

**ENSURING THE AVAILABILITY OF
AFFORDABLE TELECOMMUNICATIONS SERVICES
IN RURAL COMMUNITIES**

ISSUE

- **Universal service support is crucial for rural communities:** Universal Service Fund (“USF”) support is critical for ensuring access to public safety resources, healthcare resources, economic development, and educational opportunities for Americans living in rural areas.
 - Although reform of the contribution and distribution mechanisms could make the USF more efficient and transparent, support is necessary to ensure the availability of affordable telecommunications services in rural areas, as nearly all agree.
- **Reverse auctions have been considered as a potential means for improving the efficiency with which universal service support is distributed:** Reverse auctions allow the Universal Service Administrative Company (“USAC”) to distribute support to eligible telecommunications carriers (“ETCs”) at or near the lowest possible per-line support level.
- **Reverse auctions can have the unintended result of reducing the availability of affordable telecommunications services in rural communities:**
 - Reverse auctions are complex and expensive, which increases the cost of providing service.
 - The awarding of support through a reverse auction can result in higher retail prices for consumers in rural areas than they would experience if ETCs could compete for support on an ongoing basis.
- **Use of only one single-winner reverse auction to distribute support in each area would exacerbate the potential harms associated with reverse auctions:** Because only one ETC receives support in each area,
 - The winning ETC can set pricing at a level that discourages entry by potential competitors: retail rates would be limited only by the lower of (a) the price point at which *unsupported* carriers profitably could match the price and enter the market or (b) its total profit declines because enough consumers choose not to purchase service at all.
 - Only one type of technology will receive support, which may not be the technology of choice by all members of the rural community.
 - With one ETC having a *de facto* monopoly, members of rural communities will have few, if any, available options in terms of service providers, services plans, rate plans, technologies and devices.
- **Conducting multiple single winner auctions in each geographic regions would mitigate, but not eliminate, the potential harms associated with reverse auctions:** By holding multiple simultaneous auctions for USF support (with a carrier only allowed to win one of the auctions), multiple ETCs will be forced to compete for support, which is fully portable, and for customers without significantly increasing total support paid by the USF.

EXAMPLES

Carriers A, B, C, and D are all ETCs providing supported services in a rural high-cost service area. Within the area, there currently are 1,000 USF supported lines. Carrier D, the ILEC in the region, serves 500 lines at a total cost of \$7,500, resulting in a per-line cost of \$15. Under the current identical support rule, each of the three remaining ETCs receive \$15 in support for each line they serve in the area. As such, the fund currently provides a total of \$15,000 in support for the area (\$7,500 in ILEC costs plus 500 lines x \$15 per line). For the sake of simplicity, this example assumes that competition has driven all of the ETCs to charge a monthly rate of \$1. The current per-line support level of \$15 suggests a reasonable “reserve price” for any reverse auction.

SINGLE WINNER REVERSE AUCTION

- **Under a single winner reverse auction, only the winning bidder is eligible for support.** Bidding begins at the reserve price of \$15, and concludes at the end of all bidding rounds (using \$1 bid increments) with Carrier A’s final bid of \$10. For this example, assume that the final bids of Carriers D, C and B were \$15, \$12 and \$11 per line, respectively.¹
 - **Carriers B, C, and D must increase the price charged consumers.** Denied support, Carriers B, C, and D must pass on their full costs to consumers. These carriers are no longer competitive with Carrier A in the auction area.
 - **Carrier A can now charge up to \$11, reaping almost \$5 more per line than under the current system.** Essentially, Carrier A can increase its price to maximize its profit potential (regardless of the consumers served)² to any amount less than the next lowest bidder’s costs (*i.e.*, Carrier B, which determined that it needed \$11 of support to serve the area, will enter the market and provide service at \$12³). As such, Carrier A can earn \$5 more per line than it could under the current system (*i.e.*, Under the single winner reverse auction, Carrier B now receives a total of \$22 per line, which represents the winning bid of \$10 subsidy per line plus a monthly rate of \$11, which is \$5 less than the total of \$16 it receives under the current system, which represents the \$15 per line previous subsidy plus \$1 monthly rate).
- **As a result, the benefits of USF support would flow solely to Carrier A in the form of increased profits rather than to the rural community in the form of lower rates and more choices amount service providers, services and devices.** Assuming all consumers switch to the winning bidder with the cheapest available rate (*i.e.*, Carrier A), the USF fund would distribute a total of \$10,000 in support to Carrier A, which represents a savings of \$5,000 per month for the USF in that area. *However, rural consumers would see a price increase of \$10 per month, from the previous \$1 per month to the new rate of \$11 per month.*

¹ The final bids reflect each carrier’s best estimate of the minimum amount of support necessary for them to serve the auction area.

² Some consumers may choose to forgo service at the rates that Carrier A will charge. If enough consumers choose to forgo the \$11 service rate that Carrier A’s profits begin to decline, Carrier A will reduce its rate to the point that its profits are maximized.

³ Carrier B’s minimum service price can be calculated by adding the \$1 charged the end user with the subsidy (\$11) necessary to provide service.

Carrier A would also see an increase in profits of \$5 per line (*i.e.*, \$11 new rate plus \$10 in new support minus \$1 old rate plus \$15 old support).

MULTIPLE SIMULTANEOUS REVERSE AUCTIONS

- **Under a multiple simultaneous reverse auctions where two single winner reverse auctions are conducted in each area, support would be available to two carriers in each area.** Bidding begins at the reserve price of \$15, and concludes at the end of all bidding rounds (using \$1 bid increments) with the winning bids of \$11 by Carrier A and Carrier B (Carrier A would have been willing to bid \$10 but both Carrier A and Carrier B won at \$11 because Carrier C stopped bidding at \$12).⁴
 - **Carriers C and D must increase the price charged to their consumers.** Denied support, Carriers C and D must pass on their full costs to the consumers. These carriers are no longer competitive with Carriers A and B in the auction area.
 - **Neither Carrier A nor Carrier B may charge more than \$1 without losing customers to the other carrier.** Assuming for the sake of simplicity that consumers choose between Carrier A and Carrier B solely on the basis of price and that the carriers do not coordinate pricing, the rural community would see no increase in retail rates because Carrier A and Carrier B must compete to serve supported lines.
- **Under a multiple reverse auction plan, USF support flows to consumers rather than to carriers.** Assuming all consumers switch to one of the two winning bidders with the cheapest available rate (*i.e.*, Carriers A and B), the USF fund would distribute a total of \$11,000 in support to Carriers A and B, which represents a savings of \$4,000 per month for the USF in that area. *However, consumers continue to pay only \$1 a month for service, thus ensuring that the consumers, rather than the carriers, reap the benefit of universal service.*
- **The benefits to rural communities increase when additional carriers are permitted to compete for support.**

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⁴ The final bids reflect each carrier's best estimate of the minimum amount of support necessary for them to serve the auction area.