

**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 Universal Service	)	CC Docket No. 96-45

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**COMMENTS OF WINDSTREAM COMMUNICATIONS, INC.**

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**TABLE OF CONTENTS**

I. INTRODUCTION AND SUMMARY ..... 4

II. THE COMMISSION SHOULD CONSIDER HOW IT COULD BETTER TARGET HIGH-COST FUNDS TO ADDRESS THE NEEDS OF GRANULAR AREAS REQUIRING THE GREATEST AMOUNT OF FEDERAL ASSISTANCE. .... 5

    A. THE COMMISSION SHOULD SEEK TO PLACE PRICE CAP COMPANIES UNDER THE FORWARD-LOOKING MECHANISM..... 6

    B. THE COMMISSION SHOULD LOOK TO END ITS PRACTICE OF CONDITIONING ELIGIBILITY FOR HIGH-COST FUNDING ON AVERAGE STATE COSTS..... 12

III. THE COMMISSION SHOULD ASSESS HOW IT COULD USE A *RATE* BENCHMARK TO ENSURE RATE PARITY AND EASE THE BURDEN ON THE HIGH-COST FUND. .... 18

IV. IF IT INTENDS TO ENCOURAGE UNIVERSAL SERVICE RECIPIENTS TO DEPLOY MORE BROADBAND, THE COMMISSION FIRST MUST DETERMINE HOW IT CAN MAKE NEW FUNDS AVAILABLE TO SUPPORT BROADBAND OFFERINGS IN HIGH-COST AREAS..... 19

V. CONCLUSION..... 23

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**COMMENTS OF WINDSTREAM COMMUNICATIONS, INC.**

Windstream Communications, Inc., on behalf of itself and its affiliates (collectively “Windstream”), submits the following comments in response to the Federal Communications Commission (“Commission”) Notice of Inquiry (“Notice”)<sup>1</sup> that seeks to refresh the record regarding issues raised by the U.S. Court of Appeals for the Tenth Circuit (“Tenth Circuit” or “Court”) in the *Qwest II* decision.<sup>2</sup>

Windstream, the largest independent communications provider focused primarily on rural areas,<sup>3</sup> urges the Commission to address comprehensive high-cost reform within this remand proceeding. As Windstream has stated numerous times, the federal high-cost universal service system is in need of significant reform.<sup>4</sup> The existing high-cost mechanism fails to target funding to rural areas based on the nature of the area served,

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<sup>1</sup> *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service*, Notice of Inquiry, FCC 09-28 (rel. Apr. 8, 2009) (“Notice”).

<sup>2</sup> *Qwest Communications Int’l, Inc. v. FCC*, 398 F.3d 1222 (10th Cir. 2005) (“*Qwest II*”).

<sup>3</sup> With an average subscriber density of approximately 20 access lines per square mile, Windstream offers telecommunications services to approximately 3.0 million access lines across 16 states.

<sup>4</sup> See, e.g., Comments of Windstream Communications, Inc., WC Docket No. 05-337, CC Docket No. 96-45 (filed Apr. 17, 2008) (“Windstream Comprehensive Reform Comments”). Windstream incorporates by reference this filing and others that it previously submitted in the above-captioned dockets addressing high-cost reform.

thereby overfunding some areas while underfunding others. Bringing the high-cost system more in line with the universal service principles adopted in Section 254 of the Communications Act of 1934, as amended, (“the Communications Act”) will encourage efficiencies in operations and investment across the telecommunications marketplace.<sup>5</sup>

## **I. INTRODUCTION AND SUMMARY**

Windstream urges the Commission to use this remand proceeding as an opportunity to comprehensively reform the high-cost universal service system. In responding to the Tenth Circuit’s remand, the Commission should strive to better target support directly to granular high-cost areas. Specifically the Commission should focus on proposals to place price cap companies under a forward-looking mechanism, and reform the mechanism to eliminate eligibility requirements based on statewide average costs. These concurrent reforms would provide much-needed funding to high-cost areas that currently lack sufficient universal service support. As recognized by Federal-State Joint Board on Universal Service (“Joint Board”) member Larry S. Landis, failure to adopt such reforms that “align support with costs could put rural service at risk as surely as the unmanaged ballooning of the high cost program.”<sup>6</sup>

If it intends to use the high-cost program to support both broadband and voice, the Commission first should determine how it can make new federal funding available for the provision of broadband. Support for broadband will have the greatest impact if allocated

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<sup>5</sup> Section 254 of the Communications Act articulates principles that should serve as the basis for the Commission’s “policies for the preservation and advancement of universal service.” 47 U.S.C. § 254(b). These principles include, among others, (i) “specific, predictable, and sufficient” support should be provided “to preserve and advance universal service”; (ii) “quality services should be available at just, reasonable, and affordable rates”; and (iii) consumers in “all regions of the Nation” should have access to telecommunications and information services at “reasonably comparable rates.” *Id.*

<sup>6</sup> Statement of Commissioner Larry S. Landis, *Federal-State Joint Board on Universal Service*, FCC 07J-4, WC Docket No. 05-337, CC Docket No. 96-45, Recommended Decision (Jt. Bd., rel. Nov. 20, 2007) (“*Joint Board Recommended Decision*”).

initially in the form of grants. Grants hold the best promise of altering the economic barriers blocking new investment in remote and costly areas. They can fundamentally alter the economics of serving an area by offsetting up-front costs and blunting risks faced by investors, permitting a broadband provider to deploy and earn sufficient returns at affordable rates collected from a smaller customer base.

**II. THE COMMISSION SHOULD CONSIDER HOW IT COULD BETTER TARGET HIGH-COST FUNDS TO ADDRESS THE NEEDS OF GRANULAR AREAS REQUIRING THE GREATEST AMOUNT OF FEDERAL ASSISTANCE.**

In remanding the mechanism for non-rural carriers, the Tenth Circuit ordered the Commission to craft a support mechanism “taking into account all of the factors that Congress identified in drafting the Act and its statutory obligation to preserve and advance universal service.”<sup>7</sup> In particular, the Court demanded that the Commission reconsider its approach to ensuring universal service support is “sufficient” and that rates in rural areas are “reasonably comparable to rates charged for similar services in urban areas.”<sup>8</sup> Without fundamental reforms, the Commission’s construction of the statute will continue to be “fatal to the cost support mechanism . . . .”<sup>9</sup>

In response to the Tenth Circuit remand, Windstream urges the Commission, at a minimum, to give serious consideration to two reforms that together would better target support to high-cost areas. First, the Commission should eliminate eligibility requirements based on statewide average costs from the existing forward-looking mechanism. Second, the Commission should transform the current forward-looking, non-rural mechanism into a forward-looking mechanism for price cap carriers. These

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<sup>7</sup> *Qwest II*, 398 F.3d at 1237.

<sup>8</sup> 47 U.S.C. § 254(b)(3).

concurrent reforms would provide much-needed funding to high-cost areas that receive inadequate or altogether lack support. The reforms also would better align the Commission's cost support with interstate regulatory pricing regimes.

By adopting such reforms, the Commission would improve the business case for deploying broadband in high-cost areas that otherwise are too expensive to serve. Under a wire center targeted approach, many rural, high-cost, low density wire centers that deserve support no longer would be penalized due to variability of costs within other parts of their states. As support is recalculated and retargeted at a wire center level, many high-cost areas that are currently uneconomic to serve because of the substantial cost of shortening loops and otherwise upgrading dual-use plant would receive additional funding to help justify a case for broadband deployment.

**A. THE COMMISSION SHOULD SEEK TO PLACE PRICE CAP COMPANIES UNDER THE FORWARD-LOOKING MECHANISM.**

Any evaluation of the forward-looking mechanism should question whether it is appropriate to continue applying this mechanism only to “non-rural” carriers. Currently the mechanisms for “rural” and “non-rural” carriers are “substantially different.”<sup>10</sup> Carriers classified as “rural” are eligible for high-cost support under the embedded cost mechanism, which bases support on whether a company's historical costs in a study area exceed an average costs threshold. In contrast, carriers classified as “non-rural” receive this support only if their individual wire centers and the states where these wire centers are located qualify for support under the forward-looking mechanism. Carriers are assigned “non-rural” or “rural” status based upon a statutory definition enacted for the

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<sup>9</sup> *Qwest II*, 398 F.3d at 1226.

<sup>10</sup> *Joint Board Recommended Decision* at ¶ 20.

purpose of providing exceptions for when small carriers must comply with interconnection obligations contained in Section 251.<sup>11</sup>

Allocation of support under this bifurcated system often can be irrational. As recognized by the Joint Board, “support for customers served by one kind of carrier can be significantly more generous than for comparably situated customers served by the other kind of carrier.”<sup>12</sup> Particularly penalized are price cap carriers that fall under the rural mechanism. Price cap carriers, as compared to rate-of-return carriers, are more likely to have geographically large study areas, with a wider variation in size of wire centers contained within a study area.<sup>13</sup> Thus, these carriers are more likely to experience instances where a few high-density wire centers cause the average cost for an entire study area to fall below the threshold for rural support, even though the vast majority of wire centers in the study area are very small and serve very few people.<sup>14</sup> These conditions increasingly strain price cap operations, as high-density wire centers face significant competitive pressures and can no longer offer implicit support to other wire centers.

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<sup>11</sup> See 47 C.F.R. § 54.5 (providing that “rural telephone company” in the universal service context has the same meaning as how that term is defined in 47 C.F.R. § 51.5, in the interconnection context).

<sup>12</sup> *Joint Board Recommended Decision* at ¶ 20.

<sup>13</sup> Typical rate-of-return study areas usually are limited to small wire centers that serve contiguous areas with similar size and density characteristics. The average NECA Traffic Sensitive Pool member has 4,933 access lines with 4.6 lines per square mile, and one out of four NECA Traffic Sensitive Pool Members has fewer than 1,000 access lines. NATIONAL EXCHANGE CARRIER ASSOCIATION, TRENDS 2008 (rel. 2008) at 4.

<sup>14</sup> For example, Windstream faces this issue in its Southwest Texas study area, which has 198 wire centers that range in size from a few hundred lines to 47,000 lines in the two wire centers that serve the Texarkana community. This study area spans wire centers from Texarkana, Texas (along the Texas and Arkansas border) to those in Fabens, Texas (a community near El Paso and the New Mexico border). Texarkana and Fabens are separated by 717 miles, a distance farther than that separating Washington, DC from Jacksonville, Florida. In spite of many square miles in the Texas service area, this large rural territory is treated as one rural study area, and Windstream’s costs for all wire centers in the study area are averaged. The result of this averaging is that the few high density wire centers that serve the Texarkana community cause the average cost for the entire study area to fall below the qualifying level for rural support.

Both Embarq and CostQuest highlight this problem with today's rural support mechanism. First, Embarq explains how the "use of study-area average costs (per the rural mechanism) . . . perpetuate[s] the false assumption that revenues earned in low-cost areas can offset costs incurred in higher-cost areas":<sup>15</sup>

Th[e] study-area averaging system worked adequately when local exchange carriers were protected monopolies. Such implicit subsidies, however, are utterly inconsistent with a competitive marketplace. Customers and competition are harmed by perpetuating the old system of making only a subset of customers pay the bulk of the cost of universal service through implicit subsidies. Thus, the cost of paying for this obligation should belong to all of society and not just those people who choose to be customers of an ILEC . . . .<sup>16</sup>

Second, CostQuest's Ohio study illustrates disparities caused by whether support is distributed under "rural" or "non-rural regimes." CostQuest found that "funding does not seem to line up closely with where one might expect funding: areas of low population density within the state."<sup>17</sup> "[W]hile funding hits some . . . higher cost areas," CostQuest's study of Ohio wire centers produced "no indication as to how the funding is linked to the cost per wire center."<sup>18</sup> In fact, CostQuest discovered there was "minimal funding in the highest cost areas of state, Southeast Ohio."<sup>19</sup> This analysis led CostQuest to conclude that "the fundamental classification of rural versus non-rural . . . leads to

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<sup>15</sup> Letter from David C. Bartlett, Vice President – Federal Government Affairs, to Chairman Kevin J. Martin, Commissioner Michael J. Copps, Commissioner Jonathan S. Adelstein, Commissioner Deborah Taylor Tate, Commissioner Robert M. McDowell, Federal Communications Commission, CC Docket No. 96-45, WC Docket No. 05-337 (filed Sept. 18, 2008) ("Embarq Comments") ((attaching "A Plan to Promote Broadband Deployment and Reform High-Cost Support Without Increasing Overall USF Levels") ("Embarq Proposal")) at Embarq Proposal at 17.

<sup>16</sup> Embarq Proposal at 11.

<sup>17</sup> Comments of CostQuest Associates, CC Docket Nos. 96-45, 96-98, 99-68, 99-200, 01-92, WC Docket Nos. 03-109, 04-36, 05-337, 06-122 (filed Nov. 26, 2008) ("CostQuest Comments") (attaching a white paper by James Stegeman, Steve Parsons, and Mike Wilson, "The Advanced Services Model: Proposal for a Competitive and Efficient Universal Service High-Cost Approach for a Broadband World" ("CostQuest Proposal")) at 4.

<sup>18</sup> CostQuest Comments at 4.

support distribution based on and favoring company ownership not a neutral descriptor such as population, density or US Census classification.”<sup>20</sup>

For high-cost support to be distributed in a more rational manner, Windstream recommends that the Commission consider how it can transform the non-rural mechanism into a price cap carrier universal service (“PC-USF”) mechanism. A PC-USF mechanism, like the existing non-rural mechanism, should determine eligibility and distribute support based on each wire center’s forward-looking costs and, as described below, should target funds to the highest cost wire centers, without regard to state boundaries. The PC-USF mechanism should be comprised of two types of carriers: (i) price cap carriers currently subject to the “non-rural” mechanism, and (ii) price cap carriers currently subject to the “rural” mechanism.<sup>21</sup> To create the new PC-USF mechanism, the Commission would only need to move the latter carriers over to the forward-looking mechanism used in the “non-rural” regime.<sup>22</sup>

The rural mechanism should continue to operate as it does now. The only change would be to its name: The rural mechanism could be renamed the rate-of-return carrier

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<sup>19</sup> *Id.* at 5.

<sup>20</sup> *Id.* at 5.

<sup>21</sup> A “price cap carrier” should be defined on a study area basis. This definition would mean that price cap study areas of a holding company would be placed under the price cap mechanism, but to the extent a holding company has some rate-of-return study areas (e.g., because the study area is average schedule), then those study areas would be treated under the rural mechanism. The Commission also may choose to allow non-rural rate-of-return carriers that are already under the forward-looking mechanism to remain subject to this mechanism.

<sup>22</sup> As suggested by Embarq and CostQuest, the Commission also could consider how to improve modeling techniques used for the expanded non-rural mechanism. *See* Embarq Comments (attaching “A Broadband and Carrier-of-Last-Resort Support (BCS) Solution: Term Sheet” (“Embarq Term Sheet”)) at Embarq Term Sheet at 5 (“Future support level assessments could be done (every five years) using a superior model (e.g., CostQuest’s model) or some other mechanism.”); CostQuest Proposal at 3 (“We propose that the ideal, modern cost model for use in a reformed universal service system is one that is designed to model forward-looking costs; all carrier types and all technologies would be modeled, and geographic granularity would be used.”). Any development of an enhanced model will take time and could occur at a later date, after further notice and comments.

universal service (“ROR-USF”) mechanism, since it would only fund rate-of-return carriers. The Commission can implement these reforms immediately, based on the record already developed in this docket and without substantial change to rules and systems.

Other than a name change and exclusion of price cap carriers, no immediate Commission action would be required to institute an ROR-USF mechanism. This mechanism could replace the rural mechanism in title, but not in function. Small, rural, rate-of-return companies, which currently receive support based on embedded costs, would continue to receive support based on their embedded costs. Such carriers would experience no change in their regulatory status. The only difference would be that the embedded cost mechanism – premised on the recovery of actual expenses plus a return on regulated investment – would be more rationally limited to rate-of-return carriers.

This proposal is consistent with recommendations made by Embarq. Embarq urges the Commission to distribute high-cost loop support based on two separate categories: price cap and rate-of return regulated carriers.<sup>23</sup> It argues that this proposal “would better target support in accordance with the actual needs of the companies and make implicit subsidies explicit for price cap carrier high-cost and rural properties.”<sup>24</sup> While it does not call for the “all-out elimination of the rural/non-rural distinction,” Embarq asserts that “if there is a reasonable distinction to be made regarding universal service it is a ‘price cap v. non-price cap’ distinction. The fundamental difference in business models between price cap and non-price cap carriers indicates that need for

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<sup>23</sup> Embarq Proposal at 18.

<sup>24</sup> *Id.* at 18.

explicit support differs as well, as should the mechanism designed to provide such support.”<sup>25</sup>

Indeed, placing price cap carriers under a single, forward-looking mechanism would benefit consumers by better aligning price cap carriers’ universal service mechanism with their efficient-cost, incentive-based regulatory regime. Already most price cap carriers are covered by the forward-looking mechanism. By applying a PC-USF mechanism to remaining price cap carriers, the Commission would eliminate the mismatch between carriers’ basing investment and pricing decisions on the competitive marketplace, while receiving universal service support based on their embedded costs. This new mechanism would benefit rural consumers by maximizing utility of high-cost support. As the Commission observed when it established the forward-looking mechanism, using forward-looking costs provides sufficient support without giving carriers an incentive to inflate costs or refrain from efficient cost-cutting.<sup>26</sup>

This improvement could be accomplished within the confines of the current size of the high-cost fund. As explained by Embarq,<sup>27</sup> eliminating identical support for wireless eligible telecommunications carriers (“ETCs”), in conjunction with other reforms proposed above, would provide funding needed for price cap carriers under the PC-USF mechanism. This mechanism could be capped at a level equal to the total

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<sup>25</sup> *Id.* at 17 (referencing Comments of AT&T Inc, WC Docket No. 05-337, CC Docket No. 96-45 (filed May 31, 2007) in support).

<sup>26</sup> *Federal-State Joint Board on Universal Service*, FCC 97-157, CC Docket No. 96-45, First Report and Order (rel. May 8, 1997) (“*Universal Service First Report and Order*”) at ¶¶ 224-26.

<sup>27</sup> Embarq Proposal at 21. CostQuest also proposes to combine various funds into a single mechanism. CostQuest Proposal at 18 (“We believe universal service policy should focus on funding and providing access “pipes” of sufficient capability to all Americans. That is, there should be a single mechanism (collapse ICLS, IAS, HCM, HCL, LSS) that support access in those areas of the country with higher cost access pipes . . . . These pipes can then be used to provide access to voice services alone (as the current fund provides) or access to broadband or IPTV, or other services, in the future.”).

amount currently distributed to price cap carriers under the rural mechanism, all carriers under the non-rural mechanism, and competitive ETCs for access charge replacement and Local Switching Support.<sup>28</sup> Carriers would be deemed eligible for the high-cost funds only if they served wire centers with costs exceeding the national cost benchmark, which could be set at a level that ensures price cap high-cost support does not exceed allocated funding. (This cost benchmark is discussed in further detail in Section II.B below.)

**B. THE COMMISSION SHOULD LOOK TO END ITS PRACTICE OF CONDITIONING ELIGIBILITY FOR HIGH-COST FUNDING ON AVERAGE STATE COSTS.**

Another key reason for the incoherence in the current universal service system is the Commission’s decision to determine eligibility for forward-looking support on the basis of average statewide costs.<sup>29</sup> Developed in 1999, the existing forward-looking support mechanism compares the average costs of providing basic telecommunications services in a state to a national cost benchmark, awards support for states with costs exceeding the national cost benchmark, and then targets that support within a qualifying state based on wire-center costs.<sup>30</sup> As a result, despite the many high-cost areas served throughout the nation, only a handful of states qualify for forward-looking support.

The Commission originally anticipated that the forward-looking support mechanism would “enable . . . rates for services supported by universal service to remain

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<sup>28</sup> Windstream provides further details about how to constrain the size of the Universal Service Fund in universal service comments that it submitted to the Commission last year. Windstream Comprehensive Reform Comments at 18-25.

<sup>29</sup> Since the discussion here is devoted to the forward-looking mechanism, any references to “statewide” costs are referring only to the entire area within a state that is served by carriers potentially eligible for support under the forward-looking mechanism.

<sup>30</sup> 47 C.F.R. § 54.309. See *Federal-State Joint Board on Universal Service*, FCC 99-306, CC Docket No. 96-45, Ninth Report & Order and Eighteenth Order on Reconsideration (rel. Nov. 2, 1999) (“*Universal Service Ninth Report & Order*”) (basing the forward-looking cost mechanism on statewide average costs).

affordable and reasonably comparable in all regions of the nation.”<sup>31</sup> Central to this expectation was the assumption that states would use their “authority . . . to achieve reasonable comparability of rates within [their] borders.”<sup>32</sup> As envisioned in 1999, a state would calculate the average cost to provide basic telecommunications services within its borders. A state then would collect money from all customers throughout the state, and distribute that money to specific wire centers where costs exceed the statewide benchmark for average costs. Federal funding would be needed only if average state costs exceeded the national benchmark established by the Commission.

When adopting this forward-looking mechanism, the Commission acknowledged that “the 1996 Act does not require states to establish explicit intrastate universal service support mechanisms.”<sup>33</sup> The Commission, nevertheless, seemed to find comfort in the Joint Board’s prediction that “the competitive forces that prompted Congress to favor explicit federal support mechanisms may also lead states to establish explicit state support mechanisms.”<sup>34</sup> The Commission further noted the Joint Board’s majority assessment that the “only impediment to statewide averaging” was “lack of sufficient time for state action,” and the agency addressed that outstanding concern by adopting a three-year transition period prior to implementing the new forward-looking mechanism.<sup>35</sup>

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<sup>31</sup> *Universal Service Ninth Report & Order* at ¶ 2.

<sup>32</sup> *Id.* at ¶ 48.

<sup>33</sup> *Id.* at ¶ 46, n.140.

<sup>34</sup> *Id.* at ¶ 46, n.140 (citing *Federal-State Joint Board on Universal Service*, FCC 98J-7, CC Docket No. 96-45, Second Recommended Decision (Jt. Bd., rel. Nov. 25, 1998) (“*Universal Service Second Recommended Decision*”) at ¶ 26).

<sup>35</sup> *Id.* at ¶ 47 (citing *Universal Service Second Recommended Decision* at ¶ 35). This conclusion was not endorsed by all members of the Joint Board. As noted by the Commission, “[s]everal members of the Joint Board . . . believed that the federal support methodology should not account for the states’ ability to support their own universal service needs because doing so would be inconsistent with the rest of the methodology proposed by the Joint Board.” *Universal Service Ninth Report & Order* at ¶ 64. See Dissenting Statement of Commissioner Harold Furchtgott-Roth, *Universal Service Second Recommended Decision* (“[T]he fact

Now, nearly a decade later, it is clear that the statewide averaging regime would need substantially more than a three-year transition period to be successful. Many states have failed to remove implicit subsidies and make them explicit. Consequently many carriers serving genuinely high-cost areas are grossly underfunded. States fail to provide support that reduce these carriers' costs to a level equal to statewide average costs. Then compounding the problem, the Commission assumes the carriers' states have rebalanced rates (even if they have not) and, in most cases, fails to provide adequate support on that basis. Currently the federal non-rural mechanism fails to provide any high-cost model support for high-cost wire centers operating in 40 states.

The Commission should focus on how it can correct these deficiencies in the universal service regime. As recognized by the Tenth Circuit in *Qwest I*, the Commission is "obligated to formulate its policies so as to achieve the goal of reasonable comparability. . . ." of rural and urban rates.<sup>36</sup> The Tenth Circuit found that Section 254 "requires a comparison of rural and urban areas, not states."<sup>37</sup> So while the current regime may have appeared "the best policy approach at [the] time,"<sup>38</sup> the Commission cannot stand by idly now that it is clear that the forward-looking mechanism is not

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that the Joint Board presupposes a State contribution level seems to conflict with other recommendations in the report. . . . In any event, I do not support either an explicit or an implicit federal requirement that States establish intrastate universal service funds."); Separate Statement of Commissioner Laska Schoenfelder Dissenting, *Universal Service Second Recommended Decision* ("This approach is inconsistent with language contained in the recommended decision that federal support may not be made contingent upon any actions taken, or not taken, by the states.").

<sup>36</sup> *Qwest Corporation v. FCC*, 258 F.3d 1191, 1200 (10th Cir. 2001) ("*Qwest I*").

<sup>37</sup> *Id.* at 1204.

<sup>38</sup> Even in 1999 the Commission "emphasize[d] that there may be several ways in which we could design the various components of the federal support mechanism consistent with section 254 . . . ." *Universal Service Ninth Report & Order* at ¶ 34. In particular, the Commission recognized "that averaging at the study area, UNE cost zone, or wire center levels would have the advantage of providing a more granular measure of support, and that granularity of support is a desirable goal in a competitive marketplace." *Id.* at ¶ 48.

achieving reasonable comparability of rural and urban costs and rates. To ensure states appropriately rebalance rates, the Tenth Circuit held that the Commission is “obligated to create some inducement,” such as “‘a carrot’ or a ‘stick,’” that ensures “states . . . assist in implementing the goals of universal service.”<sup>39</sup>

Accordingly, the Commission should seek to eliminate the practice of statewide averaging. Rather than determining eligibility at the statewide level and then targeting support to high-cost wire centers within qualifying states (as it does today), the Commission should in the first instance base universal service support for price cap carriers on the cost conditions solely of each wire center. The Commission should average costs of providing basic telecommunications services in individual wire centers to attain a national average cost per wire center. The national average cost per wire center then should be benchmarked to ensure spending falls within a predetermined budget. This approach would be similar to how the Commission, under the current rural high-cost loop program, calculates the national average cost per loop, and then adjusts the benchmark for support to ensure total funding is below the rural cap.<sup>40</sup> Wire centers that exceed the national cost benchmark for price cap support should receive support, while those below should not.

Applying a single cost benchmark to price cap wire centers would do a better job of producing “reasonable comparability of . . . carriers’ intrastate rates” – as the Commission originally intended.<sup>41</sup> Although constraining the size of the PC-USF fund

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<sup>39</sup> *Qwest I*, 258 F.3d at 1204.

<sup>40</sup> See 47 C.F.R. § 36.604 (describing how the rural growth factor is calculated).

<sup>41</sup> *Universal Service Ninth Report & Order* at ¶ 6.

might require a higher cost benchmark than that for the non-rural mechanism,<sup>42</sup> the new PC-USF mechanism would substantially improve how high-cost funds are distributed. A mechanism that provides support to all truly high-cost wire centers is far superior to one that provides too much support in a limited number of wire centers in a very few states.<sup>43</sup> Moreover, applying a nationwide cost benchmark would more clearly identify instances where state funding is needed to fill the cost gap between (i) the cost to provide service and (ii) the revenues a carrier reasonably can be expected to collect from its customers, as supplemented by any federal high-cost support.<sup>44</sup> Such information could be used to help implement the Tenth Circuit’s requirement that the Commission “develop mechanisms to induce adequate state action.”<sup>45</sup>

Windstream’s proposal to eliminate statewide averaging is consistent with recommendations made by Embarq and Qwest. Both urge the Commission to eliminate statewide averaging.<sup>46</sup> First, Embarq argues that directing high-cost support to an individual wire center, “a granular unit of analysis,” will “remove[] most of the problems in providing sufficient support that are caused by study-area averaging.”<sup>47</sup> “At a minimum, and in light of the existence of competition in cities and towns across the

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<sup>42</sup> The national average non-rural cost per line is \$21.43, and the benchmark is set at \$28.13, two standard deviations of the average. Federal Communications Commission, Hybrid Cost Proxy Model, *at* [www.fcc.gov/wcb/tapd/hcpm](http://www.fcc.gov/wcb/tapd/hcpm) (last modified Apr. 2009) (providing model results using line count data and support amounts).

<sup>43</sup> As previously noted, the existing non-rural mechanism penalizes states, and carriers depending upon their size or classification. This mechanism does not provide support to wire centers in 40 states.

<sup>44</sup> For example, if the nationwide cost benchmark was set at \$50.00 and the affordable benchmark was set at \$25.00, then there would be a gap for all the wire centers cost that exceed \$25.00 but are less than \$50.00. The responsibility for filling that gap would fall with the states. The federal mechanism would support all wire center cost exceeding \$50.00, but would provide zero support for wire centers whose cost were between \$50.00 and \$25.00.

<sup>45</sup> *Qwest I*, 258 F.3d at 1204.

<sup>46</sup> Embarq Proposal at 15; Qwest Proposal at 22.

<sup>47</sup> Embarq Proposal at 24.

country,” Embarq argues that “the Commission must divide targeted support areas in discrete enough sizes so that it can correctly identify and group exchanges that exhibit similar types of cost characteristics.”<sup>48</sup> Embarq adds that a “Cost Benchmark would be established at a level that would precisely distribute the approximate \$1 billion fund.”<sup>49</sup>

Second, Qwest asserts that basing support for non-rural carriers on statewide average costs has produced results where “the amount of support provided in a particular rural area may bear little relationship to the cost of providing service in that area. Rather, such support is determined largely by the proportion of relatively high-cost and low-cost lines in the state.”<sup>50</sup> Given the current state of affairs, Qwest concludes that “reliance on implicit subsidies is no longer workable and is inconsistent with the statutory mandate for reasonably comparable rates and services in rural and urban areas.”<sup>51</sup> It would prefer for the Commission “to target support to wire centers with costs that exceed a particular benchmark . . . ,” which it would set at 125 percent of the national average rate.<sup>52</sup>

Adherence to a budget would ensure that adopting recommendations to eliminate statewide averaging does not result in a large increase to the total size of the fund. As noted above, forward-looking support could be capped at a level equal to savings from CETC reforms, coupled with the total amount currently distributed to price cap carriers under the rural mechanism and all carriers under the non-rural mechanism. Carriers could be deemed eligible for these funds only if they served wire centers where costs

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<sup>48</sup> *Id.* at 13.

<sup>49</sup> *Id.* at 28.

<sup>50</sup> Letter from R. Steven Davis, Senior Vice President – Federal Relations, and Shirley Bloomfield, Senior Vice President – Public Policy, Qwest, to Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 96-45, WC Docket No. 05-337 (filed May 5, 2008) (attaching a “Proposal for Implementing the Tenth Circuit’s Remand in *Qwest II*”) (“Qwest Proposal”) at 23.

<sup>51</sup> *Id.* at 23.

exceed the national cost benchmark, which could be set at a level to ensure that high-cost support for price cap carriers does not exceed allocated funding.

**III. THE COMMISSION SHOULD ASSESS HOW IT COULD USE A RATE BENCHMARK TO ENSURE RATE PARITY AND EASE THE BURDEN ON THE HIGH-COST FUND.**

Disparate state regulatory regimes have caused consumer rates to vary substantially across the nation. Since the Communications Act was revised in 1996, some states have taken on the challenge of rebalancing rates, removing implicit support, adjusting intrastate intercarrier compensation, establishing explicit universal service funds, and ensuring that rates remain affordable. Many other states, however, have not. ILECs operating in the states that have not rebalanced rates must offer local service at artificially low prices, in most cases below cost, to satisfy the states' regulations.

This system effectively penalizes residents in states where rates are rebalanced. The benefit of low prices is concentrated with residents of states that have not rebalanced rates, while the federal surcharge that helps support these artificially low prices is spread across consumers nationwide. This rate regime is contrary to Congress's express desire for consumers in "all regions of the Nation" to have access to telecommunications and information services at "reasonably comparable" rates.<sup>53</sup>

To remedy this problem and respond to the Tenth Circuit's mandate that the support mechanism take "into account all of the factors that Congress identified in drafting the Act,"<sup>54</sup> Windstream calls upon the Commission to adopt a rate benchmark in the context of comprehensive high-cost universal service and intercarrier compensation

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<sup>52</sup> *Id.* at 22.

<sup>53</sup> 47 U.S.C. § 254(b)(3).

<sup>54</sup> *Qwest II*, 398 F.3d at 1237.

reforms. The agency could develop the benchmark on its own or use as a starting point the one jointly designed for the Early Adopter Fund by state commissions and industry participants in the intercarrier compensation reform docket.<sup>55</sup> In any event, use of a rate benchmark would ease the burden on the Universal Service Fund and reliance on intercarrier compensation to support universal service goals, as well as ensure equitable and sufficient support, as required by Section 254 of the Communications Act.<sup>56</sup>

If it elects to use a rate benchmark, the Commission also should develop a means to ensure, if necessary, that carriers have the ability to increase rates below the prescribed benchmark, so carriers are not harmed by states that are unwilling to do so on their own. The Commission could permit an end-user charge, such as a subscriber line charge, to be imposed pursuant to federal jurisdiction. Without this measure, intransigent states could otherwise effectively continue to force carriers to charge below-market and below-cost rates, and could preclude carriers from qualifying for federal universal service support.

**IV. IF IT INTENDS TO ENCOURAGE UNIVERSAL SERVICE RECIPIENTS TO DEPLOY MORE BROADBAND, THE COMMISSION FIRST MUST DETERMINE HOW IT CAN MAKE NEW FUNDS AVAILABLE TO SUPPORT BROADBAND OFFERINGS IN HIGH-COST AREAS.**

In recent years, private sector broadband providers, in aggregate, have invested tens of billions of dollars annually to connect much of the Nation to broadband services.<sup>57</sup> Yet a subset of consumers has not been able to benefit from this tremendous effort,

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<sup>55</sup> See Letter from State Commissions and Missoula Plan Supporters, to Marlene Dortch, FCC, CC Docket No. 01-92 (filed Jan. 30, 2007) (describing the benchmark designed for the Early Adopter Fund).

<sup>56</sup> 47 U.S.C. § 254(b).

<sup>57</sup> See Fawn Johnson, *Obama Official: Rural Networks Key To Internet Buildout*, WALL ST. J., Apr. 29, 2009 (citing USTelecom data indicating that private technology companies have invested an average of \$68 billion annually over the last several years in landline and wireless networks). See also Press Release, Leichtman Research Group, 5.4 Million Added to Broadband from Top Cable and Telephone Companies in 2008 at 1 (Mar. 6, 2009) (reporting that the twenty largest cable and telephone providers in the United States now account for nearly 67.7 million broadband subscribers).

because there is no rational economic case for deploying high-speed networks to consumers in very high-cost, low density areas. As the Commission well knows, communications network deployment involves sizable up-front costs, which must generally be recovered over time through recurring end-user charges. In many areas, up-front costs to deploy are simply prohibitive – either because the network operator cannot be certain of sufficient subscription rates to earn back its investment over time or because it could not earn back the investment at acceptable monthly rates, even assuming high and steady subscription rates. Indeed, the cost of deploying broadband to the 5 to 10 million U.S. households that continue to lack broadband access<sup>58</sup> far surpasses the \$7.2 billion that the Recovery Act allocated to *both* the NTIA and RUS broadband programs.<sup>59</sup>

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<sup>58</sup> This statistic is suggested by data reported by industry and federal officials. The Commission indicated that xDSL was available to 82% of the residential end-user premises where ILECs provided telephone service in 2007, and cable modem service was available to 96% of those premises where cable TV service was provided that same year. See INDUSTRY ANALYSIS AND TECHNOLOGY DIVISION, FEDERAL COMMUNICATIONS COMMISSION, HIGH-SPEED SERVICES FOR INTERNET ACCESS: STATUS AS OF DECEMBER 31, 2007 (rel. Jan. 16, 2009) at Table 14. Due to carrier of last resort obligations, one can infer that these data indicate that at least 82 percent of end users can access broadband, because ILECs are obligated to offer telephone service to all households. Extrapolating a nationwide broadband deployment from cable data is more difficult. Estimates of cable TV availability, or “homes passed,” have been controversial. See *Annual Assessment of the Status of Competition in the Market for the Delivery of Video Programming*, FCC 07-206, MB Docket No. 06-189, 13th Annual Report (rel. Jan. 16, 2009) at ¶ 28 (observing that the “calculation of cable availability . . . has been a subject of controversy, in part, because a variety of data sources have been used and no two data sources produce exactly the same estimate”). More on point, the cable industry estimates that cable-provided high-speed Internet is available to 92% of U.S. households. National Cable & Telecommunications Association, *Homes Passed by Cable High-Speed Internet Service 2003 - 2008*, at <http://www.ncta.com/Statistics.aspx> (last visited Apr. 30, 2009) (referencing data reported by SNL Kagan). If the universe of xDSL availability entirely overlapped the 92% of U.S. households where cable reportedly offers high-speed Internet access, these data would suggest that approximately 8.9 million households, out of a total of approximately 111 million U.S. households, lacked access to DSL- or cable-based broadband in 2007. See OFFICE OF POLICY DEVELOPMENT AND RESEARCH, U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, AND U.S. CENSUS BUREAU, U.S. DEPARTMENT OF COMMERCE, *AMERICAN HOUSING SURVEY FOR THE UNITED STATES: 2007* (rel. Sept. 2008) at Table 1A-1 (estimating the number of non-seasonal, occupied homes in the United States to be 110,692,000 in 2007).

<sup>59</sup> Multiple reports establish that it will cost a good deal more than \$7.2 billion to build out networks in unserved areas. See NATIONAL EXCHANGE CARRIER ASSOCIATION, *THE PACKET TRAIN NEEDS TO STOP AT EVERY DOOR: EXECUTIVE SUMMARY* at 3 (2006), [https://www.neca.org/portal/server.pt/gateway/PTARGS\\_0\\_0\\_307\\_206\\_0\\_43/https%3B/prodnet.www.neca.org/source/NECA\\_Publications\\_4729.asp](https://www.neca.org/portal/server.pt/gateway/PTARGS_0_0_307_206_0_43/https%3B/prodnet.www.neca.org/source/NECA_Publications_4729.asp) (estimating a cost of \$11.9 billion to extend broadband service at 8 Mbps speeds to just 5.9 million of the nation’s rural lines); BALHOFF & WILLIAMS, LLC, *AMERICA AT A CROSSROAD: UNDERSTANDING THE CHALLENGE OF BROADBAND IN RURAL AMERICA* at 4 (2009),

Ideally any additional federal funds to offset these high deployment costs will be drawn from general revenues – rather than universal service dollars. This approach is consistent with how Congress funded American Reinvestment and Recovery Act broadband initiatives.<sup>60</sup> Funding from general taxes is especially appropriate in the context of broadband, given the widespread benefits from increased broadband usage.<sup>61</sup> Projects that deploy broadband to unserved areas will bring more individuals online, thereby maximizing the network effects of the Internet and facilitating greater use of health care, education, and business resources offered over the World Wide Web.

If it nevertheless intends to use federal universal service to spur further broadband deployment, the Commission, in any instance, should never condition receipt of *existing* universal service funds on a carrier's ability to extend its broadband offerings.<sup>62</sup> Setting an arbitrary broadband deployment threshold may cause individual wire centers to be underfunded due to specific deployment costs at the individual wire center level. Imposing this sort of condition could prevent carriers that have not yet been able to deploy broadband through an area from being eligible to receive universal service – as the cost of becoming sufficiently broadband capable could easily outweigh associated universal service support.

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<http://www.balhoffrowe.com/pdf/America%20at%20a%20Crossroad.pdf> (estimating that “the network investment to achieve 1.5 megabits per second broadband services provided over already-installed telephone plant in unserved rural regions is estimated to be \$2,000 to \$3,000 for each unserved home,” \$4,000 to \$6,000 per line for 6 Mbps, and \$8,000 to \$12,000 per line for 12 Mbps).

<sup>60</sup> American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, 123 Stat. 115 (2009).

<sup>61</sup> See Connected Nation, The Impact of Stimulating Broadband Nationally at 1 (Feb. 21, 2008) (finding that “just a seven percentage point increase in [national] broadband adoption could result in . . . \$134 billion per year in direct economic impact”).

<sup>62</sup> See *Intercarrier Compensation for ISP-Bound Traffic*, Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, FCC 08-262, App. A & App. C (rel. Nov. 5, 2008) (including a proposal for conditioning support on offering broadband Internet access service).

By effectively forcing some carriers to forgo high-cost funding, the Commission would not promote further broadband deployment. Indeed, to the contrary, placing a broadband condition on high-cost support likely would inhibit further deployment. Currently carriers may be able to use high-cost funds to help defray substantial costs of shortening loops and otherwise upgrading dual-use plant. Carriers subject to a new broadband obligation, however, might have to curtail further broadband deployment without continued access to this funding. Carriers best able to assume a new broadband condition would be those that have already ubiquitously deployed their networks.<sup>63</sup>

The Commission also should not give any credit to the false premise that voice merely is another application that could easily be supported over a broadband network. To support voice, a broadband network must be transformed into an all-IP network. This augmentation is an expensive proposition: To deploy an interconnected Voice over Internet Protocol (“VoIP”) service, Windstream expects it would need to spend hundreds of millions *above and beyond* capital and operating expenses necessary to support ubiquitous broadband.<sup>64</sup> Thus, many carriers offering interconnected VoIP would need substantial governmental support in addition to what they currently receive from the Universal Service Fund, or what they would require to offer ubiquitous broadband.

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<sup>63</sup> Likely many of these carriers would have already used universal service funds to help defray the costs of providing ubiquitous broadband coverage.

<sup>64</sup> See Letter from Eric Einhorn, Windstream, to Marlene H. Dortch, Secretary, FCC, CC Docket Nos. 96-45 and 01-92; WC Docket Nos. 99-68, 05-337, 06-122, 07-135, and 08-152 (Oct. 27, 2008) at 3 (“Consistent with common practice for mid-sized price cap carriers, Windstream installs broadband ports sufficient to support the percentage of its customers forecasted to subscribe to its broadband service (as opposed to competitive cable, wireless, satellite, or other broadband service offerings) in the reasonably foreseeable future. This practice sufficiently meets Windstream customers’ broadband demands. The use of softswitch technology for voice traffic, however, would require all voice lines to be supported by broadband ports. Thus, in areas where it already offers broadband, Windstream would need to augment existing broadband facilities with additional DSLAMs and other equipment. These upgrades likely would cause Windstream to spend about the same amount to deploy additional broadband facilities to its remaining access lines as it did for existing broadband-capable access lines – or in the aggregate, hundreds of millions of dollars.”).

If the Commission intends to use the high-cost program to support both voice and broadband, agency officials must explore how they can make new universal service funding available expressly for broadband. Such support will have the greatest impact if allocated initially in the form of grants. Grants hold the best promise of altering the economic barriers blocking new investment in remote and costly areas. They can fundamentally alter the economics of serving an area by offsetting up-front costs and blunting risks faced by investors, permitting a broadband provider to deploy and earn sufficient returns at affordable rates collected from a smaller customer base.

Based upon Windstream's experience, using grants to shorten long copper loops would be a particularly cost-effective way to reach consumers who lack access to core broadband services. Capital expenditures required to install fiber facilities and digital loop carrier systems along rural roads usually are not as great as expenditures required for other deployment initiatives – such as building out the middle mile or installing redundant networks – because projects to shorten loops are able to leverage existing infrastructure in a meaningful way.<sup>65</sup> Thus, this approach would allow the government to stretch its budget further – reaching more consumers who are unable to take advantage of remote conferencing, online banking, and distance education opportunities.

## **V. CONCLUSION**

Windstream urges the Commission to use this remand proceeding as a means to producing meaningful, comprehensive universal service reforms. The Commission should not delay in adopting measures that will target federal funds directly to individual high-cost areas, and ensure that rates in those areas are sufficiently, but not overly,

subsidized. Such reforms will ensure high-cost support is sufficient to guarantee reasonable comparability between rural and urban telecommunications rates, as directed by the Communications Act and reaffirmed by the Tenth Circuit's remand order.

Respectfully submitted,

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<sup>65</sup> Transport, or “middle mile,” expenses also may be addressed with ongoing operational support that enables broadband providers to lease transport. Such support, however, is not well suited to one-time-only capital funding.