

**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)	
)	
Notice of Inquiry Seeking to Refresh)	
The Record Regarding the Issues Raised)	
By the Tenth Circuit in the Qwest II Decision)	

COMMENTS OF AT&T INC.

Cathy Carpino
Christopher Heimann
Gary L. Phillips
Paul K. Mancini

AT&T Services, Inc.
1120 20th Street, N.W.
Suite 1000
Washington, D.C. 20036

(202) 457-2044 - telephone
(202) 457-3046 - facsimile

Its Attorneys

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I. INTRODUCTION AND SUMMARY

In the Telecommunications Act of 1996 (1996 Act), Congress directed the Commission, working in cooperation with the states, to develop and implement universal service support mechanisms that will preserve and advance universal service objectives in a competitive environment. In particular, section 254(b) of the 1996 Act¹ directs the Commission to implement mechanisms that will ensure, *inter alia*, that consumers across the nation, regardless of where they live, have access to state-of-the-art telecommunications and information services at rates that are affordable and reasonably comparable to those charged in urban areas. It further requires that all providers contribute equitably to the preservation and advancement of universal service objectives, and that federal and state universal service support mechanisms provide support that is specific, predictable and sufficient to preserve and advance those objectives.

¹ 47 U.S.C. § 254(b).

Twice, the Commission has implemented a mechanism for so-called non-rural carriers and, twice, the Tenth Circuit has sent the Commission back to the drawing board for failing to adopt a mechanism that appropriately accounts for and balances all of Congress's objectives in section 254(b).² At every stage, AT&T has called upon the Commission to undertake fundamental reform of the nation's universal service support mechanisms to preserve and advance those objectives in today's increasingly competitive and rapidly evolving communications marketplace. Now, thirteen years later, we face a communications landscape that is vastly different from the one confronting Congress and the Commission in 1996. Indeed, changes in the ways that people connect to communications networks, the capabilities of those networks, and the new and evolving business models associated with those networks threaten to make irrelevant whatever action the Commission may take in this proceeding if it acts without regard to the profound implications of these unfolding changes. If ever there was a time for the Commission to return to principles, and to put aside policies and rules inconsistent with those principles, it is now.

Universal service policy as it exists today at both the federal and state levels is centered on a business model that is dying. The plain old telephone service (POTS) model, by which local exchange carriers provide "basic local exchange service" combined with "interexchange access" to long distance services, will soon go the way of the slide rule – an earlier casualty of digital technology. In today's communications marketplace, the only thing falling faster than subscribership to basic local exchange service is the volume of switched access minutes carried on the networks of incumbent local exchange carriers (ILECs). In these circumstances, the

² See *Qwest Corp. v. FCC*, 258 F.3d 1191 (10th Cir. 2003) (*Qwest I*); *Qwest Communications Int'l, Inc. v. FCC*, 398 F.3d 1222 (10th Cir. 2005) (*Qwest II*).

Commission could not hope to prop up the POTS model for long, even if it wanted to.³ Instead, it must be forward looking, and initiate comprehensive and fundamental reform of its universal service policies and mechanisms to promote and advance universal service objectives for the 21st Century. That will require the Commission finally to confront the rapidly eroding implicit subsidies in the disappearing service called switched access, and to establish explicit funding mechanisms to ensure that its universal service objectives are met.

As the Commission considers the issues raised in this proceeding, it will at the same time be formulating the national broadband plan called for by Congress in the American Recovery and Reinvestment Act of 2009. Indeed the Commission will deliver its plan to Congress by February 17, 2010 – a mere eight weeks before the date by which it has committed to adopt an order in this proceeding. As the goal of the national broadband plan can be nothing less than bringing broadband to every American within the near future, the Commission will inevitably confront the need for fundamental universal service reform as part of that plan. The Commission must coordinate its actions in this proceeding with the development of the national broadband plan. A lack of coordination would not only result in wasted resources but, more importantly, in a squandered opportunity.

In these comments, AT&T sets out a vision, based on the guiding principles enunciated by Congress in section 254(b), for ensuring the continued relevance of the Commission's universal service program. Ultimately, that vision requires the transition of all high-cost funding from the legacy POTS business model to support for business models that are viable in the

³ An opinion piece in today's New York Times shines a spotlight on the challenges confronting ILECs and questions whether the phone industry will be the next in line for a government bailout. *See* Saul Hansell, "Will the Phone Industry Need a Bailout, Too?" New York Times (May 8, 2008) (noting that ILECs are losing around 10 % of their access lines each year though their costs of maintaining facilities is not falling nearly as quickly) (available at: <http://bits.blogs.nytimes.com/2009/05/08/will-the-phone-industry-need-a-bailout-too/>).

hyper-connected digital world in which growing numbers of us live, thereby not only preserving but also *advancing* universal service as required by Congress and the Tenth Circuit.⁴ As part of this transition, the Commission must move toward a support mechanism that is narrowly targeted to rural and other high-cost areas, and that prepares for the end of the POTS model.

II. DISCUSSION

In both its *Qwest I* and *Qwest II* decisions, the Tenth Circuit identified significant deficiencies with the Commission's non-rural high-cost support mechanism. In particular, the Tenth Circuit faulted the Commission for failing to define key terms in section 254(b), to consider and appropriately balance the full range of congressional objectives set forth in that section, and to develop a complete plan for preserving and advancing universal service objectives in all high cost areas without regard to the size or classification of the carriers serving those areas.

Our comments respond to the deficiencies identified by the Tenth Circuit with a proposal, described below, that is grounded in all of the relevant principles of section 254(b) and, consistent with those principles, seeks to meet the needs of consumers in the 21st Century, rather than continuing to perpetuate a rapidly obsolescing business model. In its recent *Tenth Circuit NOI*, the Commission sought comment on several proposals submitted at earlier stages of this proceeding.⁵ These proposals, which aim largely to support POTS networks and services, might

⁴ *Qwest II*, 398 F.3d at 1235-37.

⁵ *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service*, WC Docket No. 05-337 and CC Docket No. 96-45, Notice of Inquiry, FCC 09-28 (rel. April 8, 2009) (*Tenth Circuit NOI*).

have made sense if they had been implemented a decade ago.⁶ But, the breakneck speed at which technology has transformed communications has rendered almost all of these proposals obsolete. Supporting POTS simply cannot be the Commission's long-term universal service goal. If the Commission adopts an order next year that interprets section 254(b)'s mandate to preserve and advance universal service as merely requiring the Commission to narrow any gap in POTS rates, the Commission will fail to fulfill not only its mandate under section 254 (and thus congressional objectives), but also the broadband deployment objectives of the new Administration. It also will condemn the Commission's universal service support mechanism for so-called non-rural carriers to rejection for yet a third time at the Tenth Circuit. The Commission thus should not just tinker with the existing high-cost model mechanism, but rather adopt a "complete plan for supporting universal service"⁷ in today's rapidly evolving communications marketplace.

In previous Commission filings, AT&T has proposed that the Commission establish two broadband funds (one for fixed infrastructure and a second for mobile wireless infrastructure) that would provide targeted, project-based support to encourage deployment of broadband facilities and services to unserved areas.⁸ AT&T urges the Commission to adopt those proposals, and ultimately transition all high-cost universal service funding mechanisms to support broadband. Recognizing that this transition will not be made overnight, the Commission should

⁶ However, Qwest's blatantly discriminatory proposal to deny support to two non-rural carriers (AT&T and Verizon) never would have survived judicial scrutiny even a decade ago. AT&T will discuss this proposal and the three others in its reply comments.

⁷ *Qwest I*, 258 F.3d at 1205.

⁸ AT&T USF NPRMs Comments, WC Docket No. 05-337 and CC Docket No. 96-45 (filed April 17, 2008) (AT&T April 2008 Proposal).

immediately reform its legacy high-cost model support mechanism for non-rural ILECs.⁹ Specifically, the Commission should retarget support to those “rural” and other “high cost” areas where support is needed to meet universal service objectives using more precise and legally sustainable definitions of key statutory terms. The Commission also should eliminate statewide averaging, which assumes continued reliance on unsustainable and rapidly declining implicit subsidies, and more narrowly target support based on the demographic and other characteristics (such as topography) of the areas served, rather than on the classification of the carriers serving those areas. To that end, the Commission should begin the process of consolidating the high-cost support mechanisms for rural and purportedly non-rural carriers.¹⁰

As discussed herein, after identifying areas that are eligible for funding under the legacy/transitional universal service support mechanisms, the Commission should apply benchmarks to determine whether and how much support carriers providing service in those areas should receive to ensure the reasonable comparability of their rates and sufficiency of support. This explicit federal support should not be used to perpetuate implicit carrier-to-carrier subsidies contained in high intrastate access charges, which are ill-suited to preserving and advancing universal service. AT&T therefore recommends that the Commission condition receipt of high-cost support on reductions in intrastate switched access charges.¹¹ The Commission should make available support where needed to reduce end-user rates in rural and

⁹ Competitive eligible telecommunications carrier (ETC) funding will be subject to its own transition discussed below.

¹⁰ See, e.g., *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Recommended Decision, 22 FCC Rcd 20477, ¶¶ 19-23 (2007) (*Recommended Decision*).

¹¹ Further intercarrier compensation reform may require removal of additional implicit support from interstate and intrastate switched access charges.

high-cost areas to a level reasonably comparable to the level in urban areas. The Commission should also ensure that sufficient support is available to maintain reasonably comparable rates in rural and high-cost areas. Finally, the Commission should consider making additional support available where needed to remove implicit subsidies from switched access charges while maintaining reasonably comparable rates.

A. The Commission Must Reconsider its Application of the Universal Service Principles in Section 254(b).

As the Commission recognized in the *Tenth Circuit NOI*, the court in *Qwest II* faulted the Commission for adopting a rural and urban rate comparability benchmark that treated rates as “reasonably comparable” if they were two standard deviations above the national average urban rate, thus guaranteeing that “significant variance between rural and urban rates [would] continue unabated.”¹² The court concluded that, on remand, “the FCC must define the term ‘reasonably comparable’ in a manner that comports with its concurrent duties to preserve and advance universal service.”¹³ The court also determined that the Commission had failed to “articulate a definition of ‘sufficient’ that appropriately considers the range of principles identified in the text of the statute.”¹⁴ And, in *Qwest I*, the court directed the Commission to present a “complete plan for supporting universal service.”¹⁵ But, eight years later, the Commission has yet to do so.

¹² *Qwest II*, 398 F.3d at 1236.

¹³ *Id.* at 1237.

¹⁴ *Id.* at 1234.

¹⁵ *Qwest I*, 258 F.3d at 1205. In its *Tenth Circuit Remand Order*, the Commission did list the proceedings that it had completed to date as well as the numerous proceedings that were pending in 2003. Unfortunately, five and a half years later, the Commission has yet to act on those critical pending proceedings. See *Federal-State Joint Board on Universal Service*, CC Docket No. 94-45, Order on Remand, Further Notice of Proposed Rulemaking, and Memorandum Opinion and Order, 18 FCC Rcd

Thus far, the Commission has been unable to defend its high-cost model mechanism because it was not generated by any deliberative application of the section 254(b) principles. Rather, it was the product of a results-driven process that sought to control for the size of the federal universal service fund without regard to the other objectives of section 254(b). It thus continued to rely on unsustainable implicit subsidies to achieve federal universal service objectives for the majority of consumers living in rural and other high-cost areas served by “non-rural” carriers. In order for the third time to be the charm, and finally pass muster, the Commission must return to the basics and appropriately balance all of the principles in section 254(b). AT&T proposes herein a high-cost action plan that, if adopted, would appropriately balance the full range of congressional objectives and universal service principles enunciated in section 254(b), as well as provide a complete plan for meeting those objectives and principles in the 21st Century. In this section, we discuss all of the relevant principles and how the Commission should apply them going forward.

Affordability. “Quality services should be available at just, reasonable, and affordable rates.” 47 U.S.C. § 254(b)(1). The best evidence of whether a rate is affordable is that consumers are willing and able to pay that rate in order to obtain a particular good or service.¹⁶

22559, ¶¶ 106-07 (2003) (*Tenth Circuit Remand Order*) (listing intercarrier compensation reform, review of the rural carrier mechanisms, review of IAS and ICLS, contribution methodology reform). Of the list of open items, the Commission has acted on just one of them: capping competitive ETC support, though even that action was simply a band-aid pending further additional Commission action. *See High-Cost Universal Service Support, Federal-State Joint Board on Universal Service*, WC Docket No. 05-337, CC Docket No. 96-45, Order, 23 FCC Rcd 8834 (2008) (*Interim Cap Order*).

¹⁶ Of course, such rates also must be just and reasonable. As the Commission has long recognized, in competitive markets, such as the burgeoning market for broadband services, market forces will ensure prices are just and reasonable. AT&T recognizes that some parties might debate whether the market, and thus the prices, for other services (such as for basic local exchange services) are competitive. The Commission need not resolve those debates here. Rather, where prices for particular services have been de-regulated, the Commission can presume that the markets for those services are competitive, and thus that the prices for such services are just and reasonable. Likewise, the Commission can presume that the

Thus, to determine whether rates for a particular service or services (such as those encompassed within the universal service definition) are affordable, the Commission should consider evidence that consumers are subscribing to a service at high levels of penetration and the range of rates at which they are obtaining such a service. Any rate falling within the resulting range of rates should be deemed to be an “affordable” rate.¹⁷

The Commission already has data regarding the range of rates for wireline voice services and rates for wireless voice services, both of which have achieved very high levels of penetration among consumers across the country.¹⁸ For broadband services, which lack the ubiquitously high penetration rates of wireline and wireless voice services, the Commission should review the range of rates that consumers pay in areas where the subscribership rate is high. Broadband pricing data is available to the Commission from numerous market analysts and other firms that specialize in collecting such data, both at the macro level to track broad industry-wide pricing trends and at the micro level to capture company-specific, service-specific and speed-specific

rates for such services are just and reasonable to the extent they remain subject to regulation (which, of course, is designed to ensure that rates are just and reasonable) either at the state or federal level.

¹⁷ AT&T recognizes that not all consumers may be able to afford to purchase a service at a particular rate. But that does not mean that the rate is not “affordable.” To the extent that a consumer is unable to purchase a supported service based on his or her individual economic circumstances, the Commission should ensure that such individuals receive appropriate support to purchase such services through its low-income support mechanism.

¹⁸ See *2008 Reference Book of Rates, Price Indices, and Household Expenditures for Telephone Service*, Tables 1.3, 1.4; *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993, Annual Report & Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services*, WT Docket No. 08-27, 13th Report, DA 09-54, ¶¶ 111-18 (rel. Jan. 16, 2009); CTIA Semi-Annual Wireless Industry Survey (available at: http://files.ctia.org/pdf/CTIA_Survey_Year-End_2008_Graphics.pdf). See also Blumberg, Luke, *Wireless substitution: Early release of estimates from the National Health Interview Survey, July-December 2008* (May 2009) (available at: <http://www.cdc.gov/nchs/nhis.htm>) (survey finding that only 1.9% of households had no telephone service).

pricing information at the state and/or local level.¹⁹ In addition, for more than a decade, the Commission has published data related to the affordability of telephone service that it collects from the Bureau of Labor Statistics, the Bureau of Economic Analysis and a data vendor known as TNS Telecoms.²⁰ These data enable the Commission to analyze how much Americans spend on telephone service each year, both in terms of dollars spent per household and as a percentage of total household expenditures. The Commission could work with these and/or other sources (e.g., Census Bureau) to obtain similar data on broadband expenditures.

Access to Advanced Services. “Access to advanced telecommunications and information services should be provided in all regions of the Nation.” 47 U.S.C. § 254(b)(2). Today’s high-cost support mechanisms, which are predicated on supporting the legacy POTS network and business model, do almost nothing to satisfy this principle. Consequently, if the Commission were to simply tinker with, rather than overhaul, the high-cost model mechanism, it could not even pay lip service to section 254(b)(2)’s mandate when it responds to the *Qwest II* court next year. To survive judicial review this time, the Commission must explain to the Tenth Circuit how the modified high-cost mechanisms are designed to ensure that access to advanced telecommunications and information services is provided in all regions of the country by supporting investment in broadband network facilities.

Reasonable Comparability. “Consumers in all regions of the Nation, including low-income consumers and those in rural, insular, and high cost areas, should have access to telecommunications and information services, including interexchange services and advanced telecommunications and information services, that are reasonably comparable to those services

¹⁹ See, e.g., AT&T Form 477 Comments, WC 07-38, at 10 & n.28 (filed Aug. 1, 2008).

²⁰ See, e.g., *2008 Trends in Telephone Service*, 3-1 to 3-6.

provided in urban areas and that are available at rates that are reasonably comparable to rates charged for similar services in urban areas.” 47 U.S.C. § 254(b)(3). In *Qwest II*, the Tenth Circuit rejected the Commission’s conclusion that Congress intended, through this principle, to merely preserve the existing variation in rates for supported services across the nation. The court observed that section 254(b) requires the Commission to adopt policies that not only preserve but also advance congressional objectives, including the goal of reasonable comparability of rates across regions. The court observed that Congress’s directive that the Commission *advance* universal service incorporates “a concept that certainly could include a narrowing of the existing gap between urban and rural rates.”²¹ AT&T notes, however, that, by using the term “reasonably comparable,” Congress plainly envisioned that there may be some variance in rates for supported services between urban and rural areas. Had Congress intended the Commission (together with the states) to design a high-cost mechanism(s) to ensure that rates for supported services in rural areas would be no higher than in urban areas, it would have said so, as it did in section 254(g), which requires providers of interexchange telecommunications services to charge rates in rural and high-cost areas that are “no higher” than the rates that such providers charge in urban areas.²² The Commission thus has flexibility to appropriately balance the full range, and potentially competing, goals of section 254(b) in determining whether rates for supported services are reasonably comparable in urban and rural areas.

The reasonable comparability principle in section 254(b)(3) is not limited only to rates. Rather, it also requires that low-income consumers and those in rural and other high-cost areas should have access to telecommunications and information services (including advanced

²¹ *Qwest II*, 398 F.3d at 1236.

²² 47 U.S.C. § 254(g).

services) that are reasonably comparable to those services offered in urban areas. Thus, to fully comply with this principle, the Commission cannot base its universal service policies and mechanisms on supporting only the existing supported services. Rather, those policies and mechanisms should be designed to ensure that no region of the country is left behind by the revolution in telecommunications and information services taking place. Accordingly, as AT&T previously has advocated, the Commission should ultimately transition all of its legacy high-cost support mechanisms to broadband-focused mechanisms that target high-cost support to areas where service meeting the definition of “advanced telecommunications capability”²³ are not yet available.

AT&T recognizes that the Tenth Circuit did not specifically identify the Commission’s failure to consider whether consumers in all regions of the country have access to comparable telecommunications and information services (including advanced services) in rejecting the Commission’s prior high-cost model support mechanism in *Qwest I* and *Qwest II*. However, in light of marketplace developments, including the broad deployment of advanced broadband capabilities and subscription to broadband services by consumers in urban areas in the intervening years, the Commission must demonstrate in its promised 2010 order how its universal service support policies and mechanisms will ensure that consumers in rural areas have access to telecommunications and information services that are reasonably comparable to those services provided in urban areas. To date, the Commission has given short shrift to this aspect of section 254(b)(3) by focusing entirely on the reasonable comparability of *rates* (and POTS rates at that). It can do so no longer.

²³ 47 U.S.C. § 706(c)(1).

Equitable and Nondiscriminatory Contributions. “All providers of telecommunications services should make an equitable and nondiscriminatory contribution to the preservation and advancement of universal service.” 47 U.S.C. § 254(b)(4). As AT&T has explained previously, the existing high-cost support mechanisms continue to rely heavily on implicit subsidies in state rates (primarily in intrastate access rates). As a consequence, some carriers – principally those so-called “non-rural” carriers that receive support (if any) for providing service to the majority of customers residing in rural and other high-cost areas based on their statewide average costs – and, more importantly, their end user customers bear a disproportionate share of the cost of supporting high-cost consumers.²⁴ Today’s high-cost support mechanisms thus cannot be said to ensure that all carriers’ contributions to the preservation and advancement of universal service are equitable. The Commission must ensure that its universal service support mechanisms and policies do more to encourage states to eliminate such implicit subsidies. In particular, the Commission should condition the receipt of federal explicit high-cost support on reductions in intrastate switched access charges. Only by continuing to remove implicit access subsidies can the Commission (and the states) fulfill section 254(b)(4)’s mandate that carriers’ contributions to the preservation and advancement of universal service be equitable and nondiscriminatory.

Exacerbating the inequity in the current system is the Commission’s current revenues-based contribution methodology. Universal service support cannot be used to promote broadband deployment as envisioned by the policy makers unless it is supported by a stable, sustainable, and technology-neutral contribution methodology. For years, providers have warned the Commission about the ever increasing problems with identifying interstate end-user telecommunications service revenues and have cautioned that a revenues-based methodology is

²⁴ See, e.g., AT&T *Qwest II* NPRM Comments (filed April 3, 2006).

unsustainable. Although the Commission has previously acknowledged these difficulties, and recognized the wisdom of moving to a numbers-based mechanism, it has yet to respond.

The passage of time is only making the flaws in the current methodology more pronounced. The Commission's contribution factor may reach and even exceed 12 percent for the first time in the next quarter. In the near future, we will reach the tipping point at which time the high contribution factor will price some consumers out of the market, thus rendering certain communications services – interstate telecommunications services, to be precise – unaffordable.²⁵ There is no basis to conclude that the contribution factor will do anything other than continue to increase. AT&T urges the Commission to act now to establish a more sustainable and efficient contribution methodology by adopting the telephone numbers- and connections-based contribution methodology proposal that it filed with the Commission last year.²⁶

The Commission also must recognize that it cannot ensure that all carriers contribute equitably to the preservation and advancement of universal service through reform of only the federal high-cost support mechanisms and the universal service contribution methodology. Rather, it must finally complete comprehensive intercarrier compensation reform, which was one of the proceedings the Commission listed as pending in its *Tenth Circuit Remand Order* issued

²⁵ See, e.g., *Alenco v. FCC*, 201 F.3d 608, 620 (5th Cir. 2000) (*Alenco*) (“excessive subsidization in some rates may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market”); *Qwest II*, 398 F.3d at 1234.

²⁶ Letter from Mary L. Henze, AT&T, and Kathleen Grillo, Verizon, to Marlene Dortch, FCC, *Universal Service Contribution Methodology, Federal-State Joint Board on Universal Service*, WC Docket No. 06-122; CC Docket No. 96-45 (filed Sept. 11, 2008); Letter from Mary L. Henze, AT&T, and Kathleen Grillo, Verizon, to Marlene Dortch, FCC, *Universal Service Contribution Methodology, Federal-State Joint Board on Universal Service*, WC Docket No. 06-122; CC Docket No. 96-45 (filed Oct. 20, 2008); Letter from Mary L. Henze, AT&T, to Marlene Dortch, FCC, *Universal Service Contribution Methodology, Federal-State Joint Board on Universal Service*, WC Docket No. 06-122; CC Docket No. 96-45 (filed Oct. 28, 2008).

five and a half years ago. That proceeding cannot languish any longer. The Commission has a massive record, refreshed most recently in late 2008, upon which to base a legally sustainable decision that overhauls the antiquated intercarrier compensation regime.

Specific, Predictable, and Sufficient High-Cost Mechanisms. “There should be specific, predictable and sufficient Federal and State mechanisms to preserve and advance universal service.” 47 U.S.C. § 254(b)(5). As is the case with too many of the other universal service principles, the Commission’s current high-cost model mechanism does not satisfy even one of this principle’s components. As noted above, by basing support on a carrier’s statewide average costs of serving customers, that mechanism forces non-rural carriers to continue to rely on implicit subsidies in state rates (principally, intrastate access rates) to achieve universal service objectives and ensure that rates in rural and other high-cost areas are affordable. As a consequence, the existing high-cost model mechanism is obviously not “specific,” as demonstrated by the fact that AT&T provides service to more rural access lines than any other carrier yet it receives high-cost model support in just three of its 22 ILEC states. Nor is this mechanism predictable or sufficient insofar as it continues to rely on implicit subsidies that are eroding at an accelerating pace as carriers continue to lose a growing number of lines every quarter. Indeed, the only thing that is “predictable” about this mechanism is that too many purportedly “non-rural” carriers are assured of receiving inadequate (and dwindling) support to provide service in high-cost areas. Until the Commission finally does something to induce the states to make explicit the implicit support in intrastate rates, the Commission’s high-cost support mechanisms will never be specific, predictable or sufficient.

It is entirely possible that there is “sufficient” universal service support sloshing around the existing federal and state, explicit and implicit access mechanisms and that no

additional support is necessary to comply with Congress’s universal service mandates. But until the Commission requires the removal of implicit support in intrastate access charges through the use of some combination of carrots and sticks, it will be hard-pressed to demonstrate that any high-cost mechanism that it will adopt in next year’s order will be “sufficient” to preserve, let alone *advance*, universal service. To “preserve” universal service, any high-cost mechanism that the Commission adopts must ensure the availability of voice communications using any technology or application. To “advance” universal service, such mechanisms must ensure that consumers in rural and high-cost areas have access to advanced telecommunications and information services that are reasonably comparable to those that are ubiquitously available in urban areas. In 2009, such services clearly include broadband.

Competitive Neutrality. “Universal service support mechanisms and rules should be competitively neutral. In this context, competitive neutrality means that universal service support mechanisms and rules neither unfairly advantage nor disadvantage one provider over another, and neither unfairly favor nor disfavor one technology over another.”²⁷ The Commission adopted this principle pursuant to its authority under 47 U.S.C. § 254(b)(7). The Commission previously interpreted this principle to mean that it must fund competition (i.e., competitive ETCs). The result of that decision was explosive growth in the overall size of the universal service fund, prompting the Commission to cap competitive ETC funding last year.²⁸ The Commission need not fund competition to meet this principle and, indeed, it should not. Instead, it simply must ensure that it gives no advantage to a particular carrier, class of carrier, or technology when determining which provider should receive high-cost support.

²⁷ *Universal Service First Report and Order*, 12 FCC 8776, ¶ 47 (1997).

²⁸ *See Interim Cap Order*.

Additional Principles. “Such other principles as the Joint Board and the Commission determine are necessary and appropriate for the protection of the public interest, convenience, and necessity and are consistent with this Act.” 47 U.S.C. § 254(b)(7). While we are not advocating that the Commission establish additional principles at this time, AT&T urges the Commission to consider that the other universal service principles be informed by this last subparagraph, in particular, Congress’s injunction that the Commission and states must ensure that universal service policies and mechanisms are “necessary and appropriate for the protection of the public interest.” AT&T believes that applying this principle means, among other things, that federal high-cost support should not be used to perpetuate state implicit subsidies in intercarrier rates. Allowing such subsidies to continue has the effect of forcing consumers in some states to support artificially low rates for consumers in other states. Unless the Commission makes removal of implicit subsidies from intrastate access charges a condition for receipt of federal high-cost support (to recover costs classified as “intrastate”), it will perpetuate this inequity.

B. Applying the Principles of Section 254(b) to a High-Cost Mechanism Designed for the 21st Century.

A fresh look at the universal service principles should lead the Commission to conclude two things: (1) the Commission’s obligation to *advance* (and not simply preserve) universal service can only be satisfied by the Commission overhauling and re-directing its high-cost support mechanisms to promote the deployment of broadband infrastructure in areas that currently lack broadband service; and (2) the Commission must do more to eradicate state implicit access subsidies, which pose a formidable obstacle to the promotion of broadband deployment.

1. The Commission Should Establish New Broadband Funds and Transition Legacy Support to These New Funds.

Just over a year ago, AT&T offered a proposal for the Commission to transition its current, POTS-centric high-cost support mechanisms to two broadband funds – one fund that would support deployment of fixed location infrastructure and a second for mobile wireless infrastructure.²⁹ In formulating this proposal, AT&T sought to build this proposal upon the Joint Board’s recommendation that the Commission establish a broadband fund and a mobility fund.³⁰ With a one sentence decision, the Commission declined to implement the Joint Board’s recommendations last November.³¹ While the Commission may have satisfied one statutory obligation in section 254 (i.e., “to complete any proceeding to implement” Joint Board recommendations within one year),³² meeting its other obligations under this statute in order to respond to the Tenth Circuit will require dramatically more effort.

AT&T also sought to respond to the expressed desire of a number of policy makers that broadband and mobility services should be made ubiquitously available to consumers throughout the United States. Since then, Congress and the Administration have earmarked billions of dollars in the economic stimulus package for broadband deployment in unserved and underserved areas,³³ thus removing any doubt as to the importance that these policy makers place on pushing broadband facilities ever farther into rural high-cost areas. Modifying and retargeting

²⁹ See AT&T April 2008 Proposal.

³⁰ See generally *Recommended Decision*.

³¹ *ISP-Bound Reciprocal Compensation Mandamus Order*, FCC 08-262, ¶ 36 (rel. Nov. 5, 2008) (“We choose not to implement these recommendations at this time, however.”).

³² 47 U.S.C. § 254(a)(2).

³³ American Recovery and Reinvestment Act, § 6001.

the Commission's high-cost mechanisms to promote broadband deployment not only would respond to the will of Congress and the Administration, it would also promote the full-range of objectives in section 254(b), as discussed herein.

a. Summary of AT&T's Broadband Proposal.

In its April 2008 proposal, AT&T encouraged the Commission to establish a Broadband Incentive Fund and an Advanced Mobility Fund and to transition wireline legacy support to the former fund and mobile wireless legacy support to the latter fund. While AT&T recommended that the wireline transition initially should apply to support mechanisms applicable to price cap carriers only, the Commission has committed to respond to the Tenth Circuit's remand of its high-cost support mechanism, and thus must (as the court required in *Qwest I*) develop a "complete plan" for universal service reform to present to the Tenth Circuit next year. Any such plan obviously must include rate of return carriers.³⁴ As AT&T previously has proposed, the Commission ultimately should seek to merge all of its high-cost support mechanisms, and provide support to all service providers based on the high cost of serving particular customers rather than the identity or classification of the provider serving them. This means that, in the long run, the Commission also must transition its high-cost support mechanisms for so-called rural carriers to support deployment of broadband. AT&T recognizes, however, that the Commission may deem it appropriate to adopt a different timetable for that transition than it

³⁴ That is particularly true now that such carriers are beginning to experience the same, dramatic losses of access lines and minutes as that of price cap carriers earlier in the decade, which is increasing the size of the federal universal service fund, and thus the contribution factor for carriers and consumers across the country.

would apply to price cap carriers. In any event, the Commission should begin the transition for price cap carriers as soon as possible.³⁵

Under AT&T's proposal, participation in both broadband funds would be voluntary. Fixed network and mobile wireless network providers would submit applications to the state commission or the Commission for project-based funding to construct new broadband network facilities in unserved areas. An unserved area is one in which broadband service is not available.³⁶ In its application for funding to construct broadband facilities, an applicant would identify the amount of support it believes necessary to deploy and maintain the infrastructure necessary to provide the supported services in the designated area for the service term. If selected, the applicant must commit to making those services substantially available throughout the designated area within a two-year period and then continuing to make those services available for five years thereafter. At the end of the term of service, each funding recipient would have the opportunity to petition the Commission to treat a "served" area as "unserved" if continued support was necessary to maintain service in that area and no other provider offers such service in that area.

In identifying and mapping which areas are "unserved," the Commission could rely on information that it gathers from fixed location and mobile wireless broadband providers,

³⁵ The Commission should, of course, allow so-called "rural carriers" to opt-in to the Broadband Incentive Fund mechanism.

³⁶ For the Broadband Incentive Fund, a successful applicant would be required to provide users with "advanced telecommunications capability" (as defined in section 706) and any other pre-defined criteria (e.g., minimum downstream transmission capability), as well as access to voice communications capabilities and Lifeline service. For the Advanced Mobility Fund, a successful applicant would be required to provide users with advanced telecommunications capability as defined in section 706 and consistent with the Commission's current broadband definition, as well as access to mobile wireless voice communications and Lifeline service.

information compiled by other sources (e.g., Connected Nation) or information provided by applicants themselves. AT&T suggests that the Commission consider permitting applicants to self-identify unserved areas, at least at the inception of the new mechanisms, until more comprehensive broadband service mapping work is completed.³⁷ The minimum area covered by a Broadband Incentive Fund application should be all unserved areas within a wire center. For the Advanced Mobility Fund, the Commission should consider making support available in the near term for both CDMA and GSM technologies.³⁸ If the Commission does so, an “unserved area” is an area in which mobile wireless broadband service is not available at all or is available using CDMA or GSM mobile wireless technologies, but is not available from both. Advanced Mobility Fund applicants would apply to provide service to unserved areas that they select, which might or might not include all unserved areas within an ILEC’s wire center.³⁹

Next, the Commission would determine, by state, how much support would be available to fund applications. This determination would be based primarily on the extent to which a state has unserved areas for fixed and mobile wireless broadband services.⁴⁰ However, the Commission could set aside funding for meritorious applications that would not otherwise receive funding based on how the Commission allocated funding among the states. Alternatively, for the Broadband Incentive Fund, the Commission could set aside funding to

³⁷ The Commission or the states would, of course, verify that the applicant proposed to serve an unserved area.

³⁸ Present mobile wireless technologies do not allow CDMA customers to roam on GSM networks (and vice versa). For example, if a CDMA customer is in an area where service is available only using GSM technologies, that customer would not be able to make a wireless call to 911.

³⁹ AT&T believes that this flexibility is appropriate for mobile wireless providers because the service areas covered by their licenses bear no relationship to ILEC wire centers or study areas.

⁴⁰ In addition to the population to be covered in unserved areas within each state, for the Advanced Mobility Fund, the Commission also could consider the amount of unserved miles along federal and state highways and other public roads.

encourage states to establish matching fund programs. The Commission then would make available information about the particular unserved areas (e.g., location, size of the unserved area, population density, planned development in the area) and the amount of funding available in each state. It should do so as soon as possible following the effective date of a Commission order establishing these new funds so that would-be applicants can evaluate whether to apply for support to serve those areas.

Interested providers would submit applications to either the relevant state commission or the Commission to provide the supported services in unserved areas. An applicant would submit its application to the Commission to review if the state commission determines that it has no jurisdiction to review applications for funding to provide broadband service. Applicants should be required to include in their applications the following information and commitments: the project proposal (which would identify the number of unserved households and, for mobile wireless providers, information regarding the population and amount of unserved highway mileage covered by the application); the amount of requested funding to deploy and maintain the facilities and supported services in the area for the term of the award; the facilities the applicant proposes to deploy; the applicant's build-out plan (which should include a deployment schedule not to exceed two years); sufficient financial information for the state or the Commission to determine whether the applicant will have the ability to meet its commitment to serve for the term of the award; a commitment to make the supported services substantially available to households in the unserved area (for the Broadband Incentive Fund applicants) or to substantially all of the unserved area (for Advanced Mobility Fund applicants) within two years and, then, for five years thereafter; a commitment to provide the supported services at rates, terms, and conditions that are reasonably comparable to those services offered in urban areas; and for

mobile wireless applicants, a commitment to negotiate in good faith with providers using other technologies to deploy their own wireless transmission facilities at any new cell sites constructed with Advanced Mobility Fund support, to the extent feasible and on a nondiscriminatory basis.

A state (or the Commission) would follow clear and detailed criteria in reviewing and ranking applications for funding to provide supported services in that state. Those criteria should include an evaluation of the requested amount of support per number of unserved households (for Broadband Incentive Fund applicants) or per population (for Advanced Mobility Fund applicants) covered by the application, financial qualification requirements, a minimum population density per square mile or a minimum population to be covered by the application, and the time to build-out the unserved area. For Advanced Mobility Fund applicants, the criteria should also include a minimum amount of unserved mileage along frequently traveled roads and an explanation of any other unfulfilled public safety, homeland security or other need that may warrant funding. Based on these Commission-specified criteria, the states should rank those applications that would result in the greatest utilization of the supported services (e.g., those projects that target the greatest population density and/or unserved mileage along highways) over applications that propose to serve less densely populated areas and/or fewer highway miles.⁴¹ The Commission would provide substantial deference to the states' rankings in reviewing and granting applications. And the Commission would fund only one fixed broadband provider per unserved area and up to one CDMA and one GSM wireless mobile broadband provider per unserved area.

⁴¹ When ranking mobile wireless applications, AT&T recommends that areas and applications be prioritized in the following descending order: areas without mobile wireless *voice* service from any provider; areas where mobile wireless *voice* service is available from just one technology; areas where mobile wireless *broadband* service is not available at all; and finally, areas where mobile wireless *broadband* service is available from one but not both technologies.

Balancing the universal service principles, the Commission must determine how much funding it should disburse through the new broadband funds. In its *Recommended Decision*, the Joint Board suggested that the Commission disburse about \$1 billion of funding per year through the new mobility fund (for mobile wireless voice)⁴² and \$300 million through a new broadband fund, although some deemed the latter amount inadequate.⁴³ Regardless of how much funding the Commission decides to disburse through the broadband fund, it should immediately begin to transition to the Advanced Mobility Fund all funding previously provided to wireless competitive ETC under the existing high-cost support mechanisms. AT&T has recommended that beginning one year after the effective date of a Commission order adopting this proposal, the Commission should reduce all legacy wireless support by 20 percent per year over a five-year period, and to redeploy such funding to the Advanced Mobility Fund. AT&T further recommended that such support should be earmarked for projects in the state in which such support was provided under the legacy high-cost support mechanisms until that state has no unserved areas, at which time such support would be released to the fund advanced mobile services in unserved areas in other states.

AT&T also proposed that the Commission transition all price cap legacy wireline support to the Broadband Incentive Fund. This transition would be triggered on a state-by-state basis once the relevant state commission grants price cap ILECs in that state complete retail pricing

⁴² *Recommended Decision* at ¶ 28.

⁴³ *Id.* at ¶ 29. *See also* Statement of Acting Chairman Michael J. Copps to the *Recommended Decision* (“Instead of bold recommendations to implement our historic decision, the Joint Board only suggests that \$300 million of federal dollars be dedicated to this challenge.”).

flexibility.⁴⁴ The length of the transition would correspond to the amount of time over which the state fully phases in such pricing flexibility. Legacy price cap ILEC support that is redeployed to the Broadband Incentive Fund should be earmarked for projects in the state in which such support was provided under the legacy high-cost support mechanism until that state has no more unserved areas *or* areas in which fixed location broadband service is available but does not satisfy the Commission-specified criteria for the supported service, at which time the support would be redirected to the general Broadband Incentive Fund for use in any state.

b. Applying the Universal Service Principles to AT&T's April 2008 Proposal.

AT&T's proposal to establish a Broadband Incentive Fund and an Advanced Mobility Fund would promote and appropriately balance each of the principles set forth in section 254(b), thereby preserving and advancing universal service:

Affordability. As discussed above, the Commission should find that a service is being offered at an "affordable" rate if a significant number of consumers are subscribing to those services, and either the market for such services is competitive or such services remain subject to regulation. The Commission previously has concluded elsewhere that the market for broadband services is robustly competitive with a variety of inter- and intramodal competitors vying to attract and retain customers. Although broadband subscription rates are not as ubiquitously high as they are for POTS or mobile wireless service,⁴⁵ the Commission can and should review the

⁴⁴ For purposes of this proposal, by "complete" or "full" retail pricing flexibility, AT&T means pricing flexibility with respect to all retail services, including basic residential and business access lines.

⁴⁵ That is so for a variety of reasons that have nothing to do with the cost of broadband services. For example, to take advantage of such services, consumers must own a computer, which some customers may not be able to afford even if they could afford to purchase broadband Internet access and other advanced services.

range of rates that consumers pay for such services in areas where broadband subscribership is high. Under AT&T's proposal, applicants to the Broadband Incentive Fund and the Advanced Mobility Fund would have to commit to provide supported services in the areas for which they seek universal service support at rates and on terms and conditions that are reasonably comparable to the rates offered in urban areas. In addition, the Commission – working in conjunction with other federal agencies – could obtain data on how much Americans spend on broadband services each year as a percentage of total household expenditures and compare that percentage to other discretionary expenditures to periodically evaluate the affordability of broadband service. As discussed above, successful applicants would have to commit to offer the supported services at an affordable rate for seven years.

AT&T recognizes that, although broadband service providers may be providing broadband services at an affordable rate, low-income consumers still may be unable to afford to purchase such services because of their individual economic circumstance. Consequently, AT&T has urged the Commission, as part of the shift in focus of federal universal service policy to broadband, to revise its Lifeline rules to enable broadband providers to participate in the Commission's low-income programs.⁴⁶ Currently, only eligible *telecommunications carriers* may participate, which means that providers of information services (e.g., broadband service providers) are, by definition, excluded. AT&T recommends that the Commission exercise its Title I authority to establish a Lifeline Service Provider designation that is independent from (and not subject to all of the requirements of) the traditional ETC designation established under section 214(e). Expanding the universe of eligible providers in this manner will not only

⁴⁶ See AT&T April 2008 Proposal at 25-27; AT&T Intercarrier Compensation/Universal Service Comments, WC Docket Nos. 05-337, 03-109, 06-122, 04-36, CC Docket Nos. 96-45, 99-200, 96-98, 01-92, 99-68, at 51-56 (filed Nov. 26, 2008).

increase participation in the Commission's low-income programs, it will serve to increase broadband Internet access penetration more generally.

Access to Advanced Services. By re-focusing the Commission's high-cost support mechanisms to target support to broadband infrastructure deployment projects in unserved areas, AT&T's broadband proposal is directly responsive to the Commission's mandate in section 254(b)(2) that it ensure that access to advanced telecommunications and information services should be provided in all regions of the country.

Reasonable Comparability. As discussed above, the Commission's existing high-cost support mechanisms have done nothing to ensure that consumers in rural, insular, and high-cost areas have access to telecommunications and *information services* that are reasonably comparable to those services provided in urban areas.⁴⁷ The longer that the Commission's high-cost support mechanisms target support to POTS, the greater the gap will be between the "advanced telecommunications and information services" offered in urban areas and those services offered in rural areas.

AT&T's proposal addresses this issue head on: applicants will commit to providing reasonably comparable telecommunications *and* information services (i.e., advanced telecommunications capability and access to voice communications) in rural, insular, and high-cost areas at rates, terms, and conditions that are reasonably comparable to those offered in urban areas for a seven-year period (i.e., the length of the term of service).

⁴⁷ According to the Pew Internet Project, in 2007, 52% of American adults living in urban areas had broadband service at home. This percentage plummets to just 31% for adult Americans living in rural areas. See Pew Internet Project, Home Broadband Adoption 2007, June 2007, at 4 (available at: http://www.pewinternet.org/~media/Files/Reports/2007/PIP_Broadband%202007.pdf.pdf).

Equitable and Nondiscriminatory Contributions. Because the current non-rural high-cost support mechanism relies on discriminatory implicit subsidies from a subset of carriers, the Commission cannot demonstrate that carrier contributions to the existing high-cost support mechanisms are equitable and nondiscriminatory. By transitioning support away from the POTS model to business models that do not rely on implicit subsidies, AT&T's broadband proposal alleviates, to some degree, the inequity in the current policies. But, to fully satisfy this principle, the Commission cannot stop with universal service high-cost distribution reform. It must also modify its universal service contribution methodology and revamp its intercarrier compensation rules.

Specific, Predictable, and Sufficient High-Cost Mechanisms. Under AT&T's proposal, applicants would be required to identify in their applications for support how much support would be necessary for them to deploy broadband infrastructure in unserved areas. Winning applicants thus would receive support that is both "predictable" and "sufficient" to *advance* universal service objectives. AT&T's proposal also would permit applicants to petition the Commission for additional support if it would not be economic to continue offering supported services in that area without continued universal service support. AT&T's proposal thus would ensure that support is predictable and sufficient to *preserve* universal service. And, insofar as support would be targeted to fund particular broadband infrastructure deployment projects, it also would be "specific."

Competitive Neutrality. AT&T's proposal is competitively neutral because any provider of the supported services could apply for funding. To comply with this principle, the Commission simply must not favor any provider or technology when selecting applicants for project-based broadband funding.

2. During the Transition to the Broadband Incentive Fund, the Commission Should Immediately Recalibrate Existing Support and Condition Recalibrated Support on Lowering Intrastate Access Charges to Interstate Levels.

The Commission should move quickly to establish the two broadband funds. While transitioning legacy mobile wireless support can be accomplished methodically and without delay, it is likely that transitioning legacy wireline support will require more time since the trigger AT&T has proposed for transitioning legacy wireline high-cost support to the Broadband Incentive Fund relies on individual state commission action. But, to comply with section 254(b) and to respond to the Tenth Circuit’s remand orders, the Commission cannot continue using its invalidated, non-rural high-cost model support mechanism pending the completion of the Broadband Incentive Fund transition. Accordingly, the Commission must act immediately to reform this mechanism.⁴⁸

In *Qwest II*, the court concluded that the Commission failed to demonstrate how its comparability benchmark, set at the national urban average plus two standard deviations, not only results in “reasonably comparable” rural and urban rates but preserves and advances universal service.⁴⁹ The court also faulted the Commission for neglecting to consider all of the relevant principles in section 254(b) when it concluded in its *Tenth Circuit Remand Order* that universal service support is “sufficient” so long as it enables “states to achieve reasonable

⁴⁸ Mobile wireless competitive ETC support would not be affected by this reform. Instead, wireless competitive ETC support would be subject to its own transition (i.e., 20% reduction in support each year for a five-year period) that is completely divorced from the legacy wireline transition.

⁴⁹ See *Qwest II*, 398 F.3d at 1236-37 (finding both that the Commission’s benchmark ensures that “significant variance between rural and urban rates will continue unabated” and that the Commission ignored its concurrent obligation to advance universal service, “a concept that certainly could include a narrowing of the existing gap between urban and rural rates”).

comparability of rural and urban rates in high-cost areas served by non-rural carriers.” On remand, the court directed the Commission to “articulate a definition of ‘sufficient’ that appropriately considers the range of principles identified in the text of the statute.”⁵⁰

Because the current non-rural high-cost model support mechanism relies on statewide averaging (and thus on implicit subsidies in state rates), too many rural and high-cost areas do not receive any support, much less sufficient support to ensure that universal service objectives are preserved and advanced in a competitive marketplace. Carriers serving such areas confront rapidly accelerating losses in access minutes and lines – particularly in more densely populated (and thus lower cost) wire centers – and thus have suffered precipitous declines in the implicit support that made it possible for them to offer services comparable to those offered in urban areas in rural and other high-cost areas at affordable rates.

The amount of explicit support disbursed to non-rural carriers for their high-cost wire centers is not only insufficient, but also not specific (i.e., targeted to those areas where support is needed to preserve and advance universal service objectives) as required by the statute.⁵¹ AT&T notes in this regard that, although it provides service in some of the most rural areas of the country, AT&T receives support through the high-cost model mechanism in just three of its 22 states.⁵² And, insofar as the existing high-cost mechanisms do nothing to encourage states to make explicit the implicit subsidies in access charges, those mechanisms force non-rural carriers

⁵⁰ *Id.* at 1234.

⁵¹ *See* 47 U.S.C. § 254(b)(5).

⁵² Moreover, AT&T receives state high-cost support in just six of its 22 states and that support is diminishing, in some cases significantly.

to rely on rapidly diminishing – and thus wholly unpredictable – support to achieve universal service objectives in rural and other high-cost areas served by non-rural carriers.

AT&T recognizes, as did the Tenth Circuit, that the greatest impediment to the Commission meeting all of the directives contained in section 254(b) has been the limits on its authority over intrastate rates and its reluctance to condition receipt of explicit federal high-cost support on removal of intrastate implicit subsidies. But further inaction to address the consequences of the rapid decline in those subsidies is no longer an option. Thus, even if section 2(b) of the Act places limits on the Commission’s authority to regulate intrastate rates, the Commission is obligated, under section 254, to take action to ensure that these marketplace developments do not further undermine universal service objectives. Accordingly, it should take the Tenth Circuit up on its suggestion, made almost nine years ago, that the Commission condition a state’s receipt of federal funds upon adequate state action to ensure reasonable comparability of rates between urban and rural areas.⁵³ As that court recognized, it would be “impossible for the FCC alone to ensure reasonably comparable rates . . . unless it were willing to commit massive federal support. . . .”⁵⁴ And doing so, of course, would violate other principles in section 254(b).⁵⁵ While the *Qwest II* court concluded that Congress did not foreclose the possibility of the continued existence of state implicit support mechanisms that “function effectively to preserve and advance universal service,” no one can seriously contend that, for example, high intrastate switched access charges “function effectively” to ensure that congressional objects are met in a competitive marketplace; indeed, as AT&T has described in

⁵³ *Qwest I*, 258 F.3d at 1203-04.

⁵⁴ *Id.* at 1203.

⁵⁵ *Qwest II*, 398 F.3d at 1234; *Alenco*, 201 F.3d at 620.

other filings, they impede universal service by, among other things, creating disincentives to broadband deployment and widespread adoption.⁵⁶

To respond to the Tenth Circuit’s mandate and thus address the shortcomings of the existing non-rural support mechanism, AT&T recommends that the Commission “recalibrate” how support is calculated and disbursed to “non-rural” carriers.⁵⁷ First, the Commission must jettison statewide averaging and target support to wire centers or to census block groups (or portions of census block groups) within wire centers. In so doing, the Commission must identify rural and high-cost areas using definitions that are relevant to the costs of serving a particular area (such as based on demographics and/or topological factors) – not the size or classification of the carrier (i.e., “rural” or “non-rural”) serving an area. Second, the Commission should condition the recalibrated support on a carrier lowering its local rates to the Commission-established rate comparability benchmark,⁵⁸ and reducing intrastate switched access charges to interstate levels. We provide additional detail below.

⁵⁶ See AT&T April 2008 Proposal; Letter from Robert W. Quinn, Jr., AT&T, to Chairman Kevin Martin, FCC, CC Docket Nos. 01-92, 96-45, 99-68, WC Docket Nos. 05-337, 07-135 (filed July 17, 2008). See also Phoenix Center for Advanced Legal & Economic Public Policy Studies, *Do High Call Termination Rates Deter Broadband Deployment?*, Phoenix Center Policy Bulletin No. 22 (October 2008) at 8-9 (concluding that “in high-cost areas, the incentive of an incumbent LEC to upgrade its network to broadband service is diminished – and perhaps even outright deterred – by the current system of high, carrier-specific call termination rates”).

⁵⁷ Like the Broadband Incentive Fund, the Commission should permit “rural” carriers to opt-in to this reformed high-cost mechanism.

⁵⁸ As the Commission no doubt is aware, rates in rural and other high-cost areas generally have been set well-below cost and, indeed, below rates for comparable services in urban areas pursuant to state regulation. In most cases, such rates are based on purportedly lower “value of service” pricing schemes (on the theory that, because rural areas have lower population densities than urban areas, subscribers in those areas can connect to fewer subscribers in the local calling area). Of course, one could argue that subscribers in rural areas value telephone service more highly than those in urban areas because, for example, subscribers in rural areas are more dependent on such service to contact friends, neighbors and emergency services – all of which are not as readily accessible as they are in urban areas). In any event, the reality is that rates in rural and high-cost areas are, in most cases, below those in urban areas. These

The first step in recalibrating support is to identify those areas that are “rural” or “high-cost.” In so doing, the Commission should rely on the Census Bureau’s definition of “rural.” The Census Bureau is the federal government’s expert agency on issues of demographics. It is thus sound policy for the Commission to rely on the Census Bureau’s definition of this key term as well as consistent with recent changes that the Commission has made to its 477 form.⁵⁹ According to the Census Bureau, “rural” consists of all territory, population, and housing units located outside of an “urban” area, which consists of core census block groups or blocks that have a population density of at least 1,000 people per square mile and surrounding census blocks that have an overall density of at least 500 people per square mile.⁶⁰ Next, the Commission must identify which areas are “high cost.” As a general matter, low population density is what makes an area a “high cost” one for a carrier to serve.⁶¹ The Commission should evaluate the distribution of census block groups (or census blocks) by population density. Such data are readily available to the Commission.

circumstances are becoming increasingly problematic with the ever-increasing levels of competition in the communications industry. Value of service pricing was the consequence of a heavily regulated monopolistic environment which no longer exists and, consequently, needs to give way to a cost of service pricing regime with explicit support to high-cost areas where the cost-based rates are deemed to be too high.

⁵⁹ See *477 Modification Order*, WC Docket No. 07-38, Report and Order and Further Notice of Proposed Rulemaking, 23 FCC Rcd 9691, ¶ 12 (2008) (explaining that the Commission will require broadband providers to report their numbers of broadband subscribers on a Census Tract basis after concluding that census-based units are more stable and static than ZIP Codes and correspond more consistently to actual locations).

⁶⁰ U.S. Census Bureau, Census 2000 Urban and Rural Classification (available at: http://www.census.gov/geo/www/ua/ua_2k.html).

⁶¹ As the Commission notes in its *Tenth Circuit NOI*, terrain and climate conditions also contribute to a carrier’s costs in providing service but these factors are the exception, not the rule, in driving carrier costs. See *Tenth Circuit NOI* at ¶ 27. The one state where these factors are most pronounced, Alaska, does not have any carriers that receive support under the non-rural carrier high-cost support mechanism. See also *Joint Board Recommended Decision* at ¶¶ 12, 16 (discussing the effect of low customer density on the need for continuing operating subsidies).

Next, based on a balancing of the section 254(b) principles, in particular, balancing concerns about ensuring the sufficiency of support against concerns about not creating a disproportionate and unsustainable burden, the Commission must decide where on the population density scale to define areas as “high cost.” In particular, the Commission would have to weigh the potential impact on the size of the fund of supporting more areas. The more areas that are supported, the greater the risk that the overall fund size will become too large. As both the Fifth and Tenth Circuits recognized, at some point, increasing the size of the fund, and thus the contribution burden on subscribers in urban areas, will itself implicate affordability, as well the sufficiency of support.⁶² Plainly, establishing this parameter as well as setting the comparability benchmark (discussed below), is not an exact science. In the end, the Commission will have to balance these factors in a reasonable manner in arriving at a determination of what constitutes “high cost,” and explain its decision. The Commission also could adjust the density distribution for terrain, proximity to metropolitan areas, and, perhaps, daytime population rather than strict residential population but the Commission would first have to develop a methodology to do so.

Once it has identified the areas in which non-rural carriers are eligible to receive high-cost funding, the Commission must then determine how much, if any, support such carriers should be eligible to receive for providing service in those areas. To make this calculation, the Commission should first establish a rate comparability benchmark. This benchmark would be set using a simple calculation. First, the Commission would identify the relevant “urban” rate that would be used as the basis for comparison with rates in rural and high-cost areas. That rate, for example, could be the national average urban rate, median urban rate or some average above

⁶² *Alenco*, 201 F.3d at 620 (“excessive funding may itself violate the sufficiency requirements of the Act. . . . [E]xcess subsidization in some cases may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market.”); *Qwest II* at 1234 (excessive subsidization affects affordability of telecom services thus violating section 254(b)(1)).

the median rate. Next, the Commission would establish a comparability factor that would be used to determine whether rates in high-cost areas are “reasonably” comparable with the urban rate benchmark.⁶³ Again, in setting the comparability factor, the Commission would have to balance the principles of section 254(b). The higher the factor, the less universal service funding would be required to ensure that rates in high-cost areas are “reasonably comparable” to those in urban areas. Of course, the higher the comparability factor, the greater the potential variation in rates between low and high-cost areas, and thus the less likely the factor would withstand judicial scrutiny.⁶⁴ The following example demonstrates how this process would work. Assume that the national average urban rate is \$25. If the Commission applies a comparability factor of 1.2, the comparability benchmark would be \$30.

Next, the Commission would compare rates in rural and high-cost areas and make support available where needed to ensure that rates do not exceed the rate comparability benchmark. The Commission would make support available in two circumstances: (1) to reduce rates in rural and high-cost areas where rates exceed the benchmark and (2) to fund an appropriate portion of any gap between the cost of providing supported services⁶⁵ in high-cost

⁶³ This factor could be set in part based on a consideration of what portion of the universal service burden should be borne by the respective jurisdictions.

⁶⁴ *Qwest II*, 398 F.3d at 1236 (establishing a comparability benchmark at the national urban average plus two standard deviations ensures that significant variance between rural and urban rates will continue unabated, thus violating section 254(b)(3)).

⁶⁵ The Commission could calculate costs in one of several ways, including using the existing cost model. Other options including applying regression techniques to link household density with forward-looking costs or using a competitive process (e.g., carriers apply to provide the supported services as the COLR in a particular rural high-cost area for a certain amount of funding). The Nebraska Commission applies a regression analysis to calculate how much support carriers will receive through its state high-cost fund. *See, e.g., In the Matter of the Nebraska Public Service Commission, on its own motion, seeking to establish a long-term universal service funding mechanism*, Application No. NUSF-26, Progression Order No. 5 (June 29, 2004). If the Commission anticipates that the reformed non-rural high-cost support

areas and the expected retail revenues associated with those supported services or some other measure.⁶⁶ Finally, the Commission should condition support on reductions in intrastate access charges. Recipients of federal high-cost support should be required to reduce their intrastate access charges both to account for any increases in end-user rates needed to reach the comparability benchmark and for any support received through the reformed high-cost support mechanism.

This “recalibrated” non-rural high-cost support mechanism addresses the *Qwest II* court’s concern that the existing non-rural support mechanism does nothing to narrow the gap between rural and urban rates and thus “advance universal service.”⁶⁷ By identifying rural and high-cost areas at a more granular level, support disbursed through this reformed high-cost support mechanism will be more “specific” than today’s non-rural high-cost model support mechanism, which provides support to high-cost areas in just ten states. Moreover, AT&T’s proposal finally gives the Commission the tools it needs to establish a “sufficient” mechanism that balances the principles of section 254(b). Only by doing more to stamp out implicit access subsidies, will the Commission have any ability to gauge whether its non-rural carrier high-cost support mechanism is “sufficient.” This reformed and recalibrated mechanism, however, has a limited shelf life. It should be apparent from the preceding discussion of the section 254(b) principles that, in 2009, the Commission will be unable to satisfy all of those principles, which it must, unless it shifts the focus of its high-cost support mechanisms from POTS to advanced telecommunications and

mechanism will only be used for a relatively brief period of time (i.e., until the transition to the Broadband Incentive Fund is complete), it may be prudent for it to continue using its existing cost model.

⁶⁶ Such revenues should be calculated assuming that end-user rates are at the comparability benchmark. This will ensure that the federal mechanism does not support unfairly low rates.

⁶⁷ *Qwest II*, 398 F.3d at 1236.

information services, thereby *advancing* universal service. When the Commission presents its complete plan to the Tenth Circuit next year, it should provide an order that implements, in tandem, AT&T's broadband and non-rural carrier high-cost model support reform proposals.

III. CONCLUSION

It should be clear to the Commission from these comments that incremental reform to its non-rural carrier high-cost model support mechanism will be insufficient to withstand judicial scrutiny. Instead, the Commission is required by statute to make universal service relevant to existing market conditions, particularly when bringing broadband to every American is a national policy goal. AT&T has offered a proposal that is grounded in all of the principles enunciated by Congress and it urges the Commission to incorporate this proposal into its proposed rules that it will issue in December.

Respectfully Submitted,

/s/ Cathy Carpino

Cathy Carpino

Christopher Heimann

Gary Phillips

Paul K. Mancini

AT&T Inc.

1120 20th Street NW

Suite 1000

Washington, D.C. 20036

(202) 457-3046 – phone

(202) 457-3073 – facsimile

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Its Attorneys