wireless Corp. Petition for Preemption of an Order of the South Dakota Public Utilities Commission,* Declaratory Ruling, 15 FCC Rcd. 15168 (2000) ("*South Dakota Declaratory Ruling*")).

that competitive neutrality requires that competitive ETCs and incumbent LECs receive the same level or amounts of universal service support, notwithstanding Alltel's suggestion otherwise.

Commenters' reliance upon the statement in *Alenco* that the universal service program "must treat all market participants equally" is misplaced.[37] The court was merely making clear that both competitive ETCs and incumbent LECs must be eligible for universal service support, since 47 U.S.C. § 214(e)(1) requires that all "eligible telecommunications carriers ... shall be eligible to receive universal service support." The court's "equal treatment" language cannot reasonably be read to suggest that competitive neutrality mandates that incumbent LECs and competitive ETCs receive equal levels of universal service funding.

Although commenters generally agree that the competitive neutrality principle with respect to the distribution of universal service subsidies is intended to ensure that no competitor receives an unfair advantage in the marketplace,[38] they do not seriously dispute that competitive ETCs, particularly wireless carriers, enjoy a significant advantage under the current USF system. By basing support on the incumbent LEC's costs and by allowing the recovery of support for multiple handsets to a customer, wireless ETCs are able to recover subsidies at levels well in excess of their costs. Moreover, much of the support to incumbent LECs – including high cost loop and safety valve support – is already capped, whereas support to competitive ETCs is not. The competitive playing field is currently tilted in favor of competitive ETCs, and the interim

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[37] CTIA Comments at 11 & 15; Sprint Nextel Comments at 6-7.

[38] *Federal-State Joint Board on Universal Service*, Report and Order, 12 FCC Rcd 8776, ¶ 48 (1997), as corrected by *Federal-State Joint Board on Universal Service,* Erratum, CC Docket No. 96-45, D.A. No. 97-157 (June 4, 1997), *aff'd in part, rev'd in part, remanded in part sub nom. Texas Office of Public Utility Counsel v. FCC*, 183 F.3d 393 (5th Cir. 1999) ("*First Report and Order*") (principle of competitive neutrality would "ensure that . . . no entity receives an unfair competitive advantage that may skew the marketplace or inhibit competition ...").

cap certainly would not give incumbent LECs' wireline service a competitive advantage, as some commenters claim.[39]

Indeed, wireline service is and will continue to be under significant competitive pressures that would be unaffected by the interim cap. Between June 2000 and July 2006, incumbent LECs lost more than 37 million switched access lines.[40] This line loss is likely to continue as new providers enter the telecommunications market offering a wide array of services to consumers, often without the benefit of any universal service subsidies. For example, cable companies are expected to offer telephony services (IP-based or circuit-switched) to some 95 percent of households by the end of this year, up from 32 percent at the end of 2004 and 76 percent at the end of 2006, and are projected to offer service to 99 percent of U.S. households by the end of 2008.[41] Collectively, cable companies provided service to more than 8.7 million voice lines as of the end of 2006, and are expected to serve more than 13 million voice lines by the end of 2007, and more than 19 million lines by year-end 2008 without any high-cost support.[42]

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[39] CTIA Comments at 20 ("A cap on support that affected only competitive carriers would blithely sacrifice [] competition for rural consumers by providing an unfair advantage to wireline incumbents"); Sprint Nextel Comments at 10-11 ("making ILEC-provided services relatively less expensive than CETC service (by an amount equal to the high-cost support provided to the ILEC that is not available to their competitors) provides an artificial incentive and incorrect economic signal to consumers to select the ILEC over the CETC, even if the ILEC is the less efficient competitor ...") (citations omitted); Alltel Comments at 20 (the interim cap "would make it difficult or impossible for wireless carriers to engage in head-to-head competition with subsidized ILECs ...").

[40] *See* FCC, Industry Analysis & Technical Division, Wireline Competition Bureau, *Local Telephone Competition: Status as of June 30, 2006,* at Table 1 (Jan. 2007) (available at http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-270133A1.pdf) (*"Local Competition Report"*).

[41] Craig Moffett, et al., Bernstein Research, *VoIP: The End of the Beginning* at Exhibit 3 (Apr. 3, 2007).

[42] *Id.* at Exhibit 8.

Wireless carriers also are competing vigorously, serving approximately 217 million of the 389 million voice lines in this country as of June 2006.[43] According to CTIA, "There are now 26 percent more wireless handsets in service than wireline connections, and about 12.8 percent of households have abandoned wireline service altogether and subscribe only to wireless service."[44]

The interim cap on competitive ETC would have no effect on these market trends. There is simply no reason to believe that consumers will turn away from cable telephony or wireless offerings and flock back to wireline service from the incumbent LEC merely because competitive ETC support has been capped on an interim basis, particularly when cable operators and two of the four largest wireless operators currently receive virtually no high cost support.

Various commenters take issue with the Joint Board's analysis of the regulatory differences between competitive ETCs and incumbent LECs that, according to the Joint Board, warrant a different approach to universal service support to these groups of carriers.[45] But some of these same commenters concede that incumbent LECs and competitive ETCs historically have been treated differently for universal service purposes, primarily because of these regulatory differences. Alltel Comments at 16.

Some commenters also question why these regulatory differences, particularly with respect to rate regulation, "justify" a different approach to universal service support.[46] This question ignores the limits that exist on an incumbent LEC's ability to recover its costs from local rates – limitations that do not apply to competitive ETCs. While incumbent LECs have been granted greater pricing flexibility at the state level in recent years, many of their rates,

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43 *Local Competition Report,* at Tables 1 & 14..

44 CTIA Comments at 10.

45 Alltel Comments at 9-15; CTIA Comments at 12-15.

46 Alltel Comments at 13; CTIA Comments at 13.

particularly for basic telecommunications services, remain heavily regulated. Thus, while competitive ETCs, which are not subject to any rate regulation, can recover their costs directly from their customers, the same is not true for incumbent LECs, whose prices for certain regulated services continue to reflect social pricing policies of a bygone era.

C. The Interim Cap On Competitive ETC Support Would Not Violate The Other Statutory Principles In Section 254 Upon Which The Commission Must Base Its USF Policies.

Claims that an interim cap on competitive ETC support would violate the other statutory principles in section 254 that must guide the Commission's USF policies are without merit.[47] For example, although rates in rural and other high-cost areas should be "reasonably comparable" to those in urban areas, the interim cap would not run afoul of this principle, particularly for wireless ETCs. Wireless carriers offer nationwide pricing plans, which are available to customers in both rural and urban areas.[48] There is no reason to believe that an interim cap on competitive ETC support would change the structure or availability of these national pricing plans, particularly given the competitive trends in the wireless market.[49]

With respect to the argument that the interim cap would cause support to competitive ETCs to fall "below the level deemed 'sufficient' under the otherwise applicable distribution mechanisms," CTIA Comments at 22, CTIA ignores that the "sufficiency" principle "requires sufficient funding of *customers*, not *providers*." *Alenco,* 201 F.3d at 620. As the *Alenco* court

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[47] Sprint Nextel Comments at 12-15; CTIA Comments at 20-23.

[48] For example, Alltel offers its National Freedom ® plan, which gives customers in all areas within its coverage area the ability to make calls to major U.S. cities and surrounding metropolitan areas in the Alltel national network without additional roaming or long-distance charges. *See* http://www.alltel.com/personal/wireless/plans/plans_individual.html. The rates for this plan vary by the number of minutes the customer purchases under the plan, not the customer's location in urban or rural areas.

[49] *See Eleventh Report,* ¶ 88 (noting the lack of evidence that carriers in rural areas can "raise prices above competitive levels" or "alter other terms and conditions of service to the detriment of rural consumers," particularly when "rural carriers are rolling out competitive national pricing plans with 'surprisingly low per-minute pricing'") (citations omitted).

made clear, "So long as there is sufficient and competitively-neutral funding to enable all customers to receive basic telecommunications services, the FCC has satisfied the Act and is not further required to ensure sufficient funding of every local telephone provider as well." *Id.* Here, by capping competitive ETC support on an interim basis, the Commission would be protecting the affordability of telecommunications services consistent with the Act, regardless of its impact on individual competitive ETCs.

D. The Commission Has Greater Discretion In Imposing The Interim Cap On Competitive ETC Because It Is Transitional In Nature.

The law is clear that the Commission is afforded considerably greater deference in adopting interim universal service requirements that "are merely transitional,"[50] as is the case with the interim cap on competitive ETC support, the purpose of which is to facilitate the transition to a new universal service system. As the Joint Board noted, the cap on competitive ETC support it is recommending "should be an interim measure that is used to stem the growing crisis in high-cost support growth while the Commission and Joint Board consider further reform." *Recommended Decision* ¶ 8. Accordingly, the Commission has more latitude in imposing the interim cap, notwithstanding CTIA's argument to the contrary. CTIA Comments at 23.

CTIA argues that earlier "efforts to enact permanent reform have stalled," causing interim solutions to become "'permanent' regulatory frameworks." *Id.* However, the solution to this problem is not to abandon the interim cap proposed by the Joint Board. Rather, it is for the

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[50] *Alenco*, 201 F.3d at 616; *see also Texas Office of Public Utilities Counsel v. FCC*, 183 F.3d 393, 437 (5th Cir. 1999) ("Where the statutory language does not explicitly command otherwise, we defer to the agency's reasonable judgment about what will constitute 'sufficient' support during the transition period from one universal service system to another"); *MCI Telecomm. Corp. v. FCC*, 750 F.2d 135, 140 (D.C. Cir. 1984) (noting "substantial deference by courts is accorded to an agency when the issue concerns interim relief").

Joint Board, the Commission, and the industry to work diligently to implement comprehensive reform as expeditiously as possible.

V. CONCLUSION.

For the foregoing reasons, the Commission should impose an interim cap on the amount of high cost support that competitive ETCs may receive until the Commission puts in place comprehensive universal service reform.

Respectfully submitted,

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