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Chairman Kevin J. Martin
Commissioner Michael J. Copps
Commissioner Jonathan S. Adelstein
Commissioner Deborah Taylor Tate
Commissioner Robert M. McDowell
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: *High-Cost Universal Service Support*, WC Docket No. 05-337; *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45.

Dear Chairman Martin and Commissioners:

Nearly everyone recognizes that the high-cost mechanisms in the federal universal service fund (USF) badly need reform. The current system of high-cost support sends too much support to some areas and far too little support to other areas, chiefly as a result of study-area averaging. The time has come to focus high-cost support where it is needed. The Commission should provide explicit support for all areas where a free market would not provide such service at affordable rates comparable to those available to consumers in urban areas. It should end support in areas where a free market would produce such affordable service without support. The Commission should also take this opportunity to promote broadband deployment in areas where the underlying telecommunications networks do not receive sufficient support today. Those are the areas where broadband deployment is lagging.

Today, Embarq offers a proposal to solve the problems surrounding the high-cost USF program: the Broadband and Carrier-of-Last-Resort Support (BCS) solution. Its basic principle is that price-cap study areas should be converted to more targeted USF support on a wire center basis, because implicit support (through study area averaging) does not work for consumers in those areas. The BCS solution would:

(1) stimulate substantial new broadband deployment;

(2) stabilize support for carrier of last resort (CoLR) universal service;

(3) make substantial progress on the recommendations of the Joint Board and this Commission in the three NPRMs issued last fall;

(4) comply with the remand by the United States Court of Appeals for the 10th Circuit;

(5) create a more-stable foundation for further reform of USF; and

(6) do all of this without increasing overall USF support levels.

The problem with today's high cost USF program.

As described in detail in the attached Term Sheet and white paper, the BCS solution would address the fundamental problems with federal high-cost support today. The central problem with the current regime is its use of average cost calculations. It assumes that a CoLR will be required by regulation to offer averaged rates and, consequently, it presumes that higher returns in low-cost areas will offset negative returns in high-cost areas. Competition has rendered this assumption utterly obsolete. Competitors, lacking the obligation to serve high-cost areas, charge lower rates and win customers in low-cost areas. That reduces the CoLR's total revenues and eliminates the higher returns that were implicitly subsidizing the below-cost service in high-cost areas. At the same time, in today's regime, even in areas where cost averaging does not provide adequate support for CoLR service, competitors are being provided universal service support, regardless of whether they need support -- or whether that actually even serve the truly high-cost parts of the supported areas. The current regime's flawed assumptions mean too much support is provided in some areas, too little is provided in others, and consumers are harmed in both instances.

It was to avoid these types of problems that the Telecommunications Act mandated that universal service subsidies be explicit. Indeed, the Commission has acknowledged that implicit subsidies cannot survive the increasing competition that is now firmly established in cities and even the small towns throughout the country. Accordingly, high-cost support must be more narrowly targeted to serve the truly high-cost locations within price-cap study areas if the Commission to fulfill the directive of section 254 to make universal service support explicit, predictable, and sufficient. In doing so, the Commission can and should also promote broadband deployment, as directed in section 706 of the Act.

The BCS solution would make significant progress in fundamental USF reform. Plainly, the problems with the current USF distribution—directing too much support to some places and too little support to others—are most acute in, if not largely confined to, areas served by the incumbent local exchange carriers (ILECs) regulated in the federal jurisdiction under incentive or price cap regulation. Unlike customers served by rate-of-return carriers, rural customers served by price-cap carriers face growing threat of service degradation, because price-cap carriers are not permitted to raise end-user or access rates to offset rapidly eroding CoLR support. Moreover, what explicit USF support is available is strictly capped in price-cap study areas. Finally, because support for the continuing CoLR obligation continues to erode with the loss of access lines in low-cost areas, price-cap ILECs will less and less able to invest in and maintain their networks. Those networks are the foundation for service in rural areas, relied upon not merely by wireline voice consumers but also by all broadband and wireless providers. Consequently, the growing impact of the flaws of the existing federal high-cost USF are undermining broadband deployment and threatening the future of service to rural America.

The BCS Mechanism.

Embarq proposes that the Commission replace the current Non-Rural High-Cost Model Support mechanism, and current High-Cost Loop Support in price cap study areas, with a new mechanism (the BCS) based on wire centers. The BCS mechanism targets supports to wire centers having household densities below a national benchmark calculated to distribute support to those areas most in need. Once set, the BCS would be capped at its initial level. The cap would increase only by express Commission action, such as to facilitate any conversion of rate-of-return study areas to price-cap regulation. In such cases, as shown by several ILEC conversions over the past year, any increase in the BSC would be offset by a decrease in other support mechanisms.

The BCS requires no additional USF funding.

Creating the BCS would require no new USF funding. Funding for the new BCS would come from adding access replacement funds (IAS and ICLS) received today by wireless carriers to the amount in the current Non-Rural High-Cost Support mechanism and the amount of High-Cost Loop support distributed in price-cap study areas. This redistribution is in the public interest. It makes far better use of the funding, as the Commission recognized in tentatively concluding that wireless competitive eligible telecommunications carriers (CETCs) should not receive access replacement support.

The BCS proposal, however, actually does not prevent wireless ETCs, in the aggregate, from continuing to receive most of the access replacement support they receive, even though the Commission tentatively concluded in the Identical Support NPRM that it should end such support altogether. Instead, under the BCS, competitive ETCs would be eligible for support under the new mechanism and, in the aggregate, they may receive most of the support they receive today. Moreover, wireless ETCs will continue to receive the support they receive today through the rural high-cost loop support mechanism.

Promoting rural broadband deployment and satisfying the 10th Circuit Remand

To promote broadband deployment and investment in rural areas, BCS support recipients in price-cap areas would be required to make three commitments:

- They would commit to offer broadband of at least 1.5 Mbps downstream to at least 85% of the customers in each wire center receiving support.
- They would commit to provide supported local service at rates that meet the statutory requirements of affordability and comparability, which would be established by offering basic service in the wire center at a rate that falls on the range identified by the list of urban rates in the FCC's Reference Book of Rates, Price Indices, and Household Expenditures, Table 1.3.
- They would commit to build-out and serve the entire wire center using only their own facilities within five years.

Rural rate-of-return study areas would be unaffected by the BCS solution, apart from remaining subject to the Commission's tentative conclusion that wireless CETCs should not receive ICLS payments. All ETCs would continue to receive loop support in rate-of-return study areas as they do today and, should the study area convert to price cap regulation, they would all be eligible to receive funding through the BCS (which would be increased to accommodate the transition). In all other respects, USF support in rural rate-of-return areas would continue as it does today, even as the reforms in price-cap study areas would put all high-cost areas on more equal footing.

Administrative simplicity.

The Commission can implement the BCS relatively simply and quickly by using current information and methodologies. Support would be directed to wire centers. This, in practice, provides a competitively neutral distribution method in low-density areas, as all networks are built out around towns and use the same backbone network to connect to the rest of the country.

Under the BCS, the capped total amount of support would be distributed among the supported wire centers on the basis of relative costs as measured by household densities. To facilitate implementation and minimize legal concerns that would likely accompany any new and un-reviewed density-allocation metric, Embarq suggests the Commission use a proxy for a density allocator. The logical choice is the loop cost output in the current iteration of the Hybrid Cost Proxy Model, which the Commission already uses today. The primary factor for relative loop costs in the model is line density, which provides a reasonable estimate of household density. Instead of estimating total cost of local service, the HCPM would be used one last time for the sole purpose to identify estimated loop costs. Future assessments could be done on a five year cycle using a superior model or some other mechanism.

Appropriately, support levels would not vary with changes in the number of lines served by the CoLR. That is consistent with the economics of the carrier-of-last-resort obligation. A CoLR's costs of providing service do not diminish when lines are lost, and line loss is concentrated in the relatively low-cost areas targeted by competitors. Ensuring consistent support would remove the perverse effect of the current system, which reduces support for high-cost customers when low-cost customers choose switch take their business from the CoLR to a competitor. Once support levels are set, each wire center would receive the same support for five years. Support levels and corresponding obligations would be revisited thereafter at five-year intervals.

Targeted support for CETCs.

The BCS would offer support to a CETC in each wire center. No more than one CETC would receive support in any given wire center, however. To receive support, a CETC must meet the same broadband, rate comparability, and build-out commitments required of all supported ETCs. Where only one CETC makes the commitments in a wire center, it would be designated under the BCS as the supported CETC for that wire center. The BCS support for the wire center then would be divided equally between the ILEC and the CETC. Where more than one CETC seeks to be designated in a wire center, the designating authority (either the state commission or the Commission, as appropriate) would select a single CETC, for example through an RFP review process or auction. This approach allows wireless carriers to have the same access to high-cost support, on the same conditions, but avoids directing high-cost support to multiple CETCs in the same areas.

Conclusion.

The BCS would significantly promote new broadband deployment in rural America. It would stabilize support for CoLR universal service, which is otherwise at increasing risk. It would make real progress on the recommendations of the Joint Board and this Commission in the three NPRMs issued last year. It would fulfill the Commission's obligations following the

10th Circuit's remand. It would provide a secure foundation for further USF reform. And it would accomplish all of these important goals this without increasing the overall costs of USF support. Embarq encourages the Commission to consider the BCS solution carefully and to recognize its many public interest benefits. Embarq looks forward to discussing this proposal with the Commission.

Pursuant to Section 1.1206(b) of the Commission's rules, a copy of this submission is being filed in each of the above-referenced dockets.

Sincerely,

David C Bartlett

cc: Joint Board Commissioners and staff
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