

Executive Summary

The ACA supports the consideration of a Universal Service mechanism to fund broadband as part of the National Broadband Plan; one that is competitively and technologically neutral and is precisely targeted to users that lack access in areas that are unserved or underserved. Over the past several months ACA and its diverse membership have worked diligently to develop a proposal that evolves and reforms Universal Service to support broadband in an efficient, non-discriminatory manner where 1) one industry segment is not favored over another and 2) one technology is not favored over another.

The ACA proposal looks to correct problems with the current Universal Service program and target the funding to where it is actually needed. An overriding guide in developing the ACA proposal is the fact that the consumer is the ultimate contributor to Universal Service. Thus the ACA plan is tailored to efficient funding where truly needed. The main components of the ACA proposal are:

1. Cap the Entire Universal Service Fund and the High Cost Portion of the Fund at 12/31/09 Level;
2. Create a New Broadband Fund for Unserved and Underserved Areas (Last Mile Wireline & Wireless, and Middle Mile);
 - a. The amount of funding for the Broadband Fund would be the difference between the capped high-cost fund amount as of 12/31/09 and the level of the high cost fund as it is reduced through the mechanisms described in Section 3.
 - b. Funding would be awarded separately for last-mile wireline and wireless providers and for middle-mile providers with the FCC determining the appropriate allocation. Funding would be awarded on a first-come, first-served basis, with unserved areas being funded first; if multiple last-mile providers seek capital funding in unserved areas or multiple middle-mile providers seek capital funding, reverse auctions (or another neutral selection method) would be used.

- c. For unserved areas, last-mile funding would be in the form of (1) capital grants for the construction of infrastructure to provide eligible broadband services (unless such funding has been obtained from other government programs), and (2) operating funds (\$X/line/month) conditioned on serving the customer. The amount of the operating fund subsidy would be calculated based on the cost of providing broadband service (either wireline or wireless) in the unserved area versus the average nationwide cost of providing broadband service. For purposes of administrability, the FCC would calculate the cost by examining costs in representative (census block) areas which then could be linked to the level of density or other factors closely-linked to costs.
 - d. For households in underserved areas, last-mile funding would be in the form of operating funds (\$X/line/month) conditioned on serving the customer. The amount of the operating fund subsidy would be calculated based on the cost of providing broadband service (either wireline or wireless) in the underserved area versus the average nationwide cost of providing broadband service. For purposes of administrability, the FCC would calculate the cost by examining costs in representative (census block) areas, which would be linked to the level of density.
 - e. For middle-mile infrastructure for unserved and underserved areas, funding would be in the form of capital grants for the construction of infrastructure to provide eligible broadband services.
 - f. The FCC would evaluate operating support at regular intervals to determine the level of such support and whether such support continues to be necessary.
 - g. The FCC would make additional and separate funds available for low-income households to subscribe to broadband service.
3. Transition the High Cost (Voice) Fund Using Savings to Fund Broadband;
- a. Provide Smaller Eligible Telecommunications Carriers (“ETCs”) with continuing support for their provision of traditional voice service and eliminate funding where competition is present.
 - b. Current wireline ETCs (Eligible Telecom Carrier) with fewer than 100,000 access lines would continue to draw from the fund as they draw today (by area) for the provision of voice service unless they choose to access funding from the new Broadband Fund to serve that area (other than access to the fund for purposes of funding middle-mile infrastructure), in which case the funding mechanism in the new Fund replaces the current mechanism.
 - c. Current wireline ETCs with more than 100,000 access lines would draw from the fund based on the “current high cost differential” per access line

multiplied by the number of voice access lines in service annually. No such wireline ETC would draw from the fund for an access line if (1) the user can obtain voice service from another wireline provider who is able to serve the user without drawing from the fund, (2) the state regulator has deregulated the wireline ETC's provision of voice telephone service for the user, or (3) the wireline ETC accesses funding from the Broadband Fund to serve the user (other than access to the fund for purposes of funding middle-mile infrastructure).

- d. A wireline competitive ETC ("CETC") would draw from the fund based on the number of voice access lines served, except that (1) no funds would be awarded if another competitive wireline provider was able to serve the same customer without drawing from the fund, and (2) no funds would be awarded if the CETC accesses funding from the Broadband Fund to serve that customer (other than access to the fund for purposes of funding middle-mile infrastructure).
 - e. A wireless competitive ETC ("CETC") would draw from the fund based on the number of voice access lines served, except that (1) no funds would be awarded if another wireless provider was able to serve the same customer without drawing from the fund, and (2) no funds would be awarded if the CETC accesses funding from the Broadband Fund to serve that customer (other than access to the fund for purposes of funding middle mile infrastructure).
 - f. No high-cost voice funds would be provided to areas or customers not currently receiving funding.
 - g. Maintain the CETC "interim" cap during the transition to use of the Broadband Fund. No new funding would be awarded to a CETC entering a new service area after 12/31/09.
4. Contribution Methodology
- a. Move from the current contribution mechanism of placing an assessment on interstate telecommunications revenues to hybrid numbers/connections based approach -- with a cap on revenue at current level of total USF.

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I. Introduction

The American Cable Association (“ACA”) files these Comments in response to the Commission’s Public Notice for Comments on the Role of the Universal Service Fund and Intercarrier Compensation in the National Broadband Plan.¹ The ACA, given its diverse membership with a long history of bringing broadband services to rural areas, is uniquely qualified to assist the Commission.

The ACA brings a unique perspective because it is a microcosm of the telecom and broadband universe. Small markets and rural areas across the country receive video services from nearly 900 small and medium-sized independent operators represented by the ACA. More than half of ACA’s members serve fewer than 2,000 subscribers. ACA’s diverse membership is comprised of traditional cable and phone providers who operate as corporations, cooperatives, and municipalities, all of whom provide video services, and most of whom deliver other traditional and advanced services, including high speed Internet access and VoIP services to more than 7 million households and businesses.

Not only does ACA membership cover the gambit of the telecommunications industry, but with specific regard to the Universal Service fund, the ACA membership includes:

- Cable operators who provide high speed broadband service in rural areas who do not draw from the fund;
- Cable operators who provide high speed broadband and VOIP services in rural areas and contribute to the fund but do not draw from the fund;

¹ Public Notice, *Comments Sought on the Role of the Universal Service Fund and Intercarrier Compensation in the National Broadband Plan*, GN Dockets 09-47, 09-51, 09-137 released Nov. 13, 2009.

- Cable operators who provide high speed data and VoIP services in metropolitan non-high cost areas who contribute but do not draw from the fund;
- Incumbent telephone operators in rural areas who also provide video service and high speed broadband services and currently draw from the fund as eligible telecommunication carriers;
- Competitive telephone operators who also provide video service and high speed broadband service and currently draw from the fund as competitive eligible telecommunications carriers, both as for wireline and wireless services.

The diverse make-up of the ACA membership necessitated a balanced approach to developing a position on Universal Service that required a weighing of different interests through numerous discussions, committee work and one-on-one interviews with members who provide service as cable, phone, and even wireless operators, and who contribute and may receive funding from the Universal Service fund in all sorts of various combinations. After months of hard work, the ACA has developed a proposal to reform and evolve Universal Service for the broadband era in an efficient, competitively neutral manner that best serves the consumer, who ultimately funds Universal Service.

The result is a plan that evolves and reforms Universal Service to support broadband in an efficient non-discriminatory manner where 1) one industry segment is not favored over another and 2) one technology is not favored over another. ACA supports the consideration of a Universal Service mechanism to fund broadband but only if it is competitively and technologically neutral and is precisely targeted to users that lack access in areas that are unserved or underserved.

Evolving the current Universal Service fund into an efficient funding mechanism to provide broadband expansion where needed, without unnecessarily impacting consumers, necessarily involves reviewing the problems with the current program,

reviewing the interests of providers and coming up with a plan that treats all providers fairly, while assuring that the goal of expanding broadband to areas where it is not currently available is achieved over time. As more fully described herein the ACA proposal takes into account all of these factors.

The ACA proposal addresses concerns raised by the Joint Board, Congress and industry groups with the current Universal Service funds. The plan benefits the consumer who is the ultimate funding source for Universal Service by capping the Universal Service fund and High Cost fund at the December 31, 2009 funding level and targeting funding to where it is needed. The plan suggests changes which will allow funds to be reoriented to broadband services through a more targeted funding approach, thus providing a fund for broadband expansion. At the same time, the plan provides small Eligible Telecommunications Carriers with continuing support for their traditional voice services and provides continued support in other instances where it is truly needed. Finally, the proposal supports a move from the current contribution methodology to a hybrid numbers/connections based approach, again with revenue capped at current Universal Service levels. At the very least the contribution methodology needs to be changed to address the discriminatory and arbitrary VoIP safe harbor calculation.

In considering a Universal Service mechanism for the National Broadband Plan the Commission should be primarily guided by the observation noted by the Joint Board that “it is consumers who must pay universal service contributions.”² This was a

² *In re High-Cost Universal Service Support*, 22 FCC Rcd 20477, ¶2 (Nov. 20, 2007) (“Joint Board Nov. 2007 Recommended Decision”)

primary guiding factor kept in mind by the ACA in developing its proposal and an extremely important part of any Universal Service Fund (“USF”) analysis.

II. USF Issues and Concerns

Any effort to have the universal service funding mechanism evolve into a fund to support advancement of broadband service must be accompanied by serious reform to eliminate existing inefficiencies and ineffectiveness and to do so in a competitively and technologically neutral manner. The “new” plan for the USF should focus, consistent with the statute and sound policy, on the development and availability of broadband services, with continued allowances during the transition in demonstrated circumstances for support for voice services, albeit on a much more limited scale than is the case today. Before addressing its proposals, the ACA discusses major issues and concerns with the current program.

A. The USF Funds Voice Service in an Era Where Availability of Broadband Services Has Become the Primary Concern

In the mid-1990s, the Universal Service Fund correctly focused on expansion of voice services to all Americans. By March 2009, the Commission reported that over 95% of all Americans have access to voice services.³ Tens of millions of consumers today take voice services from competitive providers, including CLECs and cable operators, and millions of consumers have decided that they do not need voice wireline services at all, choosing wireless alternatives.

It is clear and commonly held that, today, more than a decade later, the focus should be on making broadband services available to all citizens and businesses in the

³ Telephone Subscribership in the United States, Table 1 (rel. March 2009).

United States. The Broadband Technologies Opportunity Program administered by the National Telecommunications and Information Administration (“NTIA”) and the Broadband Initiatives Program administered by the Rural Utilities Service (“RUS”) under the American Reinvestment and Recovery Act of 2009 are a good, but limited first step in making broadband services available to more persons in the nation. As already indicated in the status reports of the National Broadband Plan staff, there are a significant number of housing units that either lack access to any broadband or do not have access to broadband of a sufficient speed.⁴ The Commission now has the opportunity to fill that gap as it reevaluates the primary thrust of universal service support in a broadband era and whether there should be a new broadband funding mechanism. The USF should be redirected to support broadband development as its primary focus while continuing to support making available voice services in those limited, insular areas where it is not available today.

B. The Fund Distorts the Marketplace and is Not Available for Many Competitive Providers

The current USF supports some but not all rivals in the marketplace and thus inhibits competition. For example, in 2006, the Commission introduced requirements that interconnected VoIP providers contribute to the fund. Although the VoIP providers had no opportunity, as non-telecommunications carriers, to obtain distributions from the fund, these providers, including many ACA members, have had to help subsidize the local voice telephone services of the incumbent local carriers at the same time that

⁴ See, *Broadband Gaps*, Presentation of the National Broadband Plan Staff, FCC November Commission Open Meeting, November 18, 2009 at 8, available at: http://www.fcc.gov/openmeetings/2009_11_18-ocm.html.

these providers began to introduce competition and win customers away from the incumbents.

Further, last year, the Commission made the decision to adopt a cap on high-cost support received by competitive Eligible Telecommunications Carriers (“CETCs”).⁵ While the Commission tried to justify this decision as necessary to “reign in the explosive growth” of the fund, the limitation of extending the cap only to competitive carriers was inexplicable. This sort of targeted regulatory fiat makes clear that the fund is not competitively or technologically neutral.

The non-competitively neutral structure of the USF is problematic. It creates competitive imbalances, as traditional incumbent carriers are most likely to be the entities receiving support. Although some cable operators have succeeded in achieving Eligible Telecommunications Carrier (“ETC”) status, the burdens and delays associated with the process, the continued uncertain regulatory status of interconnected VoIP providers, and the cap on funding for CETCs, has allowed incumbent LECs to be disproportionately favored, even where they face competition. Without regulatory mechanisms forcing carriers benefiting from the fund to wean themselves from support when competition has been introduced, the fund will remain inefficient and lack competitive and technological neutrality.

The current rules governing the USF do not account for changed circumstances. Frequently, cable operators and other facilities based providers are providing services in non-urban areas without USF support in competition with incumbent carriers receiving support. The presence of competition strongly suggests that support for the

⁵ *High Cost Universal Service Support*, 23 FCC Rcd 8834 (2008) (“CETC Cap Order”).

incumbent's services are no longer necessary to ensure that rates for the services are at affordable and reasonably comparable rates.⁶ The rules inadequately address the changed conditions from when USF funds were first made available to incumbents in these areas, focusing woodenly on the high costs of incumbent carriers rather than the rates for the services they provide, hampering the success of the incipient competition. In other words, support is still allocated based on a presumption of need rather than a demonstration that USF funding is needed to ensure affordable and reasonably comparable rates for consumers.

C. The Size of the Fund Has Grown Substantially, Requiring Substantial Increases in Assessments on Contributors Per Revenue Dollar

With advancements in technology and competition, the need for universal service awards should be declining for voice services. Unfortunately, these developments have been accompanied by escalating demands for support due to deficiencies in the Commission's rules which have not evolved with the marketplace. Indeed, as will be discussed further in the next section, all components of the USF have grown substantially over the past decade, and the current contribution factor stands at over 12% on interstate telecommunications revenues, more than double what it was in 1997 despite the inclusion of interconnected VoIP revenues, conference calling services, and others in the contribution base. The Congressional Budget Office has warned that the fund will become increasingly bloated unless significant changes are made.⁷ The

⁶ See 47 U.S.C. § 254(b)(1) ("Quality services should be available at just, reasonable, and affordable rates") and § 254(b)(3) ("reasonable comparability").

⁷ *Factors That May Increase Future Spending from the Universal Service Fund: A CBO Paper at 1* (Congressional Budget Office, June 2006).

continuing expansion of the fund and the increasing burden on ratepayers of interstate telecommunications actually serves to undermine the goal of making services available ubiquitously at affordable prices.

D. Administration of the Fund Often is Inadequate and Has Become too Complex and Costly

The USF has always been an awkward government program. It is the vestige of an industry-operated subsidy program developed for a monopoly era. It is off-budget, eschewing the normal federal accountability mechanisms. It splits management between the Commission and a non-government entity. The unusual nature of the program has become even more evident as it is forced to address issues in an industry that has become more diverse, complex, and dynamic. As a result of these factors, there are real questions about the program's effectiveness, inefficiency and overall operations. These concerns have been tracked by the U.S. General Accountability Office ("GAO"), which three times over the past five years has criticized the management of the USF:

The USF faces a myriad of management challenges. USF disbursements operate outside of the annual appropriations process, and a nongovernmental entity runs the day-to-day operations of the USF. In several reports, we have identified weaknesses with the management and oversight of the USF, including a lack of performance goals and measures and weak internal controls. Because of these weaknesses, it is not clear whether the USF is achieving the desired outcomes in an effective and

cost-efficient manner.⁸

There are numerous examples of the program's administrative shortcomings. For instance, the ability of CETCs to obtain funding is at the mercy of a complex and uncertain process often plagued by delays. Moreover, CETCs must wait until the end of the year to discern how much support they will receive because the cap mechanism applicable to them dictates, on a state-by-state basis, how much funding will go to CETCs as a whole based on the number of requests received and the amount of USF funding allocated for CETCs available in that state.⁹

Further, the burdens placed on ETCs to facilitate oversight are excessively complex and costly. The potential for USF audits imposes considerable recordkeeping requirements on all ETCs, absorbing considerable expense and human resources that detract from the provision of services to consumers. USF distribution audits remain an extremely invasive and time consuming process, and numerous carriers and interested parties have pushed for reform to streamline the recordkeeping requirements and other processes.

Similarly, on the contribution side, where assessments remain based on interstate and, in most cases, international telecommunications end user revenues, carriers and other providers of telecommunications constantly face numerous complicated regulations and regulatory burdens to ensure they are complying with the USF regime. The Commission's instructions for the Form 499A, the basis for contributions and the focus of compliance audits, seemingly grow with each passing

⁸ See, <http://www.gao.gov/highrisk/agency/fcc/managing-and-overseeing-universal-service.php>.

⁹ *CETC Cap Order*, 23 FCC Rcd at 8847.

year, reflecting the complexity and the growing commitment of resources contributors face. Providers must obtain and maintain reseller certificates in many situations if they offer wholesale telecommunications and regularly deal with uncertain line-drawing in today's ever changing marketplace where telecommunications services are increasingly frequently bundled with non-telecommunications products.

In sum, the USF program is badly in need of reform, which must be undertaken in conjunction with the transition to support for broadband advancement. The following sections set forth the ACA's proposals to achieve these objectives.

III. Amount of Universal Service Funding: Cap the Fund at 2009 Levels

A. Introduction: Factors Driving the Cap and Sufficiency for Broadband Deployment

The first inquiry in the Public Notice addresses the issue of the size of the USF and its various components and the sufficiency of the fund to “advance the goal of universalization of broadband.” The diverse membership of the ACA –many of whom contribute to the fund and some of whom draw – wrestled with this same inquiry in fashioning a complete reform plan for USF, which includes new support for broadband. They concluded, for the following reasons, that both the fund and the components should be capped at year end 2009 levels and that this would leave sufficient funding for broadband advancement:

- First, because competition has developed in many areas where entities currently receive funding – and might receive funding for broadband – funding in such areas is no longer required or, at least, can be more targeted.
- Second, evidence over the past decade indicates that entities drawing from the fund have strong incentives to maximize their individual take and that, absent a hard cap, the Commission is not

likely to limit (or will have a very difficult time limiting) the collective distribution.

- Third, the funds have increased in size so significantly over the past decade, and there is evidence that the funds are not operated efficiently.
- Fourth, the “tax” on telephone consumers to pay for the fund has increased dramatically. Because of the off-budget nature of the program and the ease with which this “tax” has been increased, this will be a continuing concern even if the contribution base is broadened or the methodology altered.
- Fifth, support for broadband advancement can in many instances be in the form of capital funding for infrastructure deployment, which is to ensure that consumers in unserved areas have last mile and middle mile broadband networks which they can access. Such support has at least two advantages. First, the deployment of new network facilities will decrease operating expenses significantly, thus lowering ongoing subsidies. Second, capital funding does not need to be a grant but rather can be in the form of alternative financial instruments (*e.g.* loan guarantees) that can leverage USF resources, thus extending the resources of the fund.

When taken in combination, these factors led the ACA members to conclude that the fund and the components should be capped and that, even with the cap, there should be sufficient funding available for broadband advancement. The sections that follow discuss the ACA’s rationale for the cap and its sufficiency for broadband support in greater detail.

B. Greater Competition Means Funding Can Be More Targeted

The USF was established with several goals, including ensuring that low income consumers and consumers in rural or high cost areas have access to telecommunications services and rates that are reasonably comparable to services and rates offered in urban areas.¹⁰ The USF also seeks to provide schools, libraries and

¹⁰ 47 U.S.C. § 254(b)(3).

health care providers with access to advanced telecommunications services.¹¹ All of these are laudable objectives, but the question the Commission must deal with is whether these goals can be achieved without support from the USF. Because of the development of competition in so many areas of the country over the past decade, the answer is clearly “yes.” Most residential consumers of both voice and broadband service and many in rural areas have a choice of facilities-based providers. Ironically, this conclusion is buttressed by the growth in competitors drawing from the fund to serve the same areas and customers, and the Commission’s own decision to cap the amount CETCs draw from the fund.

The FCC’s most recent report on local telephone competition found that, as of June 30, 2008, competitors accounted for approximately 20 percent (30 million) of the nation’s access lines, of which 9.4 million were provided over coaxial cable connections. Most of these cable connections were provided to residential customers. In addition, competitors served customers in 82 percent of the nation’s Zip Codes, which contain about 97 percent of the nation’s households.¹² These statistics are echoed and elaborated upon in the recently filed Petition for Rulemaking by the National Cable & Telecommunications Association, which determined that cable operators currently provide voice service to between 74 and 84 percent of the households overall and 43 percent of the households (6.6 million) in rural LEC study areas and that cable voice service is available in most rural study areas, and, in 21 percent of the study areas,

¹¹ 47 U.S.C. § 254(b)(4).

¹² *Local Telephone Competition: Status as of June 30, 2008*, Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, July 2009, at 2-3, available at: http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-292193A1.pdf.

coverage exceeds 50 percent.¹³ It is thus evident that the competitive landscape has developed considerably since 1996 when Congress enacted the new universal service statute in the Telecommunications Act and a decade ago when the Commission implemented this law. This reality needs to be taken into account as the Commission reorients the USF for the broadband era.

As further evidence of the need to reform the USF, it is worthwhile to examine the “counter-intuitive” effect the development of competition has had on the overall size of the fund. There is little doubt that the dramatic growth of the USF has been exacerbated by the unnecessary distribution of funds to carriers that apparently do not need support. The entry of competitors in a market has always been seen as a means of increasing consumer choice and potentially decreasing the price for those services. Unfortunately, many competitive carriers have chosen to access the USF program by seeking USF support even though the carriers previously provided service in the same market without utilizing universal service support.¹⁴ The fact that carriers are able to provide services without relying on USF support shows that the continued distribution of USF high-cost support in these situations is not necessary to ensure consumers have access to telecommunications services. Even the Federal-State Joint Board (“Joint Board”) has stated that it “is no longer in the public interest to use federal universal service support to subsidize competition and build duplicate networks in high-cost

¹³ Petition for Rulemaking, Reducing Universal Service Support In Geographic Areas That are Experiencing Unsupported Facilities-Based Competition, RM -- , National Cable & Telecommunications Association, Nov. 5, 2009, at 6-7 and n.17. (“NCTA Petition”)

¹⁴ See, e.g., Comments of the Independent Telephone and Telecommunications Alliance, WC Dkt. 05-337, CC Dkt. 96-45 at 8 (June 6, 2007); Comments of CenturyTel, Inc., WC Dkt. 05-337, CC Dkt. 96-45 at 4 (June 6, 2007)

areas.”¹⁵ The Commission should reduce the size of the USF by limiting or denying support to a carrier where another carrier is willing to provide the same services in the same area without USF support.

C. USF Support Has Burgeoned and is Inefficient, Placing a Burden on Consumers

In 2007, the Joint Board warned the Commission that the growth of the USF, and in particular, the high-cost fund threatened the stability of the USF program and urged the Commission to take measures to rein in the size of the fund.¹⁶ While the Commission did take the first step toward stability by imposing an interim cap on CETC support under the program, it is clear that more must be done.¹⁷ Since the Joint Board first raised the alarm, the high-cost fund has continued to grow, and consumers have continued to bear a greater percentage of the costs of the USF program. In 2000, the high-cost program support fund was \$2.2 billion, and, by 2008, the amount had doubled to \$4.4 billion.¹⁸ While consumers contributed to the fund at rates of 5.5% to 5.8% in 2000, by the 4th quarter of this year the contribution rate climbed to 12.3%,¹⁹ and it

¹⁵ *Joint Board November 2007 Recommended Decision*, ¶ 35.

¹⁶ *In re: High-Cost Universal Service Support; Federal-State Joint Board on Universal Service*, 22 FCC Rcd 8998, ¶¶ NN (2007).

¹⁷ *In re: High-Cost Universal Service Support*, 23 FCC Rcd 8834 (2008) (“CETC Cap Order”).

¹⁸ Federal and State Staff for the Federal-State Joint Board on Universal Service; *Universal Service Monitoring Report*, CC Docket No. 98-202, Table 3.1 (2002) (“2002 USF Report”); Federal and State Staff for the Federal-State Joint Board on Universal Service; *Universal Service Monitoring Report*, CC Docket No. 98-202 (2008) (“2008 USF Report”).

¹⁹ See Public Notice: Proposed First Quarter 2000 Universal Service Contribution Factor, DA 99-2780 (CCB Dec. 10, 1999); Public Notice: Proposed Third Quarter 2000 Universal Service Contribution Factor, DA 00-1272 (CCB June 9, 2000); Public Notice: Proposed Fourth Quarter 2009 Universal Service Contribution Factor, DA 09-2042 (OMD Sept. 14, 2009) (“Fourth Quarter 2009 Contribution Notice”).

appears that the rate for the next quarter will be above 14%.²⁰

Although much of the industry focuses on the high-cost program as the largest and fastest-growing component of the USF, the other programs supported by the USF continue to grow and impact the overall size of the fund. In 2000, funding for Low Income consumers was \$519 million and had grown to \$824 million by 2007.²¹ Similarly, in 2000, the Commission committed to providing \$2 billion in funding for the Schools and Libraries (“E-Rate”) program and this commitment level had increased to \$2.4 billion in 2007.²²

In addition to continuously-increasing funding and support levels, as discussed earlier in these comments, the USF program is hampered by inefficient spending as well as waste and abuse of the program funds. The unnecessary and continued growth of the USF and waste of USF funds harms the very consumers it was intended to benefit.

1. The Size of the Current USF Imposes Significant Burdens on Consumers

While the goals of the USF program are laudable, the continued growth of the USF has resulted in presumably unforeseen burdens on consumers. Over a nine year period from 2000 to 2008, the USF high-cost fund grew from \$2.2 billion²³ to \$4.4

²⁰ See, e.g. Prepared Testimony of Verizon Senior Vice President Peter B. Davidson U.S. House of Representatives Committee on Energy and Commerce, Subcommittee on Communications, Technology, and the Internet, “Universal Service Reform Act of 2009” Tuesday, Nov. 17, 2009 at 2. (“Statement of Peter Davidson”)

²¹ 2008 USF Report, Table 2.2.

²² 2008 USF Report, Table 4.1.

²³ Federal and State Staff for the Federal-State Joint Board on Universal Service; *Universal Service Monitoring Report*, CC Docket No. 98-202, Table 3.1 (2002) (“2002 USF Report”).

billion²⁴ and the burden on consumers increased as well, with consumers contributing at factors ranging from 5.7% to 11.4%.²⁵ In 2007, support for the high-cost program was over \$4.2 billion, with CETCs receiving \$1.2 billion, and carriers typically recovered USF contributions from their subscribers at rates ranging from a low of 9.7% to a high of 11.7% of the subscribers' interstate service costs.²⁶ Currently the contribution factor for the fourth quarter of 2009 stands at a whopping 12.3%, the second-highest contribution factor since 2000.²⁷ This contribution factor reflects only a slight decrease from last quarter's 12.9% factor (the highest factor since 2000) and is an increase of almost three percentage points from the 9.5% contribution factor assessed – and ultimately paid by consumers - in the first quarter of 2009.²⁸ As the Joint Board noted in its November 2007 Recommended Decision, “[l]arger USF contributions increase the risk that telecommunications services will become unaffordable for some, or even a substantial number, of consumers”²⁹ – a result that is clearly contrary to the goals of universal service. At a time when more and more consumers are facing financial hardships,

²⁴ 2008 USF Report, Table 3.1.

²⁵ See Public Notice: Proposed Second Quarter 2000 Universal Service Contribution Factor, DA 00-517 (CCB Mar. 7, 2000); Public Notice: Proposed Fourth Quarter 2008 Universal Service Contribution Factor, DA 08-2091 (OMD Sept. 12, 2008).

²⁶ See Public Notice: Proposed First Quarter 2007 Universal Service Contribution Factor, DA 06-2506 (OMD Dec. 13, 2006); Public Notice: Proposed Second Quarter 2007 Universal Service Contribution Factor, DA 07-1330 (OMD Mar. 15, 2007).

²⁷ Public Notice: Proposed Fourth Quarter 2008 Universal Service Contribution Factor, DA 09-2042 (OMD Sept. 14, 2009).

²⁸ See Public Notice: Proposed Third Quarter 2009 Universal Service Contribution Factor, DA 09-1322 (OMD June 12, 2009); Public Notice: Proposed First Quarter 2009 Universal Service Contribution Factor, DA 08-2706 (OMD Dec. 15, 2008).

²⁹ *In re High-Cost Universal Service Support; Federal-State Joint Board on Universal Service*, 22 FCC Rcd 20477 (2007) (“Joint Board November 2007 Recommended Decision”).

these increasing contribution rates are an unwelcome and significant burden on consumers.

2. USF Funding Is Subject to Waste and Abuse

The current structure of the USF program does not protect against waste and abuse of program funds, and in some ways, facilitates such problems. For instance, the USF program does not distinguish between primary or secondary lines for purposes of high-cost support and thus such support can, and often is, given for multiple connections for a single end user.³⁰ In 1997, when the Commission addressed the issue of support for multiple connections, the Commission acknowledged that providing support to end users with more than one connection “may be inconsistent with the goals of universal service in that business and residential consumers that presumably can afford to pay rates that reflect the carrier’s costs to provide services nevertheless would receive supported rates.”³¹ Nearly 12 years later, the USF continues to support multiple connections to a single end user, despite the pressure it places on fund growth.³² The Commission itself noted, in its 2008 Order adopting an interim cap on support to CETCs that “[a] primary consequence of the existing competitive ETC support rules has been to promote the sale of multiple supported wireless handsets in given households.”³³

Another source of inefficiency, as discussed earlier, is the Commission’s practice

³⁰ See, e.g., *In re High-Cost Universal Service Support*, FCC 08-262, Appendix A, ¶ 7 (2008).

³¹ *In re Federal-State Joint Board on Universal Service*, 12 FCC Rcd 8776, ¶ 95

³² See, e.g., *In re High-Cost Universal Service Support*, FCC 08-262, Appendix A, ¶ 7 (2008).

³³ *In re Federal-State Joint Board on Universal Service*, FCC 08-122, ¶ 9 (2008).

of permitting multiple competitors to receive funding in the same high-cost area.³⁴ While increased competition in a market can benefit consumers, the continued influx of new CETCs seeking access to high-cost support, even in markets where there are ample choices of service providers, is inflating the USF High-Cost program. By the time the Commission finally acted in 2008 to impose an interim cap on CETC support, high-cost support had grown from \$17 million to \$1.18 billion over a 6 year period.³⁵

Examples of abuse of the USF can be found in the E-Rate program. A sampling of Commission suspension and disbarments from participation in the E-Rate program in 2009, reveals offenses ranging from mail fraud,³⁶ bribery and money laundering³⁷ to other “multiple schemes.”³⁸ The mail fraud case netted Douglas Benit and his companies at least \$2.276 million,³⁹ Frankie Wong bribed his way into receiving at least \$35 million in revenue from the Dallas Independent School District and USAC⁴⁰ and the “multiple schemes” of Judy Green impacted the E-Rate program to the tune of \$57

³⁴ See, e.g., *In re High-Cost Universal Service Support*, FCC 08-262, Appendix A, ¶ 7 (2008).

³⁵ See, e.g., *In re High-Cost Universal Service Support*, FCC 08-262, Appendix A, ¶ 8 (2008).

³⁶ *In re: Notice of Suspension and Initiation of Debarment Proceedings*, Letter to Douglas A. Benit from Hillary S. DeNigro, Chief, Investigations and Hearing Division, FCC, File No. EB-09-IH-0402, DA 09-1345 (June 17, 2009).

³⁷ *In re: Notice of Suspension and Initiation of Debarment Proceedings*, Letter to Frankie Longyang Wong from Hillary S. DeNigro, Chief, Investigations and Hearing Division, FCC, File No. EB-08-IH-5313, 24 FCC Rcd 2456 (Feb. 26, 2009).

³⁸ *In re: Judy Green*, Notice of Debarment, File No. EB-08-IH-1139, 24 FCC Rcd 5956 (2009).

³⁹ *In re: Notice of Suspension and Initiation of Debarment Proceedings*, Letter to Douglas A. Benit from Hillary S. DeNigro, Chief, Investigations and Hearing Division, FCC, File No. EB-09-IH-0402, DA 09-1345 (June 17, 2009).

⁴⁰ *In re: Notice of Suspension and Initiation of Debarment Proceedings*, Letter to Frankie Longyang Wong from Hillary S. DeNigro, Chief, Investigations and Hearing Division, FCC, File No. EB-08-IH-5313, 24 FCC Rcd 2456 (Feb. 26, 2009).

million.⁴¹ In each case the Commission required the parties to make some amount of restitution but with the individuals being sentenced to prison, it is unlikely the Commission actually will receive the required restitution amounts. Further, the damage to the E-Rate fund already has been done as the illegally obtained funds already have been distributed.

3. The USF Program Is Not Subject to Normal Budget Oversight; the Program Lacks the Accountability Imposed on Budget Programs

As noted earlier, the USF is an off-budget spending and collection mechanism. Funds are not distributed pursuant to the annual Congressional authorization and appropriations process. Collections too are not run through the annual federal budget process. As a result, the annual scrutiny normally performed by Congress for federal program does not occur with USF, and basic issues of accountability remain open.

While other mechanisms have been put in place in an attempt to deal with this material shortcoming, there has often been a lack of oversight over the USF program, which has contributed to excessive, and likely unnecessary, spending, particularly in the high-cost program. In particular, the lack of specific performance goals and measures prevents the Commission from evaluating whether the program is achieving the intended goals and permits carriers to use USF funding with little or no oversight. In June 2008, the GAO conducted an in depth review of the Commission's oversight mechanisms for the high-cost program and concluded that the mechanisms are "limited and exhibit weaknesses that, collectively, hinder [the] FCC's ability to assess the risk of

⁴¹ *In re: Judy Green*, Notice of Debarment, File No. EB-08-IH-1139, 24 FCC Rcd 5956 (2009).

noncompliance with program rules and ensure cost-effective use of program funds.”⁴²

The GAO recommended the Commission adopt specific goals and performance measures but despite these recommendations, the Commission still has not established performance goals and measures for the high-cost program.⁴³ The United States Office of Management and Budget (“OMB”) also has noted that the USF program does not measure the impact of program funding on telephone subscribership or other potential measures of success nor does the FCC base future CETC funding on measurable benefits.⁴⁴ Unless and until the FCC establishes clearly-defined goals, it will be difficult, if not impossible to determine if the USF program is successful and may result in unnecessary, continued USF spending.

The GAO Report noted that the FCC currently utilizes three methods to monitor carrier use of high-cost funds: (i) carrier audits; (ii) carrier certification; and (iii) validation of carrier data.⁴⁵ However, none of these measures enable the Commission to measure carrier compliance with the USF program and thus are not effective in ensuring carriers are using USF support as intended or limiting unnecessary spending.

Carriers receiving high-cost funds are subject to audit by the FCC, USAC or the states in which the carriers operate. However, in practice, audits are rarely conducted and thus do little to rein in excessive spending. The GAO Report findings on audit

⁴² United States Government Accountability Office, Report to Congressional Committees: Telecommunications, FCC Needs to Improve Performance Management and Strengthen Oversight of the High-Cost Program, GAO-08-633 at 5 (June 2008) (“GAO Report”).

⁴³ *GAO Report* at 5.

⁴⁴ *GAO Report* at 26.

⁴⁵ *GAO Report* at 6.

practices revealed that: (i) since 2002 USAC has audited 17 of 1400 carriers; (ii) between 2006 and 2007 the FCC has solicited information from a sample equal to 65 of 1400 carriers; and (iii) only seven of 50 states report conducting audits.⁴⁶ Further, only one state reported revoking a carrier's ETC designation as the result of an audit, and several states note they do not believe they had jurisdiction to conduct audits.⁴⁷ Thus the audit process, generally is not an effective or reliable method of determining or encouraging carrier compliance with requirements governing use of USF support.

The second Commission oversight process involves the filing of certifications stating carrier compliance with requirements for use of High Cost program funds. The FCC typically requires an annual statement from states and some CETCs that USF funds are being used properly and in accordance with USF program requirements.⁴⁸ However, there is no standardized carrier certification process so the certifications are not guaranteed to be reliable.

Finally, the processes for validating data provided by carriers also fails to confirm if USF support is being used as intended. USAC and the states collect line count and cost data from carriers but current validation methods appear to focus more on whether a carrier's submission is complete as opposed to whether it is accurate.⁴⁹ The National Exchange Carriers Association ("NECA") and USAC both conduct limited reviews of carrier submissions to compare a carrier's filing against the carrier's financial

⁴⁶ *GAO Report* at 36.

⁴⁷ *GAO Report* at 36.

⁴⁸ 47 C.F.R. §§ 54.313, 54.314.

⁴⁹ *GAO Report* at 38.

statements but neither entity penalizes carriers when discrepancies are found. The process still does not confirm whether USF funds are used as intended or encourage compliance with USF spending requirements. These shortcomings in the FCC's oversight methods mean that billions of dollars are distributed and spent each year with little or no accountability.

D. Numerous Proposals Agree That The USF Must Be Capped Or Limited

The USF, and in particular the high-cost support program, is facing challenges as the number of entities seeking support and the amount of support traditionally provided have continued to grow. Imposing a cap on USF support is an effective and efficient means of limiting the growth of the USF program while allowing sufficient funds for broadband advancement. The imposition of a cap on the USF program is not a novel idea as the Commission successfully has implemented caps in the past. Further, there is widespread support – both by industry participants and others – for a cap on the USF.

1. The FCC Already Has Recognized the Need, and Imposed, A Cap on Competitive ETC Funding

As the largest of the USF support programs, the high-cost program is the most significant contributor to the instability of the USF program and the burden on consumers. The Commission recognized the need to limit this program, and, in 2008, in response to a recommendation of the Joint Board, the Commission adopted an interim cap on high-cost funding to CETCs.⁵⁰ At that time, the Commission noted that “the rapid growth in high-cost support places the federal universal service fund in dire

⁵⁰ *In re: High-Cost Universal Service Support*, 23 FCC Rcd 8834 (2008) (“CETC Cap Order”).

jeopardy.”⁵¹ The Commission rightly noted that continued growth of the fund imposes inordinate pressure on consumers: “the continued growth of the fund at this rate is not sustainable and would require excessive (and ever growing) contributions from consumers to pay for this fund growth.”⁵² Further, the Commission has already confirmed that a cap on CETC support was both legal and consistent with the goals of the USF so there is no legal impediment to the Commission’s adoption of a permanent cap.⁵³

This cap was not the first as the Commission previously had implemented caps on high-cost loop support and interstate access support for ILECs.⁵⁴ In fact, funding for the E-Rate and Rural Healthcare programs have been capped as well.⁵⁵ Accordingly, from the perspective of the government, a cap on USF funding is an often-used regulatory tool.

2. There Have Been Several Government Proposals to Cap the USF

The issue of whether and to what extent the Commission should cap the USF has been addressed, not only by carriers, but also by government entities. In particular, the Joint Board has continued to urge the Commission to adopt caps on the USF. In addition to the CETC cap it proposed in May 2007, the Joint Board six months later recommended the Commission adopt an overall cap on the high-cost fund.⁵⁶ The Joint

⁵¹ *CETC Cap Order*, ¶ 6.

⁵² *CETC Cap Order*, ¶ 6.

⁵³ *CETC Cap Order*, ¶¶ 12-23.

⁵⁴ *CETC Cap Order*, ¶ 9.

⁵⁵ See 47 C.F.R. §§ 54.507(a), 54.623.

⁵⁶ *In re High-Cost Universal Service Support*, 22 FCC Rcd 20477, ¶ 26 (Nov. 20, 2007) (“Joint Board Nov.

Board emphasized the fact that “it is consumers who must pay universal service contributions”⁵⁷ and that “unrestrained growth in the universal service fund, regardless of the source, could be, and would likely be, catastrophic for universal service.”⁵⁸ The Joint Board’s proposed solution to this growing problem was an overall cap on high-cost funding that would be applicable to each of the five support mechanisms: High Cost loop, Local Switching, Interstate Common line, Interstate Access and High Cost Model.⁵⁹

Even members of Congress are expressing support for a cap on the USF. After the House Subcommittee on Communications, Technology and the Internet’s hearing on draft USF reform legislation, Congressman Barton entered a formal statement into the record in which he stated that “the Universal Service Fund is in dire need of reform” and that “while the draft sets a soft cap on high-cost support, there are several exceptions that could actually increase the size of the fund. Instead of making things worse, let’s set a real cap on support.”⁶⁰

These recommendations and proposals to cap the USF illustrate that there is widespread recognition of the need for and support for a cap. Whether the proposal is offered by government officials or, as discussed below, by industry participants, the underlying basis for the cap is the same – the need to fix a program that serves an

2007 Recommended Decision”).

⁵⁷ *Joint Board Nov. 2007 Recommended Decision*, ¶ 2.

⁵⁸ *Joint Board Nov. 2007 Recommended Decision*, ¶ 25.

⁵⁹ *Joint Board Nov. 2007 Recommended Decision*, ¶¶ 26, 32.

⁶⁰ Press Release: Sparks? Sure, but No Ring Yet – Barton at <http://republicans.energycommerce.house.gov/News/PRArticle.aspx?NewsID=7553> (visited Nov. 25, 2009).

important need but that has, increasingly burdened consumers as the fund has become increasingly excessive and inefficient.

3. Diverse Groups of Industry Participants Also Support Capping the USF

The ACA is not alone in its support for a cap on the USF program. Numerous entities ranging from ILECs⁶¹ to rural ILECs⁶² to CLECs⁶³ to state commissions⁶⁴ have expressed strong support for a cap – whether interim or permanent – on the USF high-cost program. Over the past few years, industry participants have identified a number of public policy considerations supporting a cap on the USF. These considerations include: “retargeting high cost funding to the right areas and the right services”⁶⁵; “address[ing] the ‘explosive growth’ in high-cost support disbursements” and limit[ing] the risk that public support is being converted to private profits through the high-cost support mechanism”⁶⁶; and “encourag[ing] the optimal balance of public interest,

⁶¹ See, e.g., Embarq Comments on the Notice of Proposed Rulemaking (Regarding the Recommended Decision of an Interim Cap on High Cost Support for Competitive Eligible Telecommunications Carriers), WC Dkt. 05-337, CC Dkt. 96-45 (June 6, 2007); Comments of the Organization for the Promotion and Advancement of Small Telecommunications Companies, WC Dkt. 05-337, CC Dkt. 96-45 (June 6, 2007); Letter to Marlene Dortch, FCC from David C. Duncan, Iowa Telecommunications Association, WC Dkt. 05-337, CC Dkt. 96-45 (filed May 15, 2007).

⁶² Comments of the Independent Telephone and Telecommunications Alliance, WC Dkt. 05-337, CC Dkt. 96-45 (June 6, 2007); Comments of the Minnesota Independent Coalition, WC Dkt. 05-337, CC Dkt. 96-45 (June 6, 2007).

⁶³ See, e.g., Comments of TDS, WC Dkt. 05-337, CC Dkt. 96-45 (June 6, 2007); Comments of Comcast Corporation, WC Dkt. 05-337, CC Dkt. 96-45 (April 17, 2008).

⁶⁴ See, e.g., Comments of the Iowa Utilities Board, WC Dkt. 05-337, CC Dkt. 96-45 (June 6, 2007); Comments of the New Jersey Board of Public Utilities, WC Dkt. 05-337, CC Dkt. 96-45 (April 14, 2008); Comments of the New York Public Service Commission, WC Dkt. 05-337, CC Dkt. 96-45 (April 17, 2008).

⁶⁵ Comments of Verizon and Verizon Wireless, at 24, WC Dkt. No. 05-337, CC Dkt. No. 96-45 (filed May 8, 2009).

⁶⁶ Comments of the National Association of State Utility Consumer Advocates Supporting a Cap on the High-Cost Universal service Fund, at 12-13, WC Dkt. No. 05-337, CC Dkt. No. 96-45 (filed June 6, 2007).

including containing costs while expanding policy-driven (complementing market-driven) service deployment”.⁶⁷

As the ACA noted above regarding the recommendations of government agencies and officials, a strong concern of industry participants is the need to reform a program that simply has grown too large and burdensome for consumers. Industry participants – who traditionally have had diverging views on telecommunications issues – and others have shown consolidated support for the adoption of a cap on the USF.

E. Accelerated Broadband Deployment Envisioned by the National Broadband Plan Can Be Met By Current USF Funding Levels and the Proposals of the ACA

In its report to the Commission on September 29, 2009, the National Broadband Plan staff estimated that it would cost \$20 billion to serve the approximately 3-6 million housing units that lacked access to broadband service at speeds of .768-3 Mbps and \$35 billion to serve the 7-10 million housing units lacking access to 7-10 Mbps service.⁶⁸

In the following section, the ACA presents a series of proposals to enable the Commission to create within a short time an annual fund of \$1-2 billion to support broadband advancement, and it believes that over a decade this fund could double in size as carriers transition from the current mechanism. While this funding could be used in traditional ways to provide ongoing support for the provision of broadband services in high-cost areas, the ACA’s proposals envision a different mechanism, one that combines operational support with support for capital expenditures, such as is

⁶⁷ Comments of the Independent Telephone and Telecommunications Alliance, at 28, WC Dkt. No. 05-337, CC Dkt. No. 96-45 (filed May 31, 2007).

⁶⁸ National Broadband Plan, September Commission Meeting, Sept. 29, 2009 at 45, available at: http://www.fcc.gov/openmeetings/2009_09_29-ocm.html.

occurring with the current broadband stimulus programs operated by the RUS and NTIA. As noted earlier, by having a capital fund for infrastructure construction, operating costs will decrease significant. In addition, it enables the Commission to use more leveraged, alternative financial arrangements than direct grants. If properly structured, it is possible to leverage each dollar in the “new” USF potentially five to ten times, which would facilitate the deployment of broadband infrastructure to most of these housing units and still leave funding to provide operating support where needed. These proposals also will enable the Commission to meet its statutory obligations for universal service and accelerate broadband deployment within the current amount of USF funding.

IV. Transitioning the Current Universal Service High-Cost Support Mechanism to Support Advanced Broadband Deployment

A. Introduction

The Public Notice notes that the Commission and the Joint Board on Universal Service have inquired at different times about reforming the high-cost support mechanism from supporting voice service to supporting advanced broadband deployment.⁶⁹ Over the past several years, this concept has garnered support from numerous parties.⁷⁰ The ACA too endorses the creation of a new support mechanism for broadband but only if it is competitively and technologically neutral and is more precisely targeted to users that lack access in areas that are unserved or underserved.

⁶⁹ *Public Notice* at 2.

⁷⁰ See, e.g. Statement of Joel E. Lubin, Vice President-Public Policy, AT&T Services, Inc. Before: United States House of Representatives, Committee on Energy & Commerce, Subcommittee on Communications, Technology and The Internet, “The Universal Service Reform Act of 2009 [Discussion Draft]”, Nov. 17, 2009, and Statement of Peter Davidson.

As indicated at the outset of these comments, the ACA spent months working with its diverse membership about the development of a fund supporting broadband deployment, and a crucial conclusion reached by the ACA membership is that government needs to use the transition to broadband support to address the many flaws in the current high-cost support mechanism. In other words, just adding the word “broadband” to existing practices will only perpetuate the inefficiencies and inequities of the current program. In the next two sections, the ACA sets forth the structure and operations for the new broadband support mechanisms and the transition from the current mechanism. ACA believes that if its approach is followed, the Commission can relatively swiftly create a fund that can provide support of \$1 billion to \$2 billion annually for the deployment of broadband in unserved and underserved areas and that this fund would grow even further (towards the annual cap of approximately \$4 billion) as providers transition from the current mechanism.

Finally, the ACA has structured the new broadband support mechanism and the transition from the current mechanism to be consistent with the statute. Both during the transition and when completed, there will be “specific, predictable, and sufficient” universal service support mechanisms to preserve and advance voice and broadband service.⁷¹ In addition, consumers throughout the country will have access to these services at comparable rates.

B. Broadband Support Mechanism

1. Areas Needing Broadband Support: Unserved and Underserved

Even with the changes Congress adopted in the 1996 Telecommunications Act,

⁷¹ 47 U.S.C. § 254(b)(5).

the current high-cost mechanism is essentially the vestige of the monopoly era in the provision of telephone service. The mechanism was developed first by the telephone industry many decades ago as an implicit intra-industry subsidy from long distance to local providers, and then in 1984, at the time AT&T was divested, it became incorporated into a more explicit federal program. Today, despite the changes in industry structure and technology, it largely continues to fund local telephone carriers in those areas where costs are significantly higher than the national average, and, where it funds competing wireline and wireless providers, it is based primarily on the same criteria. The problem is that subscribers in these high-cost areas may already be accessing broadband service at rates reasonably comparable to those paid by users in other areas of the U.S. What then becomes the justification for the government subsidy?

Fortunately, Congress has established a new paradigm that enables the subsidy to be targeted more efficiently and effectively. The broadband amendments in the American Recovery and Reinvestment Act enacted earlier this year provide that funding for the deployment of broadband will be awarded to projects in unserved and underserved areas, that is, areas where most users lack access to broadband as opposed to areas just where costs are higher. Moreover, funds are to be used to construct new infrastructure, which in turn lowers operating expenses and thus subsidies to support ongoing operations.

As implemented by the RUS and NTIA, the new broadband stimulus programs have other advantages. First, because the Agencies with the assistance of the Commission have already developed definitions and eligibility requirements, which are

currently being refined further, the Commission can rapidly enable projects in areas where government supported broadband deployment are most needed. Second, service areas are determined by use of the smallest unit of demographic aggregation, the Census Block, which further ensures subsidies are well-targeted. Also, because support is given not only to last-mile projects but to middle-mile projects, users are less likely to experience bandwidth bottlenecks. Finally, the new programs strive for a high degree of transparency, a crucial factor for long-term support of the program.

The ACA believes that the Commission should base the new broadband funding on the concepts of unserved and underserved Census Block areas. An unserved area would be defined initially as in the first Notice of Funds Availability (“NOFA”):⁷² an area where more than 90% of the households lack access to broadband service (768 kbps downstream and 200 kbps upstream). As for the definition of underserved area, ACA suggests that it be streamlined from the first NOFA and focused on the concepts of ensuring more users have access to more advanced broadband service: an area in which at least 50% of the households do not have access to reliable broadband at offered transmission speeds of at least 5 Mbps downstream and 500 kbps upstream. To ensure that the new broadband fund has continuing relevance, the Commission could amend these definitions after receiving sufficient evidence and permitting public comment.

2. Broadband Services Needing Support: Last-Mile and Middle-Mile; Wireline and Wireless

⁷² Department of Agriculture, Rural Utilities Service, RIN 0572-ZA01, Broadband Initiatives Program, Department of Commerce, National Telecommunications and Information Administration, RIN 0660-ZA38, Broadband Technology Opportunities Program, Notice of Funds Availability, *Federal Register*, Vol. 74, No. 130, July 9, 2009.

As noted above, the broadband stimulus programs provide a model upon which the new broadband support mechanism can be based. Because adequate broadband performance can only be determined from the end-user all the way to the internet node, the programs fund both last-mile and middle-mile access. The ACA supports continuation of that approach.

The ACA also supports providing support to broadband services provided over both wireline and wireless networks, albeit, unlike in the first NOFA, determinations about the existence and extent of support should be made separately for each in a service area. While wireline and wireless broadband services may at times be substitutable, far more often the services are viewed by users as complementary. Broadband users in unserved and underserved areas thus should not be deprived of one because they have access to the other. Moreover, not only are the services received by users sufficiently different between these two networks, but the costs and revenues structure – that is, the viability and sustainability – are sufficiently different that any subsidies should be evaluated individually for each.

3. Funding for the New Broadband Support Mechanism

Funding for the broadband support mechanism will come from reductions in funding for the current high-cost mechanism. It will be the difference between the amount of the cap on the high-cost fund as of the end of 2009 and the amount of funding eligible carriers are still permitted to access after that date. Section C below discusses in detail the transition from the current high-cost mechanism and the process of freeing-up funding for the broadband support mechanism. Because of the restrictions the ACA proposes to place on continuing access to the high-cost fund, especially for

carriers subject to competition, it is anticipated that within the first two years of implementation, funding for broadband deployment could be in excess of \$1 billion each year and that this amount should grow steadily thereafter as eligible carriers transition from accessing the current mechanism.⁷³ Eventually, the fund should approach the proposed annual funding cap of approximately \$4 billion.

4. Type of Support and Priorities for Support: Funds for Capital Expenditures and Operating Expenses

Under the ACA's approach, the type of support provided – as well as the priority for support provided – will depend on whether the service area is unserved or underserved and whether the service is last-mile or middle-mile. However, in no event, should more than one wireline and one wireless last-mile provider of broadband service and one middle-mile provider be eligible to receive funding to construct infrastructure in an area. If multiple providers seek such funding in an area, the Commission should employ reverse auctions or another neutral and efficient selection method. As for the award of operating funds, in a previously unserved area (where subsidized construction has occurred), it is highly unlikely there will be competing providers seeking funding and so a selection process would not be necessary. In underserved areas, any operating subsidy should be provided on a “per user” basis; thus there is no need for a selection process. As for funding priorities, the Commission should first seek to fund the construction of infrastructure and operations in unserved areas for both wireline and wireless broadband service.

Unserved Area Last-Mile Support. Because almost all users in unserved areas

⁷³ See, NCTA Petition and the accompanying report by Empiris for evidence of the effect of a “competition” test on high-cost funding.

lack access to broadband, the new support mechanism should fund the construction of last-mile infrastructure in these areas (capital expenditures). Before providing any capital support, the Commission should ensure that there is no other adequate source of funding and may require a matching contribution from the provider. Once the infrastructure has been built, the Commission can determine whether, how much, and for how long an operating subsidy should be provided. The operating subsidy, which would be provided per broadband line served per month, would be calculated based on the forward-looking cost of providing broadband service sufficiently in excess of the average nationwide cost. As with today's distribution, the Commission should structure this subsidy to maximize its effectiveness and efficiency. For ease of administration, the Commission should consider using density or some other factor closely linked to costs as a way to determine the differential in costs among different eligible service areas. Finally, separate and apart from this new mechanism, the ACA encourages the Commission to award funding for low-income households to subscribe to broadband service in all areas.

Underserved Area Last-Mile Support. Because by definition existing providers are already providing service in underserved areas, the new support mechanism should only fund operations where costs are sufficiently above the nationwide average. As in unserved areas, the operating subsidy would be provided per broadband line served per month. As such, multiple providers could receive support in underserved areas.

Middle-Mile Support. A middle-mile provider seeking to provide access in an area currently or recently unserved or underserved area should receive funding for capital expenditures if it can demonstrate to the Commission that there is inadequate

middle-mile capacity to meet the broadband needs of the area (i.e. unserved or underserved) and that the project is viable and sustainable. As with capital funding for last-mile projects in unserved areas, the Commission should ensure there is no other adequate source of support and should require matching contributions. A middle-mile deployment may, to a lesser extent, serve other areas, but the Commission should ensure that any funding is used predominantly to link users in unserved and underserved areas to the internet.

5. Support Requirements, Accountability, and Updates

Funding under the ACA's proposal would be accompanied by strict terms and conditions. Any infrastructure project would need to be initiated and completed within a limited time. Operating funding should be based on meeting broadband service performance requirements. In all instances, providers receiving funds should file regular reports during the year, conduct an audit annually, and be subject to a government audit at any time. Every three to five years, the Commission should assess funding for each area, as well as the overall requirements of the program, to ensure adequate infrastructure has been constructed, operating support is still needed, and the program's objectives are being met.

C. Transition from the Current High-Cost Support Mechanism

1. Policy Principles for the Transition

The Communications Act, in general, provides that universal service funding shall ensure that all consumers have access to telecommunications services that are "reasonably comparable" and at rates that are "reasonably comparable."⁷⁴ The ACA

⁷⁴ 47 U.S.C. § 254(b).

has used this mandate (and the specific directives of the statute) to craft a series of policy principles to drive the transition from the current high-cost support mechanism to the new broadband support mechanism as equitably and swiftly as possible. When taken together, these principles should ensure that no consumer suffers lapses in service quality or rate increases as the providers diminish their access to the current mechanism and the new fund becomes established. Moreover, these principles should ensure that those providers most dependent on the current fund do not see precipitous declines in funding that would threaten their viability or sustainability of their provision of voice services. The ACA's recommended policy principles are:

- Smaller, more rural incumbent wireline providers – those entities most reliant on current funding – should be able to continue to access funding for as long as possible.
- Providers seeking to access funding from the broadband support mechanism for a service area should not be able to draw funding from the high-cost support mechanism for that same area.
- Providers should not be able access funding if the consumer can obtain service from another provider that does not draw from the fund or if a regulator has deregulated the provision of service to that consumer or area.
- No provider may access funding to serve an area or consumer not currently supported by funding.⁷⁵

When taken together, these principles provide a legally supportable, sound, consistent, and well-understood framework for transitioning funding for providers currently drawing from the fund.

2. Implementing the Policy Principles

⁷⁵ As part of its proposal, the ACA supports continuation of the “interim” cap on funding for competitive eligible telecommunications carriers (“CETCs”). To ease the strain on CETCs already drawing from the fund, a CETC entering a new service area would not be able to draw from the fund.

The following guidelines implement the ACA's policy principles for the high-cost support mechanism:

- Current wireline ETCs with fewer than 100,000 access lines in total may continue to draw from the fund as they draw today (by area) for the provision of voice service unless they choose to access funding from the new broadband mechanism to serve that area (other than access to the fund for purposes of funding middle mile infrastructure), in which case the funding regime in the new mechanism replaces the current mechanism.
- Current wireline ETCs with more than 100,000 access lines in total may continue to draw from the fund based on the "current high cost differential" per access line multiplied by the number of voice access lines in service annually. No such wireline ETC may draw from the fund for an access line if (1) the user can obtain voice service from another wireline provider who is able to serve the user without drawing from the fund, (2) the state regulator has deregulated the wireline ETC's provision of voice telephone service for the user, or (3) the wireline ETC accesses funding from the Broadband Fund to serve the user (other than access to the fund for purposes of funding middle-mile infrastructure).
- A wireline CETC may continue to draw from the fund based on the number of voice access lines served, except that (1) no funds would be awarded if another competing wireline provider was able to serve the same customer without drawing from the fund, and (2) no funds would be awarded if the CETC accesses funding from the Broadband Fund to serve that customer (other than access to the fund for purposes of funding middle-mile infrastructure).
- A wireless CETC would draw from the fund based on the number of voice access lines served, except that (1) no funds would be awarded if another wireless provider was able to serve the same customer without drawing from the fund, and (2) no funds would be awarded if the CETC accesses funding from the Broadband Fund to serve that customer (other than access to the fund for purposes of funding middle-mile infrastructure).

By virtue of these policies, more rural entities will have greater flexibility in making the transition for the current funding mechanism – a benefit that should redound to their consumers -- while entities subject to greater competition will not, which should

not harm their consumers. All providers, however, will be able to access the new broadband mechanism to provide service in unserved or underserved areas. Finally, because so many entities that currently draw from the high-cost fund will no longer be able to do so – and by using evidence gathered in the NCTA Petition – the amount of funding for the new broadband fund should rapidly reach more than \$1 billion.

D. Provision of a More Sustainable and Rational Contribution Method

The current USF program relies on contributions based on collected interstate and international revenues. When adopted in 1996 interstate and international revenues were growing. The total assessable revenue base however has been declining. The total assessable revenue base has declined from approximately \$78,977,000 billion in 2000 to approximately \$74,499,000 in 2006.⁷⁶ For the fourth quarter 2009 projected revenues are \$17,164,439 billion.⁷⁷ The decline in the revenue base causes the contribution factor to rise as a higher rate is needed because of the reduced revenue base.

As interstate and international prices continue to fall, it has a detrimental effect on the revenue generated. The integration of local and long distance services into bundled packages has blurred the distinction between the interstate and intrastate services. Further, the loss of traffic to internet services such as Skype and other non-

⁷⁶ See, JIM LANDE & KENNETH LYNCH, FCC, 2000 TELECOMMUNICATIONS INDUSTRY REVENUES, *tbl. 4* (2002), available at http://www.fcc.gov/Bureaus/Common_Carrier/Reports/FCC-State_Link/IAD/telrev00.pdf; JIM LANDE & KENNETH LYNCH, FCC, 2006 TELECOMMUNICATIONS INDUSTRY REVENUES, *tbl. 1.4* (2008), available at http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-284929A1.pdf.

⁷⁷ *Fourth Quarter 2009 Contribution Notice*, p.2.

interconnected VoIP services have impacted the amount of interstate and international revenues.

A more sustainable and rationale methodology for funding is required going forward. The ACA supports the review and adoption of a hybrid telephone numbers/connections contribution methodology provided it is non-discriminatory, technology neutral and capped to collect the amount of revenue currently collected under the USF.

If the Commission decides to retain the interstate/international revenue based contribution methodology it must at least revise the discriminatory interconnected VoIP provider safe-harbor calculation.

Many smaller ACA members provide VoIP services with the assistance of third party companies who are unable to provide a break down of the traffic. Thus, such operators are forced to rely on the “interim” safe harbor established in 2006 for interconnected VoIP providers which assumes that 64.9% of the traffic is interstate.⁷⁸ The 64.9% is unrealistically high and results in interconnected VoIP providers having to pay a higher percentage to Universal Service than their competitors. For example: the wireless safe harbor is 37.1%.⁷⁹ There is no reason to assume, based on the evolution of VoIP services, that interconnected VoIP service results in more interstate traffic than wireless phones which are truly mobile. Interconnected VoIP traffic would seemingly be more in line with traditional landline traffic. Further, USAC has had enough experience

⁷⁸ *In the Matter of Universal Service Contribution Methodology*, 21 FCC Rcd 7518 ¶53 (2006) (“VoIP USF Order”).

⁷⁹ *VoIP USF Order*, ¶2.

with interconnected VoIP providers that are able to delineate the traffic that a more realistic safe harbor percentage can be set based on the actual reported by those operators.

V. Conclusion

The ACA proposals provide a balanced approach for evolving USF to provide for broadband while protecting consumers by funding the broadband expansion through targeted reforms that assure that USF funding goes to areas where it is truly needed. The ACA proposals should be adopted.

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