Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
A National Broadband Plan for Our Future	)	GN Docket No. 09-51
	)	
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 07-135
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Developing an Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
Lifeline and Link-Up	)	WC Docket No. 03-109

REPLY COMMENTS OF VERIZON AND VERIZON WIRELESS

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May 23, 2011

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TABLE OF CONTENTS

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	)	
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	)	
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REPLY COMMENTS OF VERIZON[1] AND VERIZON WIRELESS

I. INTRODUCTION AND SUMMARY.

Across the board, commenters agree that the time is now to take concrete steps to fix the backwards-looking intercarrier compensation and universal service systems. It is critical for the Commission to follow through on its commitment to adopt comprehensive reforms by no later than the end of this summer. The Commission should replace the intercarrier compensation and universal service apparatus with a system that provides rational market-based incentives to deploy new technologies and services within a more stable, sustainable regulatory environment.

[1] In addition to Verizon Wireless, the Verizon companies participating in this filing ("Verizon") are the regulated, wholly owned subsidiaries of Verizon Communications Inc.

To lay the groundwork for comprehensive reform of both the intercarrier compensation system and the Universal Service Fund (USF or "fund"), commenters correctly urge the Commission first to make sure problems with the current system do not get worse. The top priority remains the urgent need to decide the proper intercarrier compensation rate for VoIP traffic that connects with the PSTN. The Commission should immediately set a single, low national default rate of $0.0007 per minute for this traffic.

In the absence of Commission action, an increasing number of carriers, state commissions and cable VoIP providers are acting unilaterally to impose legacy access charges on VoIP services despite the fact that the Commission made clear that it has not yet decided whether access charges should be extended to these innovative new services. Unless the Commission acts now to address the intercarrier compensation rules that apply to VoIP traffic, the result of this trend will be to impose a significant new tax on VoIP services that will be borne by consumers. The result would be to impose significant new costs and corresponding welfare losses on consumers, while limiting the competitive impact of these innovative services.

While extending legacy access charges to VoIP would be inappropriate in all cases, this result would be particularly egregious in the case of cable companies, which often avoid paying access charges by routing their traffic through third parties who are known to dispute the applicability of access charges on VoIP traffic, yet demand access payments for terminating traffic from other providers. The access regime was devised at the time of divestiture as a way to replace part of the subsidy that historically flowed from higher priced long distance services to local services that had been priced artificially low by regulators. But cable companies have not had their rates set by the regulators, and there is no plausible reason that customers of other providers should subsidize them.

Moreover, the Commission's VoIP compensation policy should be significantly informed by what actually happened in the wireless industry. More than ten years ago the Commission effectively set a low default rate for the large majority of wireless traffic that connects with the PSTN. Since that time the wireless industry invested more than $220 billion to deliver new, innovative services—while the average revenue per voice minute has decreased by over 72%. If allowed to grow efficiently without the burden to pay for the collapsing legacy access charge system, VoIP offers the same potential for consumer welfare gains.

With the right policy for VoIP in place, the Commission will be in a position to execute on a reasonable, balanced plan to reform intercarrier compensation and universal service comprehensively. The record reflects a collective desire to strike the right policy balance that is only possible through simultaneous reform of both the intercarrier compensation and universal service systems—promoting deployment of advanced technologies on the one hand, while limiting the costs imposed on consumers and putting the industry as a whole on more sustainable footing on the other hand.

The status quo is not sustainable, and it is no good for consumers. Existing intercarrier compensation regimes provide a disincentive to transition to next-generation technologies. The best way to put consumers first in this proceeding is to transition all intercarrier compensation rates down to a single, low default rate ($0.0007 to mirror the new VoIP rate) as quickly as possible and to eliminate arbitrage opportunities. The Commission should provide for a certain but short transition to a uniform low rate so that affected carriers can prepare to conduct business relying primarily on end user revenues. Where explicit universal service subsidies are necessary, the Commission should target those subsidies—after first capping all high cost funding—to areas that are unserved or would not be served without support. The Commission should use competitive bidding to distribute funds more efficiently, thereby reducing the size of the fund over time. Finally, the Commission should acknowledge that artificial jurisdictional barriers are irrelevant to modern, any-distance services and exercise its preemption authority over intercarrier compensation rates and state USF policies that thwart national objectives.

II. COMPREHENSIVE REFORM IS CRITICAL BUT MUST NOT DERAIL IMMEDIATE ACTION ON VOIP COMPENSATION, TRAFFIC PUMPING, AND ELIMINATION OF REMAINING CETC FUNDING.

The need to get the intercarrier compensation and universal service programs right for the broadband future should not delay action on the three critical issues that the Commission must address right away—VoIP compensation, traffic pumping, and elimination of remaining CETC funding.

1. VoIP Traffic. Though parties may disagree on the appropriate solution, commenters acknowledge that the most pressing issue before the Commission in this proceeding is the crucial need to address the proper intercarrier compensation rate for VoIP traffic that connects with the PSTN. *See, e.g.*, State Members of the Federal State Joint Board ("State Members") May 2 Comments at viii; AT&T Comments at 29; Comcast Comments at 4; Public Utilities Commission of Ohio ("Ohio Commission") Comments at 63. The Commission should act now to avoid burdening VoIP services with the costs of the uneconomic subsidies inherent in the current intercarrier compensation system and should set a uniform, low default rate for VoIP traffic. It is essential to resolve on a nationwide basis what intercarrier compensation may be due on VoIP.

Indeed, in the absence of a Commission decision, an increasing number of carriers, state commissions and cable companies are acting unilaterally to impose the legacy access regime on VoIP traffic despite the fact that this Commission has made clear that it has not yet decided whether to extend the access regime to VoIP. Across the country, traditional carriers are acting unilaterally to assert that VoIP traffic is subject to both interstate and intrastate access rates that are often several cents per minute (and in some cases are as high as ten cents per minute or more). This phenomenon also has expanded to cable companies which frequently avoid paying access charges on the grounds that their traffic is VoIP—often by routing their traffic through third parties who dispute the applicability of access charges—but at the same time demand that other providers pay access charges to terminate traffic to customers of their VoIP services. And while in all cases it would be inappropriate to extend the legacy access regime to new VoIP services, it would be particularly unwarranted to apply cable providers' high intrastate access rates—which range to more than nine cents per minute in the case of one cable provider[2]—to traffic that terminates on their VoIP services. The legacy access charge regime was devised at the time of divestiture to replace the subsidies that historically flowed from high priced long distance services to local services which were priced at artificially low levels by regulators. Cable providers, of course, have never been subject to the retail pricing constraints of traditional carriers nor have they been subject to the service obligations that applied to many traditional carriers. There is no policy justification for extending the legacy access subsidy scheme to cable providers, particularly where the effect would be to increase the cost of other services that compete with cable's own VoIP services.

[2] For example, one cable company that has brought a complaint before the Pennsylvania commission charges remarkably high switched access charges which in some areas exceed $0.09 cents per minute. *See* Verizon's Prehearing Memorandum, *Armstrong Telecommunications, Inc. v. Verizon Pennsylvania Inc. et al.*, Docket No. C-2010-2216205 (Penn. Pub. Util. Comm'n filed Mar. 17, 2011), at 3 n.4. Bright House, which has brought a complaint before the Florida commission, charges more than $0.038 cents per minute in Florida. *See* Bright House Networks Information Servcies (Florida), LLC Access Services Price List, § 4.1(A) & (B). Cox chose to bring a complaint in California where it charges $0.018 per minute (*see* Cox California Telcom, L.L.C., Schedule Cal. P.U.C. B-1, § 2.4), but elsewhere it charges rates more than twice that level. *See* Cox Idaho Telecom, LLC Idaho PUC Tariff No. 2, §§ 3.10.

In addition, absent Commission action, states are moving to fill the void on VoIP and are producing a confusing patchwork that would increase the cost and complexity, and undermine deployment of these innovative new offerings. After initially declining to address emerging VoIP issues in the wake of this Commission's *Vonage* decision,[3] state commissions have begun to assert jurisdiction over VoIP traffic that is purportedly "intrastate." Commissions in Iowa, Kansas, New Hampshire, Missouri, Georgia, Pennsylvania and Texas have purported to establish state-specific VoIP intercarrier compensation regimes in certain contexts.[4] State legislatures, including in Missouri and Wisconsin[5], also have begun to insert themselves into the VoIP compensation vacuum—and others are considering doing so. That activity has emboldened both

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[3] *See Vonage Holdings Corporation Petition for Declaratory Ruling Concerning an Order of the Minnesota Public Utilities Commission*, Memorandum Opinion and Order, 19 FCC Rcd 22404 (2004) ("*Vonage Order*").

[4] *See, e.g.*, Order, *Sprint Commc'ns. Co. v. Iowa Telecomms. Servs.*, Docket No. FCU-2010-0001 (Iowa Util. Bd. Feb. 4, 2011); Order Adopting Arbitrator's Determination of Unresolved Interconnection Agreement Issues Between AT&T and Global Crossing, *Petition of Southwestern Bell Tel. Co.*, Docket No. 10-SWBT-419-ARB (Kan. Corp. Comm'n Aug. 13, 2010); Order Addressing Petition for Authority to Block the Termination of Traffic from Global NAPs Inc., *Hollis Tel., Inc.*, *Kearsage Tel. Co., Merrimack County Tel. Co., and Wilton Tel. Co.*, DT 08-028, Order No. 25,043 (N.H. Pub. Utils. Comm'n Nov. 10, 2009); Decision, *Southwestern Bell Tel. Co. d/b/a AT&T Missouri for Compulsory Arbitration of Unresolved Issues for an Interconnection Agreement with Global Crossing Local Services, Inc. and Global Crossing Telemanagement*, File No. IO-2011-0057 (Mo. P.U.C. Dec. 15, 2010); Order Adopting in Part and Modifying in Part the Hearing Officer's Initial Decision, *Request for Expedited Declaratory Ruling as to the Applicability of the Intrastate Access Tariffs of Blue Ridge Tel. Co. et al. to the Traffic Delivered to Them by Global NAPs, Inc.*, Docket No. 21905 (Ga. Pub. Utils. Comm'n July 29, 2009); Opinion & Order, *Palmerton Tel. Co. v. Global NAPs South*, Docket No. C-2009-2093336 (Pa. Pub. Util. Comm'n Mar. 16, 2010); Arbitration Award, *Petition of UTEX Commc'ns. Corp. for Arbitration Pursuant to Section 252(b) of the Federal Telecomm. Act and PURA for Rates, Terms, and Conditions of Interconnection Agreement with Southwestern Bell Tel. Co*., Docket No. 26831 (Tex. P.U.C. Jan. 27, 2011).

[5] As discussed in Section V-A, *infra*, a Wisconsin bill awaiting the Governor's signature would both lock in many carriers' remarkably high intrastate switched access rates and require the application of the legacy switched access regime to VoIP traffic. A Missouri statute states that interconnected VoIP service is "subject to appropriate exchange access charges to the same extent that telecommunications services are subject to such charges". *See* Mo. Rev. Stat. § 392.550(2). The validity of the statute is currently being challenged in federal court.

carriers and cable companies alike to forum shop for states that will uphold requests to apply tariffed access charges to VoIP—despite clear language from this Commission that it has never decided whether the access regime should be extended to VoIP and that it intends to address that question here.[6]

Given that different states have and will approach VoIP differently, and the strong possibility that many states will develop VoIP policies inconsistent with overarching federal policy goals, any additional delay in the Commission's decision on VoIP compensation would likely create even more complexities and difficulties, because carriers will need to "undo" what they had implemented under the patchwork of state rules. The Commission should immediately adopt a single, low default rate (that applies absent a commercially negotiated alternative) of $0.0007 per minute prospectively for all VoIP traffic that connects with the PSTN, whether IP-PSTN or PSTN-IP. The Commission should not—and must not—increase the cost of VoIP in the short-term by forcing these jurisdiction-agnostic services into the current broken intercarrier compensation system. State Members May 2 Comments at 19-22. That approach would

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[6] *See Connect America Fund*; *A National Broadband Plan for Our Future*; *Establishing Just and Reasonable Rates for Local Exchange Carriers*; *High-Cost Universal Service Support*; *Developing an Unified Intercarrier Compensation Regime; Federal-State Joint Board on Universal Service*; *Lifeline and Link-Up*, Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, 26 FCC Rcd 4554, ¶¶ 608 ("The Commission has never addressed whether interconnected VoIP is subject to intercarrier compensation rules and, if so, the applicable rate for such traffic") & 609 (stating intention to establish a VoIP framework consistent with this Commission's "overarching" broadband and IP network objectives) (2011) ("*NPRM*"). Of course, particular carriers bring state commission complaints before the commissions they perceive as most likely to act in their interests. The ability to choose where to press for a regulatory advantage is important given that the emerging patchwork of state-specific VoIP policies is anything but coherent. *Compare*, *e.g.*, Iowa Utilities Board April 1 Comments (recommending that VoIP services be classified as telecommunications services and subject to the legacy regulatory regime to the extent they "exhibit a functional equivalence" to telecommunications services) with Pennsylvania Public Utility Commission ("Pennsylvania PUC") April 1 Comments at 3 (explaining that distinguishing between different types of VoIP services would be "artificial and ill-advised").

substantially deter deployment of broadband and advanced services such as VoIP. For illustrative purposes, a single VoIP customer making a relatively moderate 100 minutes of "intrastate toll" calls per month may pay an annual intrastate VoIP tax ranging from $25 to more than $120—and a customer with 200 minutes (or a little over 3 hours of talking time) would pay between $50 and $240.[7] The interstate portion of a VoIP tax would likely add at least $35 annually for 300 monthly minutes of "interstate" calling, and in many cases would be much higher, such as $60 annually for a customer who averages a still-moderate 500 minutes per month.[8]

As the Commission and others have correctly noted, history provides proof positive of the benefits that would result from setting a low default rate for VoIP that is free of the existing subsidy scheme—and, correspondingly, of the harms that would result from extending the current system to VoIP. Fifteen years ago, wireless, like VoIP today, accounted for a comparatively small amount of traffic—approximately 38 billion minutes of use in 1995[9]—and was still emerging as a relatively new technology with great promise. The Commission got it right and set a low rate (effectively $0.0007) for most wireless traffic that connects with the PSTN.[10] The result was the exponential, efficient growth of wireless networks and services—

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[7] The $25 and $50 calculations assume an average intrastate switched access rate slightly above $.02, but intrastate rates in many states are much higher. For example, in Arizona, RLECs charge intrastate switched access rates that on average exceed ten cents per minute. *See* Section V-A, *infra*.

[8] Assuming an average interstate switched access rate of $0.01 per minute.

[9] CTIA, "Wireless Quick Facts," http://www.ctia.org/advocacy/research/index.cfm/AID/10323 ("Wireless Quick Facts").

[10] The combination of the Commission's *Local Competition Order* and the 2001 *ISP Remand Order* resulted in a low, uniform rate of $0.0007 (or typically something in that range or lower where there is a commercial agreement) that applies to most wireless traffic terminated by LECs. *Implementation of the Local Competition Provisions in the Telecommunications Act*; *Interconnection between Local Exchange Carriers and Commercial Mobile Radio Service*

including a *sixty-fold* increase in minutes of use, to 2.2 trillion minutes[11]—even as prices have steadily declined. With low-cost local termination rates, wireless carriers were able to introduce attractive bucket-of-minute plans, and matters took off from there, forever changing the many ways in which we communicate and stay connected in urban and rural areas alike. The consumer benefits from efficient expansion of wireless networks and services have been enormous.[12] Since 2001, and the average revenue per voice minute has decreased by over 72%, a significant portion of which obviously could not have occurred if wireless traffic had been subject to several cent per minute intrastate access charges.[13] Over the same time period, the wireless industry has invested more than $220 billion and added approximately 36% to its employee-base.[14] To be sure, there are a number of reasons for wireless growth and success, but keeping regulatory constraints off of wireless providers and intercarrier compensation rates low have been important factors. Similarly, the amount of VoIP traffic terminated by LECs today is

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(Continued . . .)
Providers, First Report and Order, 11 FCC Rcd 15499 (1996) ("*Local Competition Order*") (establishing the current intraMTA rule that treats the majority of wireless traffic as local traffic for intercarrier compensation purposes); *Implementation of the Local Competition Provisions in the Telecommunications Act of 1996*; *Intercarrier Compensation for ISP-Bound Traffic*, Order on Remand and Report and Order, 16 FCC Rcd 9151 (2001) ("*ISP Remand Order*").

[11] *See* Wireless Quick Facts.

[12] One commenter, the State Members, actually suggests that the Commission should eliminate the intraMTA rule altogether. State Members May 2 Comments at 154. That is backwards. All of the consumer welfare gains from the Commission's long-standing (and correct) policy to keep the rates for wireless traffic low could be undone if the intraMTA rule is reversed. It is true that the intraMTA rule may be unnecessary if all intercarrier compensation rates are unified with a single, low default rate—but even if the Commission were to adopt a comprehensive reform plan today that plan would likely include a transition to a new uniform rate. Like the VoIP rate, it makes no sense—and indeed would harm consumers and the efficient deployment of advanced services—to move wireless rates up in the short-term only to move them back down as part of comprehensive reform.

[13] *See Fourteenth Report*, ¶¶ 189-190 & Table 19 (citing CTIA data through 2008).

[14] *See* CTIA, *Year-End 2010 Top-Line Survey Results*, http://files.ctia.org/pdf/CTIA_Survey_Year_End_2010_Graphics.pdf.

still relatively small, and VoIP services are still developing.[15] But there is no doubt that VoIP is the technology of the future for both wireline and wireless services, and this traffic will grow over time if it is not saddled with the cost burdens of the legacy system.

In addition, if the goal of comprehensive intercarrier compensation reform is a low, uniform default rate that applies nationwide—and it should be—then it only makes sense to start at that point for VoIP, rather than first establishing a high rate for VoIP and then lowering it to a market-based level. A uniform low rate for VoIP traffic will serve as a natural glide path to a single, low national default rate for all PSTN traffic, which is the Commission's announced goal in this proceeding and many commenters' preference for the end-state of comprehensive intercarrier compensation reform. *See, e.g.*, Sprint Comments at 21; CTIA Comments at 37-38; Comcast Comments at 5; Cox Comments at 12.

Moreover, the market is already moving toward a default rate of $0.0007 for VoIP traffic that connects with the PSTN. In just the last few weeks, Verizon Florida and a major cable company, Bright House Networks Information Services, settled an ongoing dispute and amended their interconnection agreement, mutually agreeing to exchange certain VoIP traffic at a rate of $0.0007 per minute.[16] Verizon also recently entered into a commercial agreement with

[15] For example, the Wireline Bureau has estimated that as of June 30, 2010, interconnected VoIP accounted for 28,895,000 out of 151,171,000 lines nationally. *See Local Telephone Competition: Status as of June 30, 2010*, Industry Analysis and Technology Division, Wireline Competition Bureau, http://www.fcc.gov/Daily_Releases/Daily_Business/2011/db0321/DOC-305297A1.pdf, Figure 2 (March 21, 2011) ("*Local Telephone Competition Report*").

[16] *See* Letter from Dulaney O'Roark, Verizon, to Ann Cole, Florida Public Service Commission, Docket No. O90501-TP, Document No. 02939-11, Attachment at 76 (Fla. Pub. Serv. Comm'n. filed April 29, 2011).

Bandwidth.com for the exchange of all VoIP traffic at $0.0007 per minute.[17] In addition, Verizon has entered into negotiated, publicly filed interconnection agreements with several carriers—including AT&T and Level 3—that established rates at or below $0.0007 per minute for terminating local traffic and ISP-bound traffic.[18] Verizon Wireless, too, has entered into commercially negotiated agreements with several CLECs to exchange traffic at or below the $0.0007 per minute rate.[19] These commercial arrangements make two things clear: (1) that any default intercarrier compensation rate should be just that, a default rate that applies only in the absence of a negotiated arrangement, which the Commission should encourage; and (2) that a national default rate of $0.0007 for VoIP traffic that connects with the PSTN is the right approach and it is consistent with marketplace developments.[20]

2. Traffic pumping. The Commission should prevent carriers from further gaming absurd variations in intercarrier compensation rates by clamping down now on the various forms of traffic pumping schemes that have proliferated in recent years. Variation in intercarrier

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[17] *See Bandwidth.com Enters Into a Groundbreaking Commercial Agreement with Verizon for the Exchange of VoIP Traffic*, http://bandwidth.com/about/read/verizonAgreement.html (Jan. 18, 2011).

[18] *See* Comments of Verizon and Verizon Wireless, *Developing a Unified Intercarrier Compensation Regime*, WC Docket Nos. 05-337 et al., at 49-50 (Nov. 26, 2008).

[19] *Id.*

[20] Concerns about carriers' ability to track VoIP traffic are overstated. Companies that provide VoIP services or that enable VoIP providers to route their customers' traffic to and from the PSTN know that this traffic originates or terminates in IP format. There is no issue with, for example, cable companies that only originate traffic in IP. And other companies can work cooperatively to develop methods to determine which traffic is subject to the terms of a commercial agreement addressing VoIP traffic or, in the absence of such an agreement, to the new default rate. Notably, standard and reliable traffic factoring methods already used today for intercarrier compensation billing purposes can be employed. If there are additional concerns, the Commission could address VoIP traffic identification through certifications—and if necessary through audits. The Commission, for example, required carrier certifications to identify certain prepaid calling card traffic for intercarrier compensation and universal service contribution purposes in 2006. *See Regulation of Prepaid Calling Card Services*, Declaratory Ruling and Report and Order, 21 FCC Rcd 7290 (2006).

compensation rates will likely persist for a period of time even if the Commission moves quickly on comprehensive intercarrier compensation reform, because these reform measures will take time to implement. Traffic pumping ultimately costs consumers billions of dollars. And traffic pumping and other schemes will proliferate so long as there are rate disparities for arbitrageurs to exploit.

The Commission should also resolve the longstanding—and thanks to traffic pumping, increasingly troubling—gap in its rules regarding intraMTA wireless traffic terminated by CLECs. Like VoIP and dial-up ISP traffic, the Commission should set a default rate of $0.0007 for this intraMTA traffic. Unless the Commission acts promptly to address intraMTA arbitrage, this situation will emerge as the next evolution of the dial-up ISP arbitrage schemes that were finally resolved only late last year. The dial-up ISP schemes likewise siphoned billions of dollars that could have been put to productive uses and did not stop until the Commission took decisive action in the 2001 *ISP Remand Order*. And, as discussed above and in Verizon's initial comments in this proceeding, the enormously positive consumer benefits that have resulted from the Commission's decade-old policy of uniform, low intercarrier compensation rates for most wireless traffic are at risk for so long as the Commission fails to act.

Although the FCC has, in the past, found it appropriate to allow state commissions to set rates in the first instance for intraMTA wireless traffic terminated by CLECs—and the D.C. Circuit recently found that determination to be legally permissible[21]—there are at least two reasons for the Commission, in this proceeding, to set a default rate for this traffic. First, in those prior decisions the Commission was addressing rate-setting for intraMTA traffic terminated by CLECs on a stand-alone basis. Here, in contrast, the Commission is engaged in a rulemaking

[21] *See MetroPCS Calif., LLC v. FCC*, No. 10-1003, slip op. at 4-6 (D.C. Cir. May 17, 2011).

designed to result in a uniform intercarrier compensation regime. Such uniformity will be delayed, at best, and impossible, at worst, if carriers must approach the more than 50 different state commissions to adjudicate disputes about rates before the Commission will act to ensure uniformity. Second, the Commission defended its prior decision on the ground that there was no "detailed record" in that case of "industry-wide competitive distortion" with respect to intraMTA wireless traffic terminated by CLECs.[22] But as CTIA, Sprint, T-Mobile, and others have demonstrated on the record *here*, the incidence of intraMTA traffic pumping by CLECs has increased since the Commission issued that decision, as CLECs have improperly attempted to apply their tariffed access charge rates to traffic subject to the Commission's intraMTA rule.[23] Accordingly, it is now necessary for the Commission to directly set the rate for such traffic, as the D.C. Circuit has confirmed it has the authority to do.[24]

3. <u>CETC support</u>. The Commission should immediately phase-out remaining USF support to CETCs. Eliminating what is left of this support now will put all wireless carriers on the same footing and provide a source of funding for the broadband-based intercarrier compensation and USF reforms adopted in this proceeding. The only way to ensure adequate funding for these new broadband priorities without burdening consumers with a dramatic increase in USF charges is to eliminate and repurpose remaining CETC support.

There is broad support to eliminate the remaining CETC subsidies and to put this funding to better use. *See, e.g.*, National Cable & Telecommunications Association (NCTA) Comments at 5-7; Comcast Comments at 12-15; XO Comments at 37-39; Sprint Comments at 32-34;

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[22] Brief for Respondents at 38, *MetroPCS Calif., LLC v. FCC*, No. 10-1003 (D.C. Cir. filed May 27, 2010).

[23] *See* Sprint April 1 Comments at 22; CTIA April 1 Comments at 4; T-Mobile April 1 Comments at 4.

[24] *See MetroPCS Calif., LLC*, No. 10-1003, slip op. at 4-6.

Nebraska Public Service Commission ("Nebraska PSC") Comments at 17. Commenters opposed to eliminating duplicative CETC support are mainly those parties currently receiving this support. *See, e.g.*, United States Cellular ("U.S. Cellular") Comments at 59-64; Rural Cellular Association (RCA) Comments at 15. These parties suggest that they are currently using the support to provide competitive options in high cost areas. Section 254 of the Act, however, is not designed to support multiple providers in areas that are prohibitively expensive for even one carrier to serve. Universal service support should be targeted to the most efficient provider in the best position to serve an area that is today unserved or that would not be served without support.

Not only is CETC support costly, but it creates pricing distortions that impede deployment of broadband and other next-generation technologies. For example, one analyst report concluded that while many consumers are drawn to high-end smartphone and other advanced wireless products, others have been "trading down" to more basic wireless plans because USF subsidies make lower-end products artificially cheap.[25] The analyst concluded that the resulting artificial market segmentation particularly harms providers such as Sprint and T-Mobile, which are "stuck in the middle."[26] The Commission should not leave in place a regime that creates such competitive distortions.

Moreover, in the short term, the only way to free up sufficient USF support for the Commission's USF and intercarrier compensation reform objectives in this proceeding is to follow through on the National Broadband Plan recommendation and Commission proposal to eliminate remaining CETC support in addition to the Verizon Wireless and Sprint funding.

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[25] *See* Bernstein Research, U.S. Telecommunications: The Wireless Barbell (May 10, 2011).

[26] *Id.* at 1.

NPRM ¶¶ 248-58.[27] There is no cause for delay. The Commission should include final rules for this necessary step in its next universal service and/or intercarrier compensation reform item.

All the pieces are in place, and there are no impediments to eliminating this legacy voice support immediately. The National Broadband Plan recommendations to free up broadband funding by first repurposing CETC support were issued in March of last year. NBP at 147-48. In the *Connect America Fund NPRM* (issued in April of last year), the Commission then provided notice of and sought comment on how to implement these reductions. *Connect America Fund NPRM* ¶¶ 59-62. Interested parties commented extensively then, as they have here, on the proposed reductions in current high cost universal service support teed up in the National Broadband Plan and in the initial Connect America Fund proceeding.[28]

Further, in the *Corr Order* (issued in September 2010), following extensive comment from all interested parties, the Commission adopted detailed, workable procedures to phase out Verizon Wireless and Sprint support pursuant to merger conditions, which can now be applied industry-wide. *Corr Order* ¶¶ 14-17. At the same time the Commission provided explicit, detailed instructions to the Universal Service Administrative Company to administer these support reductions. *Id*. ¶¶ 18-22. Finally, the Commission cleared the last operational hurdle

[27] *See also Connecting America: The National Broadband Plan*, http://download.broadband.gov/plan/national-broadband-plan.pdf, at 147-48 (2010) ("National Broadband Plan" or "NBP"); *Connect America Fund*; *A National Broadband Plan for Our Future*; *High-Cost Universal Service Support*, Notice of Inquiry and Notice of Proposed Rulemaking, 25 FCC Rcd 6657, ¶¶ 59-62 (2010) ("*Connect America Fund NPRM*"); *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service; Request for Review of Decision of Universal Service Administrator by Corr Wireless Communications, LLC*, Order and Notice of Proposed Rulemaking, 25 FCC Rcd 12854 (2010), *reconsideration pending* ("*Corr Order*").

[28] *See, e.g.*, Comments of the USA Coalition, *Connect America Fund*; *A National Broadband Plan for Our Future*; *High-Cost Universal Service Support*, WC Docket Nos. 10-90 & 05-337; GN Docket No. 09-51, at 41-54 (July 12, 2010) ("CAF NPRM Comments"); CTIA CAF NPRM Comments at 5-12; Qwest CAF NPRM Comments at 20-24; NECA, NTCA, OPASTCO, WTA and Rural Alliance CAF NPRM Joint Comments at 34-45.

just before the new year, changing the interim CETC cap procedures so that when a carrier relinquishes its ETC status in particular states—which may happen as support is eliminated—funding will now be freed up for new USF priorities instead of being redistributed under existing voice support programs to other CETCs in the state.[29]

Specifically, the Commission can, and should, act now to eliminate CETC support this year for multiple wireless handsets in the same household. *NPRM* ¶ 257. The National Broadband Plan recognized that "[i]n order to accelerate the phase-down of legacy support, the FCC could *immediately adopt a rule* that any wireless family plan should be treated as a single line for purposes of universal service funding." NBP at 148 (emphasis added). The Commission has similarly proposed to codify its long-standing view that Lifeline support must be limited to a single line per residence in order to achieve the statutory goal of providing "telecommunications access to low-income subscribers, while at the same time controlling the growth of the universal service fund and preventing waste, fraud, and abuse."[30] Indeed, the Commission has become so concerned that multiple ETCs are seeking reimbursement for Lifeline service provided to the same residence, it has indicated that interim action may be necessary to "address immediately the harm done to the Fund by USAC reimbursing ETCs for duplicate claims."[31] The concern over supporting multiple wireless handsets in the same household should be just as great. In 2010 dollars, over the next decade eliminating CETC support for multiple handsets in the same

[29] *High-Cost Universal Service Support; Federal-State Board on Universal Service,* Order, 25 FCC Rcd 18146, ¶ 5 (2010).

[30] *See Lifeline and Link Up Reform and Modernization*; *Federal-State Joint Board on UniversalService*; *Lifeline and Link Up*, Notice of Proposed Rulemaking, 26 FCC Rcd 2770, ¶ 47 (2011) ("*Lifeline NPRM*").

[31] *Id.*, ¶ 53.

household could help free up nearly $6 billion for new USF priorities. *See id.* ¶ 32. In addition to the *NPRM*'s inquiry regarding family plan subsidies, the Commission provided for notice and comment on eliminating duplicative family plan support as an initial step (*i.e.,* in 2011) toward eliminating legacy CETC support last July. *Connect America Fund NPRM* ¶ 60.

Those still opposed to accelerating the phase-out of remaining CETC support do not offer any rational basis to continue using scarce universal service resources to fund multiple connections in the same household in high cost areas. U.S. Cellular Comments at 62-64. Nonetheless, the "initial reduction" to CETC support need not be tied to duplicative subsidies for family plan handsets if the Commission prefers a different approach. The Commission could, for example, eliminate 40 percent of the remaining legacy CETC funding before the end of 2011 (and phase out reductions to the remaining 60 percent of this support) over the next few years. This alternative approach would be consistent with the Commission's implementing procedures for the Verizon Wireless and Sprint reductions. *Corr Order* ¶ 18.

After an initial reduction in legacy CETC funding before the end of 2011, the Commission should eliminate remaining support in equal percentage amounts over the next few years consistent with the procedures laid out in the *Corr Order*. *Id.* ¶¶ 14-17. The National Broadband Plan recommends that the Commission complete the phase-out within five years, by 2016. NBP at 144. As a practical matter, however, if the Commission moves promptly the CETC phase-out may be substantially complete well before then—thus freeing up more funding more quickly to support broadband deployment.

III. RESTRUCTURING INTERCARRIER COMPENSATION REGIMES IS CRUCIAL TO AVOIDING CONSUMER HARM AND TO FACILITATING THE TRANSITION TO NEXT-GENERATION TECHNOLOGIES.

A. Consumers Will Benefit from Unified and Reduced Intercarrier Compensation Rates.

Some commenting parties gloss over or ignore the central fact that should drive the outcome of this proceeding: the evidence is overwhelming that consumers will benefit from an efficient, pro-competitive intercarrier compensation regime with a single, low default rate that applies to all providers.

1. Arbitrage caused by disparate rates, and by the incentives for some carriers to exploit their higher rates by aggregating large volumes of traffic, is harmful—and consumers pay the price. Just one of the many types of arbitrage, traffic pumping, will burden wireless carriers alone with an estimated $170 million in excessive access charges in 2011.[33] As long as providers are required to pay millions of dollars to arbitrageurs, consumers will pay higher prices for the services purchased and will suffer as fewer funds are available for network investment and deployment of next-generation services. Although the Commission is appropriately taking expedited action to curb the worst traffic pumping schemes, arbitrageurs will find ways to exploit the system unless and until comprehensive reform is fully implemented. *NPRM* ¶ 40. So it is imperative that disparate rates be unified and reduced to levels that make arbitrage schemes unprofitable.

2. Whenever the input costs of an entire set of providers are reduced, consumers reap the benefits of the lower cost structure through market forces. Economic principles,

[33] *See* Connectiv Solutions, "The Impact of Traffic Pumping-Overview of 2010," http://www.connectiv-solutions.com/traffic-pumping.html ("Connectiv Solutions Study"). Fewer than 1% of wireless customers generate 9% of wireless long distance costs. *Id.*

confirmed by empirical research, as well as policy analyses by the Commission and others, establish that such consumer benefits are concrete. In short, cost reductions permit economic pricing and efficient investment. For example, as discussed above, the consumer welfare benefits from low local termination rates for wireless traffic have been enormous. Building on Commission decisions to establish low rates for most wireless traffic that connects with the PSTN, attractive bucket-of-minute and other wireless plans have flourished. Wireless subscriptions now exceed 300 million, roughly triple the number of subscriptions at the time of the *ISP Remand Order*; wireless penetration has also nearly tripled in that time, and now stands at 96 percent.[34] Indeed, by the first half of 2010, more than 51 percent of people ages 25-29—and more than 26 percent of all households—used *only* wireless phones, each roughly *eight-fold* increases from the first half of 2003.[35] Wireless customers make 2.2 trillion minutes of calls annually.[36] And this growth has contributed to the overall economy, as demonstrated by the dramatic increase in wireless carriers' payrolls over the last decade to $13 billion from $2 billion.[37]

The consumer benefits of low intercarrier compensation rates on the wireline side are just as tangible. Empirical economic studies have demonstrated that long distance carriers historically lowered retail prices in the wake of switched access reductions.[38] Indeed, two

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[34] *See* Wireless Quick Facts.

[35] National Center for Health Statistics, *Wireless Substitution: Early Release of Estimates From the National Health Interview Survey*: *compare* January-June 2010, http://www.cdc.gov/nchs/data/nhis/earlyrelease/wireless201012.pdf (Tables 1 and 2) *with* July–December 2006, http://www.cdc.gov/nchs/data/nhis/earlyrelease/wireless200705.pdf (Tables 1 and 2).

[36] Wireless Quick Facts.

[37] *Id.*

[38] *See, e.g.*, R.W. Crandall & L. Waverman, *Talk is Cheap: The Promise of Regulatory Reform in North American Telecommunications*, Brookings Institution Press (1997); W.E. Taylor

relatively recent studies concluded that consumers benefitted from market-driven long distance price reductions that were close to 100 percent of the reduction in long distance providers' switched access costs.[39] Whether the benefits come in the form of lower pricing, increased output, or increased innovation, consumers clearly are winners when intercarrier compensation rates are unified and reduced. As discussed above, the consumer benefits of not imposing a new, irrational tax on VoIP are particularly strong.

Comprehensive reform of intercarrier compensation is crucial right now, when wireless and broadband innovation and investment are transforming the communications landscape. Reducing and unifying intercarrier rates will increase funds available to invest in next-generation networks and technologies and advance the Commission's modernization and broadband goals. Competition to deploy 4G networks, for example, will be more extensive and more robust under a rational intercarrier compensation regime. That fact is illustrated by the tremendous wireless growth and corresponding consumer benefits that occurred over the last 10 years since the

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(Continued . . .)
& L.D. Taylor, "Postdivestiture Long-Distance Competition in the United States," 83 American Economic Review 2, 185-190 (1993).

[39] *See* D.J. Aron, et al., "An Empirical Analysis of Regulator Mandates on the Pass Through of Switched Access Fees for In-State Long-Distance Telecommunications in the U.S.," http://ssrn.com/abstract=1674082 (Oct. 14, 2010); R. Beard et al., "The Flow Through of Cost Changes in Competitive Telecommunications: Theory and Evidence", http://www.aestudies.com/library/bootflow.pdf (2005). Aron et al. note that the earlier empirical research, while confirming that consumers benefitted from switched access rate reductions, had not explored whether those benefits might have been associated with regulatory mandates that long distance carriers "flow through" access charge reductions to end users. The authors therefore account for that variable in their study. They conclude that there was no statistically significant difference in the level of consumer benefit based on whether or not the regulator had imposed a "flow-through" requirement. *See* Aron et al. at 32. They observe, moreover, that based on economic principles, regulator-mandated flow-through requirements can be expected to "affirmatively harm consumers by distorting prices." *Id*.

Commission decisions that established uniform, low rates for the majority of wireless traffic exchanged with the PSTN.[40]

3. It is also well settled that consumers benefit from the efficiencies achieved when pricing signals in the market more closely reflect the costs of the services and products consumers demand. Requiring wireless and long distance providers and their customers to subsidize the local service offerings of purportedly high-cost LECs may have some superficial appeal for the communities whose local providers receive such payments. *See, e.g.*, NECA Comments at 20-21 (opposing steep reductions in RLEC access rates because of potential "upward pressure on end-user local rates"). The reality is, however, that reducing or eliminating such intercarrier transfers translates into concrete consumer benefits. Continuing to require payers of intercarrier compensation to transfer billions of dollars to other carriers substantially distorts pricing signals, which harms consumers by delaying or preventing competitive entry into underserved areas and deployment of next-generation services. Prominent economists have propounded the consumer benefits of more efficient telephone pricing since before the break-up of AT&T. For example, more than twenty years ago, Alfred Kahn and William Shew concluded that:

> Some commenters have asserted, apparently in all seriousness, that telephone pricing is in any event a 'zero-sum game' because whatever we take off customers' long distance bills, we simply add to their local charges in the aggregate. The central conception of economics, on the contrary, is that moving in the direction of efficient pricing is far from a zero-sum game. What these observers fail to grasp is that prices *below* marginal costs cause a loss in social welfare just as much as prices above marginal costs. These two inefficiencies do not offset one another; they are additive. . . .Whatever the historic justification for the system of pricing still in effect today, it has long since disappeared. Its social cost today is to be reckoned not merely in terms of a multi-billion dollar annual

[40] As in this proceeding, rural ILECs argued then that those Commission decisions would devastate their business models and lead to harmful outcomes. Those predictions, of course, turned out to be wrong. *See* Verizon April 18 Reply Comments at 7-8.

> static welfare loss, but, perhaps even more important, in the ways in which it has discouraged the exploitation of one of our most dynamic, versatile technologies.[41]

The Commission has also confirmed that "inefficient rate structures lead to inefficient and undesirable economic behavior."[42] It has therefore repeatedly concluded that economically efficient competition and the consumer benefits it yields cannot be achieved as long as some carriers are authorized to collect their network costs from their competitors and their competitors' customers.[43] And with specific regard to rural areas, the Commission has found that rationalizing switched access rates enhances incentives for providers to originate service and foster facilities-based competition for residential subscribers.[44]

4. State regulators and consumer advocates have reached the same conclusions about the important consumer benefits—including lower prices and increased investment—that flow from reductions in intercarrier compensation rates. The state members of the Federal-State Joint Board on Universal Service, even while urging the Commission to refrain from substantially disturbing the existing intercarrier compensation regime, acknowledge that low access rates "create public benefits" and that "toll rates will decline." State Members May 2 Comments at

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41 A. E. Kahn & W. B. Shew, "Current Issues in Telecommunications Regulation: Pricing," 4 Yale J. on Reg. 191, at 208-209, 255-256 (1987).

42 *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long Distance Users; Federal-State Joint Board On Universal Service*, Sixth Report and Order in CC Docket Nos. 96-262 and 94-1, Report and Order in CC Docket No. 99-249, Eleventh Report and Order in CC Docket No. 96-45, 15 FCC Rcd 12962, ¶ 129 (2000) ("*CALLS Order*").

43 *See generally CALLS Order*; *Multi-Association (MAG) Plan for Regulation of Interstate Services of Non-Price Cap Incumbent Local Exchange Carriers and Interexchange Carriers*, Second Report & Order and Further Notice of Proposed Rulemaking in CC Docket No. 00-256, Fifteenth Report & Order in CC Docket No. 96-45, and Report & Order in CC Docket Nos. 98-77 and 98-166, 16 FCC Rcd 19613 (2001) ("*MAG Order*"); *Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, Seventh Report & Order and Further Notice of Proposed Rulemaking, 16 FCC Rcd 9923 (2001) ("*CLEC Rate Cap Order*").

44 *MAG Order* ¶ 11.

148. Similarly, the Massachusetts Department of Telecommunications and Cable ("Massachusetts DTC") found, when requiring CLECs to reduce their intrastate switched access rates, that "by capping these inter-carrier rates, a market distortion will be removed, thus furthering competition within the telecommunications industry. . . . [T]his increased competition will result in lower long distance rates for consumers in the Commonwealth."[45] In New Jersey, the consumer advocate recently summarized the economic learning on consumer benefits, noting that the benefits are expected to correspond to the amount of the reduction in intercarrier compensation rates:

> [R]educing intrastate access … will benefit consumers. Switched access is an essential component of a carriers' [sic] retail service. The cost and availability of this essential element affects the rates for retail services that consumers purchase. Lowering rates closer to the underlying costs should stimulate demand. In addition, economically efficient pricing signals lead to efficient investment decisions by suppliers and lead to efficient purchasing by consumers. In competitive markets, if costs of inputs decline, the rate for the output should decline by a corresponding amount.[46]

Against that backdrop, a few commenters— the National Association of State Utility Consumer Advocates (NASUCA), for example—are simply wrong in challenging the "mantra" that the existing system needs to be fixed. NASUCA Comments at 87 (asserting that there is "scant" evidence that the present system is "inefficient or "wasteful"). Neither NASUCA nor any other party cites a study—or even advances a reasoned argument—that might form the basis to question the consumer benefits that flow from reduced intercarrier compensation rates.

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[45] Final Order, *Petition of Verizon New England et al. for Investigation under Chapter 159, Section 14, of the Intrastate Access Rates of Competitive Local Exchange Carriers*, Docket No. D.T.C. 07-9, at 1 (Mass. Dep't. Tel. & Cable June 22, 2009).

[46] Reply Brief of New Jersey Division of Rate Counsel, *Investigation Regarding and Review of Local Exchange Carrier Intrastate Exchange Access Rates*, Docket No. TX08090830, at 2 (N.J. Bd. Pub. Utils. filed Dec. 4, 2009).

Moreover, one of the primary purposes of the 1996 Act, and this proceeding, is to move away from implicit (and uneconomic in a competitive market) intercarrier compensation subsidies.

B. A Single Low Default Terminating Rate for All Providers and All Traffic Is the Best Intercarrier Compensation Solution, and the Proposals of NECA and Others to Perpetuate the Status Quo Would Harm Consumers.

Despite the extensive evidence that reforming the existing intercarrier transfer scheme will promote investment and benefit consumers, a number of parties urge the Commission to perpetuate—or only to modify modestly and over a long period of time—the status quo. Such proposals should be rejected because they do nothing to address the distortions, inefficiencies, and arbitrage incentives that plague the industry and harm consumers.

First, the Commission should reject arguments that the final result of reform should be a single terminating rate for each *carrier*, rather than a uniform rate for the industry. NECA, for example, argues that switched access rates should be "unified" on an "individual company basis," and urges that "neither a uniform national rate nor a uniform transition period should be adopted." *See* NECA Comments at 20; s*ee also* State Members May 2 Comments at 147-48, 153-55; Sprint Comments at 8-11. A "uniform" rate per carrier, of course, is not uniform at all. Perpetuating rate disparities among carriers will not address the inefficiencies and arbitrage that plague the intercarrier compensation system today. To the contrary, as discussed above, as long as some providers are permitted to charge higher rates than others, there will be a financial incentive for terminating carriers to manipulate traffic to route it to, and through, those carriers that are permitted to charge the higher rates and, conversely, for originating carriers to manipulate routing so as to avoid those higher rates. The Commission should not permit reform opponents to cloud the reality that "wasteful attempts to game the system will likely persist as long as ICC rates remain disparate and well above carriers' incremental costs of terminating a call." *NPRM* ¶ 40.[47]

Second, proposals to pursue only minor intercarrier compensation reductions over long periods of time should be rejected as attempts to perpetuate the existing anti-consumer system. Under NECA's proposal, there would be *no* reductions in any interstate rates, and possible reductions of intrastate rates to interstate levels would happen on a vague timeline and at the "discretion" of state commissions. NECA Comments at 13. Similarly, Frontier advocates a five-year step-down in intrastate rates to interstate levels, at the end of which it urges the Commission to pause and evaluate what the "appropriate end rate" might be. Frontier Comments at 5-7. But *as long as* excessive and non-uniform access rates persist, arbitrage schemes will proliferate and consumers will be denied the benefits of a rational and efficient intercarrier compensation regime. Firms that continue to cling to uneconomic subsidies via intercarrier transfer payments

[47] The State Members are theoretically right that certain arbitrage schemes would be eliminated under a system where every carrier's terminating rate reflects its precise costs for providing terminating access. State Members May 2 Comments at 153-54. However, regulators, no matter how well-intentioned, cannot develop precise cost methodologies—and apply them on an individual company basis across all 50 states—such that would-be arbitrageurs' rates truly reflect the right measure of costs for the particular activities in which they may become involved. *Cf.* 47 U.S.C. § 252(d)(2)(B)(ii) (providing that neither the Commission nor state commissions are authorized to engage in any proceeding "to establish with particularity the additional costs of transporting or terminating calls"). As the Commission and courts have observed, ratemaking "is not an exact science." *See, e.g., AT&T Corp. et al v. Virgin Islands Tel. Corp., d/b/a Innovative Tel.*, 19 FCC Rcd 15978, ¶ 17 (2004); *see also e.g., Qwest Corp. v. FCC*, 258 F.3d 1191, 1206 (10th Cir. 2001). Opportunities for gamesmanship under such a system would be high. For example, the State Members propose that every carrier's costs would be ascertained just once (in 2012) and that the resulting rate would apply until 2017. State Members May 2 Comments at 154. That would create numerous opportunities for abuse, including by firms that establish their rates by demonstrating high costs and then upgrade (and/or increase traffic volumes) in order to reduce their per-unit costs and achieve exploitable profit margins. Moreover, while cost-based rates might address existing traffic-aggregation schemes like traffic pumping, new schemes can be expected to emerge under a system of disparate rates under which firms would arbitrage rate differences across and among carriers. In addition, cost-based rate regulation leads to network gold-plating and provides a disincentive to move to more efficient technologies—and also produces endless litigation over which costs should "count."

must be given incentives to *reduce* that dependence. The only way to create such incentives is to establish a glide path that requires meaningful reductions over a reasonable but swift period, not longer than three years. To provide a "soft landing" (*see* below) for carriers that have not yet restructured their operations to compete on a level field, the Commission can create a transitional access replacement mechanism within the USF, provided that the mechanism is truly transitional (that is, sunsets on a date certain such as in three years) and is structured to reduce—rather than perpetuate—dependence on explicit and implicit subsidies.

It is telling that none of the proponents of the "slow roll" approach to intercarrier compensation reform engages the overwhelming economic evidence about the benefits of reform. For example, the only discussion in NECA's comments about the effect of intercarrier compensation reform on consumers is a red herring. Instead of acknowledging the benefits that flow from intercarrier compensation reductions, NECA resorts to scare tactics, asserting that deep reductions in intercarrier compensation would cause end-user rates for local service to "skyrocket to unaffordable levels, and lead customers to discontinue service." NECA Comments at 23. Those scare tactics should be rejected. As an initial matter, it is unfair for some carriers and their customers to bear the burden of artificially suppressing retail rates in certain areas. For example, in a recent proceeding before the Washington commission, the commission staff's economist observed that Embarq's local rates were "completely upside down" because they were particularly low (as low as $8.90 per month for residential local service) in Embarq's more rural, higher-cost territory.[48] Dr. Blackmon explained that it was problematic for Embarq to charge only $8.90 for residential local service while "asking customers in other parts of the state who

[48] *See* Testimony of Glenn Blackmon, *Verizon Select Servs. Inc. v. United Tel. Co. of the Northwest*, Docket No. UT-081393, at 8-9, 29 (Wash. Utils. and Transp. Comm'n filed June 5, 2009).

are paying twice that rate to fund a subsidy."[49] Because of Embarq's substantial headroom to recover its network costs from its own customers, and because Embarq had failed to present evidence that its $0.06851 per minute "universal service" rate element was actually needed to subsidize any high-cost exchanges, Dr. Blackmon advised that requiring Embarq to reduce its switched access rates (including elimination of the $0.06851 rate element) would not raise any universal service concerns.[50]

Moreover, consumers have options. Even if a LEC were to raise rates, consumers could choose to "cut the cord" and rely on wireless for voice service as more than 25 percent of all households—more than half of households in some demographics—already do today.[51]. In addition, consumers can now choose from a host of cable and other VoIP products. In any event, in spite of having had several years to prepare for competition and its affects on access revenues, some parties suggest that certain carriers may yet need an additional transition period to adjust their business models. Verizon and other advocates of intercarrier compensation reform do not oppose a transitional USF access replacement fund if the transition fund does not increase the amount of the current high cost fund, which should be capped overall. Firms could recover some of their lost switched access revenues for a finite period of time (such as three years) after raising their retail rates to bring them to market-based levels. *See* Verizon Comments at 18-21. The transition fund should disburse less than 100% of the intercarrier compensation revenue a carrier loses, and that amount should be further reduced each year to account for the overall declining nature of switched access revenues. *Id.*

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[49] *Id.* at 29.

[50] *Id.* at 17-18, 32-36. Dr. Blackmon also confirmed the well-accepted policy reasons why reducing and unifying switched access rates benefits consumers. *Id.* at 4-7.

[51] *Lifeline NPRM* ¶ 17 (citation omitted).

C. The Commission Has Legal Authority to Implement a National Terminating Rate of $0.0007.

1. Preemption Is the Most Straightforward Path to a Unified Default Rate for All Traffic.

Certain parties assert that the Commission lacks legal authority to preempt state regulation of intercarrier compensation for "intrastate" traffic. For example, the State Members argue that the Act "preserved existing State authority over the rates charged for intrastate access." State Members May 2 Comments at 143-44. Nearly all of the individual state commenters raise similar arguments.[52]

The fundamental problem with those arguments is that they are premised on an assumption that is now demonstrably false—namely, there is still a meaningful distinction between "interstate" and "intrastate" traffic. As Verizon has demonstrated, that is simply no longer true, as dramatic technological and marketplace changes in recent years have rendered *all* traffic inseverable and, therefore, interstate for jurisdictional purposes. Verizon Comments at 26-42. And these days most consumers simply do not conceive of "long distance" at all because it is an anachronism, relevant only to the backwards, broken intecarrier compensation system and divestiture restrictions that no longer apply. The Commission thus has authority to adopt a uniform default rate for all traffic pursuant to Sections 201 and 332 of the Act, and to preempt as inconsistent with this federal scheme any state regime that imposes higher rates for certain types of traffic.

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[52] *See*, *e.g.*, Michigan Public Service Commission ("Michigan PSC") Comments at 8-9 (arguing that "intrastate access remains under the jurisdiction of the states," and that "[s]tates are in the best position to tackle these intrastate issues"); Massachusetts DTC Comments at 20-21 (arguing that the Commission "does not have sufficient legal authority . . . to preempt states' intrastate access charge regimes"); New York Public Service Commission ("New York PSC") Comments at 7-12 (asserting that the FCC lacks authority to "override traditional state authority over intrastate access rates"); Regulatory Commission of Alaska ("Alaska Commission") Comments at 29-30.

Most importantly, millions of consumers and businesses are increasingly opting for IP-based communications services. Not only are those services offered independent of any geographic location, but they also offer integrated features and capabilities that allow customers to perform multiple voice and data communications simultaneously; these multifaceted services are designed to—and do—transcend the traditional distinctions between interstate and intrastate traffic. These services obliterate any notion of the "end points" of a "call," the traditional means by which the Commission has determined jurisdiction. Wireless services similarly transcend jurisdictional boundaries, as consumers can make and receive calls from the same telephone number anywhere in the United States (and, often, the world). As the Commission has recognized, the effect of these significant marketplace changes—and the development of intermodal number porting and location-independent services such as "pick-your-own-area-code" and "find-me-follow-me" services—is to make telephone numbers an increasingly poor "proxy" for ascertaining subscribers' geographic locations when making or receiving calls. *Vonage Order* ¶ 26; *see* Verizon Comments 27-34.

The Commission has in numerous cases preempted state regulation where—as here—it was not practical to separate a service into interstate and intrastate components, even if it were *technically* possible to do so. *See* Verizon Comments 34-37. That rule reflects the common-sense principle that carriers should not be forced to develop new functionalities that have no *service-driven purpose* merely to ensure that the states have an "intrastate" service to regulate. *See Vonage Order* ¶¶ 25, 29. Moreover, any attempt by state commissions to maintain rates for certain types of traffic that differ from the national default rate would pose a direct obstacle to the Commission's longstanding goal of achieving *comprehensive* intercarrier compensation reform, which is achievable only to the extent rate disparities are eliminated, and would invite the very arbitrage that the Commission is seeking to eliminate.

For these reasons the Commission can, and should, find that any state regime that differs from the uniform, federal default rate conflicts with—and poses an obstacle to—federal goals and policies, and is therefore preempted. *See* Verizon Comments 37-41. This approach is consistent with the Commission's statutory duty under Section 253 of the Act to exercise its preemption authority over state and local actions that conflict with the Commission's national policy objectives. 47 U.S.C. § 253. And very recent Supreme Court precedent also confirms the wide scope of the Commission's preemption authority when implementing national intercarrier compensation and universal service policy objectives. *See AT&T Mobility LLC v. Concepcion*, 2011 U.S. LEXIS 3367 (April 27, 2011). In its decision interpreting the Federal Arbitration Act, 9 U. S. C. § 2, the Supreme Court held in *Concepcion* that even general provisions of state law—in that case California common law disfavoring class arbitration waivers—can be preempted by a "liberal federal policy" where state action "stands as an obstacle to the accomplishment and execution of the full purposes and objectives" of a federal policy. *Id*. at *10, 33. That is true even where (as is the case with the Communications Act) an underlying federal statute reserves some role for the states when state action interferes with the "fundamental attributes" of a federal policy. *Id*. at *18.

2. The Commission Has Authority to Adopt a Uniform Default Rate Pursuant to Section 251(b)(5), But That Route Carries Additional Risks.

The Commission also has authority to adopt a uniform default rate pursuant to its authority to promulgate rules implementing section 251(b)(5). *See* Verizon Comments at 42-46. NECA nonetheless argues that—with respect to traffic subject to this provision—the

Commission "cannot mandate a specific rate for any intrastate traffic, nor can it prescribe a results-oriented 'methodology' that effectively leads to a pre-determined rate," and that the Commission's authority with respect to such traffic is "limited to establishing a methodology by which a *state commission* can set rates." NECA Comments at 16 fn.27. In support of that position, NECA cites the Eighth Circuit's decision holding that the Commission's role is limited to resolving "general methodological issues" and that "[s]etting specific prices goes beyond the [Commission's] authority to design a pricing methodology." *Iowa Utils. Bd. v. FCC*, 219 F.3d 744, 757 (8th Cir. 2000). The State Members similarly argue that an FCC-mandated default rate for traffic subject to section 251(b)(5) would intrude upon state commission authority over the negotiation and arbitration of interconnection agreements under section 252 of the Act. State Members May 2 Comments at 143-44.

Those arguments are misplaced. The Supreme Court held in *Iowa Utilities Board* that "the Commission has jurisdiction to design a pricing methodology" to implement the pricing standards in section 252(d). *AT&T v. Iowa Utils. Bd.*, 525 U.S. 366, 385 (1999). The Eighth Circuit apparently concluded, in the language quoted above, that design of a "pricing methodology" is at the outer limit of the Commission's authority, but nothing in the Supreme Court's decision compels that reading of *Iowa Utilities Board*. The Commission could thus adopt a "methodology" that caps intercarrier compensation rates at $0.0007 per minute and instructs ILECs, like all other carriers and providers, to look to their customers to recover any additional compensation for the work they perform. Indeed, Section 252(d)(2)(A)—which applies only to ILECs' rates, not to all rates for all traffic subject to Section 251(b)(5)—requires only that reciprocal compensation arrangements provide for the "mutual and reciprocal recovery" of each carrier's costs; that provision does not require that a carrier recover *all* of its costs from the originating carrier. *See* Verizon Comments 44-45. This issue is not without risk.[53]

Moreover, if the Commission attempts to achieve comprehensive intercarrier compensation through section 251(b)(5), section 251(f)(2) could pose an obstacle to the development of a uniform federal policy. That provision allows state commissions to "suspen[d] or modif[y]" the requirements of section 251(b)(5) as applied to rural carriers if a state commission concludes that it is necessary to: (1) avoid a significant adverse impact on consumers; (2) avoid imposing "unduly economically burdensome" requirements; or (3) avoid imposing "technically infeasible" requirements. 47 U.S.C. § 251(f)(2). Rural LECs may seek—and state commissions may grant—exemptions from any default rate the Commission adopts to cap the rates that can be charged under Section 251(b)(5) arrangements, absent a voluntary, commercial agreement. Such exemptions would disrupt a uniform rate regime—likely by preserving some of the highest intercarrier compensation rates that currently exist—and perpetuate many of the arbitrage problems that exist today precisely because of the extremely high rates that rural carriers charge. The exemption proceedings, moreover, would inevitably lead to additional litigation before the state commissions, the courts, and this Commission, diverting resources away from investment in and deployment of broadband networks and services.

The far safer course would be for the Commission to: (1) find that *all* traffic is inseverable and, therefore, interstate for jurisdictional purposes; (2) establish a uniform default rate for all traffic pursuant to section 201; and (3) preempt any state commission regime that

[53] If the Commission instead preempts state authority and establishes uniform rates pursuant to section 201, then section 252(d)(2) would pose no obstacle, as that provision applies only to pricing standards that implement section 251(b)(5) with respect to ILEC rates.

imposes rates higher than the uniform rate or otherwise conflicts with the Commission's objectives in this proceed (*see* below).

3. The Commission Has Authority to Establish a Uniform Default Rate for Wireless Traffic.

The State Members also assert that states have "exclusive authority over intrastate rates, including toll access rates," and thus the Commission has no authority to regulate the charges imposed by LECs for termination of wireless traffic. State Members May 2 Comments at 145. In particular, the State Members assert that section 332(c)(3) gives the Commission exclusive authority only over the "rates charged" by wireless providers, not the "price paid" for access services by such providers. *See also* Public Utilities Commission of Ohio ("Ohio Commission") Comments at 49-51 (arguing that preemption under section 332 "applies only to the regulation of *retail* rates and not to access or other non-retail rates").

The Commission should reject those arguments. The State Members focus on section 332(c)(3) but ignore section 332(c)(1), which grants the Commission plenary authority over CMRS interconnection and rates. That provision states that the Commission may order any common carrier to "establish physical connections with such [wireless] service *pursuant to the provisions of section 201*." 47 U.S.C. § 332(c)(1)(B). Section 201, in turn, provides that "[a]ll "charges, practices, classifications, and regulations" with respect to such services must be just and reasonable. Given that section 332(c)(1) expressly incorporates section 201, there is no basis for concluding—as the State Members argue—that the Commission only has authority over the rates *charged* by CMRS providers, but not the rates those carriers *pay* for access services. Indeed, the Commission's authority under section 201 is at its zenith when—as here—the Commission is exercising that authority in order to eliminate "distort[ions]" and "inaccurate price signals" that could "undermine[] the operation of competitive markets."[54] Indeed, the D.C. Circuit recently confirmed that sections 332 and 201, in combination, give the Commission the authority to set the intercarrier compensation rates wireless carriers pay, including for intrastate wireless traffic.[55] Although the court found that the Commission had given a sufficient explanation for its decision to "allow[]" the California commission a chance to set that rate in the first instance, the court left no doubt that the Commission could rely on sections 332 and 201 to "preempt any rates set by the state[] that would undermine" federal policy.[56]

Moreover, while Section 2(b) of the Act provides that "nothing in this chapter shall be construed to apply or give the Commission jurisdiction with respect to . . . intrastate communication service," that provision expressly does *not* apply to "section 332 of this title," which addresses wireless services. 47 U.S.C. § 152(b); *see also Iowa Utils Bd. v. FCC*, 120 F.3d 753, 800 n.21 (8th Cir. 1997). Congress has thus made clear that any residual state authority over purely intrastate services does not extend to wireless service.

The Commission has similarly emphasized that Section 332 "generally precludes states from rate and entry regulation" of wireless providers. *Local Competition Order* ¶ 1025. Although the Commission decided in the *Local Competition Order* to regulate intercarrier compensation for certain wireless traffic through section 251(b)(5), it expressly retained authority to regulate intercarrier compensation rates for wireless providers if necessary, noting that "[s]hould the Commission determine that the regulatory scheme established by sections 251

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[54] *Core Commc'ns, Inc. v. FCC*, 592 F.3d 139, 145 (D.C. Cir. 2010) (citations omitted).

[55] *See MetroPCS Calif., LLC*, No. 10-1003, slip op. at 4-6.

[56] *Id.* at 5, 6. As explained above, although the Commission in the past has declined to exercise that authority, in light of the need for uniformity and the increased incidence of intraMTA traffic pumping, the Commission should exercise its authority now. *See supra* page 13-14.

and 252 does not sufficiently address the problems encountered by CMRS providers in obtaining interconnections on terms and conditions that are just, reasonable, and nondiscriminatory, the Commission may revisit its determination not to invoke jurisdiction under section 332 to regulate LEC-CMRS interconnection rates." *Id.*[57] Although the Eighth Circuit (erroneously) rejected the Commission's view of its authority to implement section 251, that court agreed that section 332 grants the Commission authority to regulate intercarrier compensation for wireless traffic and upheld the Commission's reciprocal compensation rules for wireless traffic, even as it struck down the rest of the Commission's reciprocal compensation rules.[58] Thus, pursuant to section 332, the Commission plainly has jurisdiction to establish a uniform default rate for the termination of *all* wireless traffic, and the Commission should exercise that authority here.

D. The Commission Should Reject Proposals to Mandate IP Interconnection under Section 251(a) or (c).

Certain commenters argue that the Commission should mandate interconnection for the exchange of traffic in IP format. For example, Google asserts that "broadband service providers have a duty pursuant to Section 251(a)(1) . . . to interconnect with other network providers for the exchange of telecommunications traffic, including local traffic encoded in IP." Google Comments at 10-11. Similarly, Time Warner Cable argues that "the Commission should rely on its Section 251 authority to mandate acceptance of traffic in an IP format within a reasonable period of time." Time Warner Comments at 12-13; s*ee also* Cox Comments at 18-19. The Commission should reject those proposals.

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[57] *See also NPRM* ¶ 511 (noting that "there is support for the proposition that section 332 of the Act also gives the Commission authority to regulate the intercarrier compensation rates paid by wireless carriers for interstate traffic—including charges that would otherwise be subject to intrastate access charges").

[58] *See Iowa Utils. Bd.*, 120 F.3d at 800 n.21.

1. Rather than interpreting Section 251 to impose a mandate to exchange traffic in IP format, the Commission should allow commercial agreements to govern such interconnection, as they do on the Internet itself. Over time, as technologies and networks continue to evolve, the industry as a whole is likely to transition to IP-to-IP interconnection as networks are rebuilt and upgraded to accommodate such interconnection. But that transition is, and should continue to be, market-led. Industry participants—including both CLECs and ILECs—are currently engaged in discussions to identify and resolve the myriad issues associated with IP interconnection, including the need to develop industry standards for exchanging traffic in IP format.[59] Such interconnection standards are best established not through heavy-handed regulation, but through industry bodies and commercial agreements between providers, no different from the voluntary standards and agreements that govern the Internet today. In the absence of *any* regulation, owners of the networks that comprise the public internet have entered into countless commercial, voluntarily negotiated agreements that specify where and how traffic will be exchanged, and whether and how compensation will be paid for the exchange of that traffic. *See* Verizon April 1 Comments at 12-13.

Given that the industry is steadily migrating toward the widespread use of IP technology for voice traffic, there is no reason to believe that providers will be unable to reach voluntary, mutually beneficial agreements for the exchange of such traffic, once the standards and capability for doing so have been developed. The commercial agreements that should govern IP interconnection will be the most efficient way to address not only technical issues, but also the countless other details—such as administrative and financial responsibility for the necessary

[59] For example, the Alliance for Telecommunications Industry Solutions—which has members from more than 250 communications companies—has created a Task Force on Next Generation Carrier Interconnection that is working to develop IP network-to-network interconnection guidelines. *See* http://www.atis.org/ngiif/index.asp.

facilities and arrangements—that would be difficult comprehensively through a top-down interconnection mandate.

2. The Commission also lacks statutory authority to mandate that telecommunications carriers interconnect with other carriers in a manner that allows for traffic to be exchanged in IP format. Even putting aside that VoIP and broadband networks are simply not regulated under Title II of the Act, Section 251 provides no authority to mandate IP interconnection and does not specify the protocol or format of interconnection.

Section 251(a) simply requires telecommunications carriers to "interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers." 47 U.S.C. § 251(a). That provision leaves it up to individual carriers to determine how they will interconnect with other carriers and imposes no substantive duties with respect to the interconnection—other than that carriers ensure they are interconnected in some manner with all other telecommunications carriers. In particular, this provision does not require that interconnection be accomplished in any particular manner. Nor has the Commission ever interpreted Section 251(a) to impose any substantive duties with regard to the type of interconnection carriers establish. On the contrary, the Commission has explained that carriers have significant discretion under Section 251(a) to provide interconnection "based upon *their* most efficient technical and economic choices." *Local Competition Order* ¶ 997 (emphasis added). Section 251(a), therefore, provides no basis for an IP-interconnection mandate.

Nor can the Commission look to Section 251(c)(2) to impose an IP-interconnection mandate on incumbent LECs alone. Although Section 251(c)(2) does include certain substantive requirements—for example, incumbents must permit interconnection "at any technically feasible point within the carrier's network," 47 U.S.C. § 251(c)(2)(B)—Section 251(c)(2) does not give carriers the right to insist on delivering traffic in IP format. To the contrary, the Commission has made clear that "the term 'interconnection' under section 251(c)(2) refers only to the *physical linking* of two networks for the mutual exchange of traffic." *Local Competition Order* ¶ 176 (emphasis added). Moreover, the law is clear that incumbents have no obligation to create *new* facilities or capabilities that do not currently exist, simply to accommodate a CLEC's preference for delivering its traffic in IP format. As the Eighth Circuit has explained, the Act requires access "only to an incumbent LEC's *existing* network — not to a yet unbuilt superior one." *Iowa Utils. Bd.*, 120 F.3d at 813 (emphasis added); *see also id.* (noting that the Act "does not mandate that incumbent LECs cater to every desire of every requesting carrier"). In addition, 251(c)(2) only applies to "telephone exchange service" and "exchange access"—and the Commission (correctly) has never held that VoIP meets either of these definitions. 47 U.S.C. §§ 153(16) & (47), 251(c)(2).

3. Even if Section 251(a) or 251(c)(2) were ambiguous on these points, it would be unreasonable for the Commission to interpret either provision to mandate IP interconnection. First, Section 251 was designed to address the *legacy* public switched telephone network—and, in Section 251(c), the specific regulatory history that led to the existence of incumbent local exchange carriers. IP traffic requires the investment in and deployment of next-generation broadband networks, where—as the Commission has recognized—there is no similar regulatory history. Instead, providers of all stripes are equally well situated to invest in this new technology.[60] Indeed, with respect to IP networks, there are no incumbents; all providers are

[60] See, e.g., *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers; Implementation of the Local Competition Provisions of the Telecommunications Act of 1996; Deployment of Wireline Services Offering Advanced Telecommunications Capability*, Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, 18 FCC Rcd 16978, ¶ 275 (2003) ("*Triennial Review Order*") (noting

"new entrants." There is no reason to interpret Section 251 to impose interconnection mandates with respect to broadband networks, thereby subjecting those networks and providers to the kinds of costly and lengthy litigation that for years followed the adoption of the Commission's rules governing interconnection to the legacy PSTN. Such costs would deter necessary investment in the increased deployment of broadband networks and services.

IV. UNIVERSAL SERVICE REFORM SHOULD FOCUS ON CAPPING HIGH COST FUNDING OVERALL, FOLLOWED BY TARGETED, EFFICIENT SUPPORT FOR BROADBAND NETWORKS IN AREAS THAT ARE UNSERVED OR WOULD NOT BE SERVED WITHOUT SUPPORT.

A. There Is Broad Agreement with the Commission's Proposal to Cap the High Cost Fund, and Over Time the Fund Should Shrink.

There is significant agreement among commenters regarding the need for the Commission to adopt its proposal to cap all high cost funding at current levels and commit that "total disbursements should be lower in the future to minimize the burden on consumers." *NPRM* ¶ 23; *see also* NCTA Comments at 4-5; Comcast Comments at 11-12; XO Comments at 36-37; New York PSC Comments at 6-7; Massachusetts DTC Comments at 8-9; New Jersey Board of Public Utilities Comments at 3-4; Florida PSC Comments at 2. Indeed, substantial growth in high cost funding over the last several years leaves no doubt that the most important first step in universal service reform is to set a reasonable high cost budget that consumers can afford. And to reduce support in the future the Commission should rely on market-based mechanisms such as a competitive bidding process (*see* below) to ensure that the fund benefits from the most efficient providers and technologies.

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that, with respect to advanced broadband network infrastructure, "entry barriers appear to be largely the same for both incumbent and competitive LECs," and that incumbent LECs "do not have a first-mover advantage").

The Commission must hold fast to its commitment in the NBP and the *NPRM* to "proceed with measured steps to assure that as it advances the nation's broadband goals, it does not increase the USF contribution factor, which is already at a public historic high." NBP at 150.[61] Moreover, there is no practical reason why consumers should not be assured that high cost funding will actually decrease from its historically high levels over time. As broadband networks are in fact deployed into those few remaining areas that still lack access, and as technology makes delivery of advanced services less expensive (*see* below discussion regarding LTE wireless and satellite broadband deployment), consumers should see benefits in the form of reduced USF contributions.

B. Revenue-Neutral Recovery from the USF Is Not Necessary Nor Fair to Consumers Who Pay for the Fund.

While most commenters agree that controlling the size of the USF as the Commission repurposes the fund for broadband is essential, some parties continue to argue that *all* losses to revenue resulting from intercarrier compensation reform must be recovered through new USF subsidies. *See, e.g.,* NECA Comments at 13-20; CenturyLink Comments at 64, 66. Revenue-neutral recovery from the USF is not necessary nor fair to consumers who ultimately pay for the fund, and it is flatly at odds with the Commission's goals of controlling the size of the new fund and providing appropriate incentives for companies to "accelerate the migration to all IP networks." *NPRM* ¶ 559. Any new "access replacement" funding should come from a USF mechanism that would be part the current high cost fund (which should be capped at current levels) and that is truly a transition fund. Transition funds should be available only to the extent firms recover a reasonable amount of their network costs by charging their end users a

[61] The National Broadband Plan notes that the USF will have nearly doubled this decade, growing from approximately $4.5 billion in 2000 to a projected $8.7 billion in 2010. NBP at 150.

reasonable retail rate, not an artificially low rate, should provide less than dollar-for-dollar recovery in order to avoid perpetuating dependence on subsidies, and should go down over time and sunset quickly (such as over three years).

To the extent the Commission adopts an intercarrier compensation recovery mechanism, it should be narrowly tailored so as to provide carriers the minimum time that would be necessary to expeditiously implement a business plan that is not dependent on the flow of carrier-to-carrier subsidies. History shows that some carriers will not break their dependence on this support unless and until comprehensive reform forces their hands. Indeed, some carriers are reporting the exact same level of dependence on intercarrier compensation revenues today that they reported over six years ago, notwithstanding the unmistakable decline in switched access traffic minutes.[62] Permitting carriers simply to shift all of their intercarrier compensation revenues to a more direct subsidy stream through the USF would be counterproductive; this approach would only increase dependence on the very uneconomic subsidies the Commission proposes to phase out. *See, e.g.,* Time Warner Comments at 8 (noting that government-guaranteed revenue protection is an "article of faith" among rural LECs).

Under no circumstance should the Commission permit dollar-for-dollar recovery of lost access charge revenues from the fund. *See* Comcast Comments at 19-20; AT&T Comments at 32. Permitting carriers to recover all of their lost intercarrier compensation revenue is not only

[62] For example, NECA reports that 29 percent of its members' revenue is derived from interstate and intrastate access charges, which is the exact same percentage of typical revenue reported by NECA for its members in 2005. *Compare* NECA Comments at 13 *with* its comments (filed as the National Exchange Carrier Association) in *Role of the Universal Service Fund and Intercarrier Compensation in the National Broadband Plan*, GN Docket Nos. 09-47, 09-51, 09-137, at 27 (Dec. 7, 2009) (stating that, in 2005, an average 29 percent of its incumbent carriers' revenues came from intercarrier compensation).

unlikely to "accelerate the migration to all IP networks," it will discourage rational investment as carriers will simply become reliant on an even more stable base of USF subsidies.

Moreover, any recovery mechanism should be structured to encourage carriers to rebalance rates by precluding carriers from receiving additional support unless and until they charge their end users retail rates that are in line with a reasonable nationwide benchmark. Even some rural carriers "acknowledge that it is appropriate for RLECs with below-average local rates to first look to their end users for a portion of the recovery of lost revenues." NECA Comments at 17; *see also* Kansas Corporation Commission Comments at 44 ("Before providing CAF or other support for access reductions, the Commission should impute the revenues that could be derived from increasing rates to the benchmark."). As the Commission observes, "high intrastate intercarrier rates have enabled local residential rates to remain artificially low in some areas, such as $8 or less." *NPRM* ¶ 54.[63] *See also* Section V-A *infra* (describing the substantial headroom many carriers have to recover more revenue from their end users without creating affordability concerns). By creating incentives for companies to rebalance rates, the Commission would both limit the size of the USF and ensure that any new funding does not result in disparate treatment of consumers. In addition, any new USF disbursements from the fund should take into account the overall declining nature of switched access minutes.[64]

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[63] There are numerous examples of local rates that are even lower. In Ohio, for example, a number of RLECs charge rates for residential basic local exchange service that range from $4.05 per month to $7.50 per month. *See* Local Exchange Tariffs of Conneaut Telephone Co.; Kalida Telephone Co. ($7.50 per month); Fort Jennings Telephone Co. ($7.50 per month); Glandorf Telephone Co. ($5.35 per month); Kalida Telephone Co. ($5.56 per month); Middle Point Home Telephone Co. ($4.05 per month); & Ridgeville Telephone Co. ($6.25 per month).

[64] Originating and terminating minutes of use have plummeted in the last decade, from a high of more than 566 billion in 2000 to a low of just over 315 billion in 2008. *See NPRM* ¶¶ 8, 503, n.719; *see also* FCC Industry Analysis and Technology Division, *Trends in Telephone Service*, http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-301823A1.pdf, at Chart 10-1 (September 2010) ("Sept. 2010 Trends in Telephone Service"). Between 2008 and 2009 alone,

However the Commission ultimately structures the recovery mechanism, the Commission should make clear that the transitional fund will sunset on a date certain (such as three years) so that companies will have a reasonable amount of time to restructure their operations.

C. Alternative Providers Should Have an Opportunity to Become the Universal Service Provider in Unserved Areas Through Competitive Bidding, and Service Obligations Should Extend Only to Auction Winners.

1. As new technologies introduce services that offer cost savings it makes sense to modify the universal service program so that consumers reap the benefits of these efficiencies. And by now there is no dispute that wireless providers offer viable alternatives to traditional voice and data services—and consumers increasingly value those services on par with (or more than) wireline services. Every year wireless substitution rates increase. The most recent wireless substitution survey conducted by the National Center for Health Statistics found that there are now twice as many wireless-only households than households with landline-only voice service.[65] The upward trend in wireless substitution will continue with both voice and data services. As CTIA observed, "over the twelve-month period from June 2009 to June 2010, the number of mobile wireless connections with download speeds of at least 768 kbps *increased by over 150%*, and accounted for *almost 85% of all new connections* in that speed range." CTIA Comments at 4. Indeed, wireless broadband services likely are the most cost-effective and technologically

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switched access lines decreased by 10 percent. *NPRM* ¶ 8. These downward trends are virtually guaranteed to continue. *See* Sept. 2010 Trends in Telephone Service at 10-3, Chart 10.1.

[65] *See* National Center for Health Statistics, *Wireless Substitution: State-level Estimates From the National Health Interview Survey January 2007–June 2010*,, http://www.cdc.gov/nchs/data/nhsr/nhsr039.pdf, at 1 (finding that as of the first half of 2010, over 26.6% of households were wireless-only, while only 12.9% of household had only landline service).

feasible way to deploy broadband in many high cost areas.[66] In addition, satellite broadband service can be extremely effective in reaching remote locations too expensive to serve with either fixed wireline or traditional wireless.[67] WildBlue/ViaSat recently demonstrated the impressive capabilities of its new satellite broadband and voice services at the Commission's second intercarrier compensation and universal service reform workshop a few weeks ago.[68] In short, Verizon agrees with the Rural Cellular Association that the "USF should support whichever competitors and whichever technology can best deliver on the promise of extending affordable and high-quality services to rural areas and low-income consumers." RCA Comments at 3.

2. A technology-neutral competitive bidding mechanism is the key to ensuring that scarce universal service dollars are targeted, efficient and "put to the best possible use." *NPRM*, *attached* Statement of Chairman Julius Genachowski at 3. Many commenters agree. *See, e.g.*, Time Warner Comments at 25-26; Comcast Comments at 16-19. Under such a system only the carrier receiving universal service funding (the "winner" of the auction)—and no other carrier—should have service or other traditional ETC and/or state "carrier of last resort" (COLR) obligations. It would be inappropriate to impose substantial regulatory obligations (whether rooted in state law or federal ETC requirements) on any carrier that does not receive such support. Imposing service obligations on any carrier not receiving universal service support

[66] *See* OBI Technical Paper No. 1, "The Broadband Availability Gap," http://download.broadband.gov/plan/the-broadband-availability-gap-obi-technical-paper-no-1.pdf, at 13, Exh. 1-J (2010).

[67] ViaSat intends to launch next generation broadband services in 2011 that will exceed the National Broadband Plan's proposed service requirements (4/1 Mpbs), while other satellite providers anticipate that "the satellite industry will be able to serve a significantly large proportion of unserved households." *See Ex Parte* Presentation of ViaSat, Inc. and WildBlue Communications, Inc. (Nov. 2, 2010); *Ex parte* presentation of DISH Network and EchoStar Satellite Services (Nov. 11, 2010), WC Docket Nos. 10-90, 05-337.

[68] *See* FCC, Advisory, Panelists Announced for April 27 Workshop on Modernizing Universal Service for Broadband (April 22, 2011).

would serve no legitimate policy purpose given that universal service goals are achieved by the funding recipient. Instead, it would artificially increase the carrier's costs and constrain its ability to compete effectively, to transition to an IP network, and to bid for other USF funding in different geographic areas. The Commission should affirmatively relieve those providers that no longer receive support from legacy ETC or other obligations. Any new or continuing regulatory obligations should flow only to recipients of new USF broadband support—which would not include all ETCs under any of the Commission's proposed long-term approaches to *Connect America Fund* support.

Verizon and others have outlined the benefits of competitive bidding many times. Market-based mechanisms offer advantages that encourage private investment and spur innovation. Competitive bidding allows the market to determine the amount of support necessary, rather than cost estimates that time has shown all too often miss the mark.[69] Competitive bidding offers incentives to carriers to provide service at the "minimum possible cost," which in turn encourages providers to make their own networks as efficient and cost-effective as possible. *Id.* ¶ 11. And competitive bidding provides a "fair and efficient means of eliminating" the subsidization of multiple providers in a given region. *Id*. These benefits are simply unavailable with cost and revenue modeling approaches, which the "record evidence" demonstrates have encouraged imprudent investment decisions designed to increase universal service support and have discouraged innovation and rational investment decisions. *NPRM* ¶¶ 171-72, 178-80, 189, 197. It is past time to try something new.

[69] *See High Cost Universal Service Support*; Federal-State Joint Board on Universal Service, Notice of Proposed Rulemaking, 23 FCC Rcd 1495, ¶ 11 (2008) ("*Reverse Auctions NPRM*").

Those that oppose competitive bidding largely offer tired, unpersuasive policy arguments. *See, e.g.*, NECA Comments at 76-79; State Members May 2 Comments at 79-85. Contrary to these arguments, there is no reason to believe that a competitive bidding approach to USF funding will result in a widespread "race to the bottom" and poor service quality or, worse yet, no service at all. NECA Comments at 76-79. In fact, the government uses competitive bidding to procure many of our nation's essential services where quality is at a premium, including healthcare, engineering and military services, and has done so successfully for decades. Critical education and rural healthcare services are purchased with universal service support based on competitive-bid contracts, and competitive bidding is the hallmark of the Commission's widely successful USF E-rate program. 47 C.F.R. § 54.504. Competitive bidding is simply the standard way that the government purchases goods and services, and there is no reason it cannot work in the communication industry as it does in so many others. Moreover, the high cost funding distribution system is entirely irrelevant to the enforceability of service quality standards. NECA Comments at 78. Service quality standards can and should remain the same regardless of how USF funding is distributed. If service quality deteriorates in a particular area to an unacceptable level, funding could be redistributed to a different service provider (through re-auction or otherwise), and the Commission could take other steps to enforce the service provisions of the contract that results from the competitive bidding process. Such enforcement is common in government procurement.

Nor is there is any merit to the argument that a competitive bidding process will hinder network investment. NECA Comments at 77-78; State Members May 2 Comments at 82-83. In reality the record evidence demonstrates that the *current distribution mechanism* already results in imprudent and irrational network investments that have led to increased costs for everyone with little benefits to consumers overall. *NPRM* ¶¶ 171-72, 178-80, 189, 197. A market-based distribution mechanism, which encourages providers to offer service in the most efficient manner—will encourage network investment.

Some commenters do not oppose a market-based USF distribution mechanism such as competitive bidding, but advocate for multiple auction winners or multiple auctions (one for fixed and one for wireless, for example) in each unserved area. *See, e.g.,* RCA Comments at 17-19. Those opposed to a single-winner auction generally argue that a single winner will undermine competition by favoring one type of provider over another. The Rural Cellular Association argues that a single-winner process will favor ILECs. *Id*. Others argue that single-winner auctions would favor wireless providers. *See, e.g.,* Indiana Utility Regulatory Commission Comments at 5-6. There is, however, no reason to believe that a technology-neutral competitive bidding process will generally favor one type of provider over another.

Moreover, nowhere in the Act did Congress require the Commission to subsidize multiple providers in areas that are prohibitively expensive for even a single provider to serve. 47 U.S.C. § 254(b). It is simply not "in the public interest to use federal [high cost] support to subsidize competition and build duplicative networks ."[70] Funding for multiple carriers in high cost areas is also inconsistent with the sufficiency principle in Section 254, which requires the Commission to award funding that is "adequate, but no greater than necessary, to achieve the goals of the universal service program."[71]

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[70] *Federal-State Joint Board on Universal Service*, Recommended Decision, 22 FCC Rcd 20477, ¶ 35 (2007) ("*Recommended Decision*"); *see also* Nebraska PSC Comments at 18 (concluding that the public interest is not served by subsidizing "multiple networks within a given support area, due to the cost involved and the related impact on customers within the state").

[71] *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, Joint Petition of the Wyoming Public Service Commission and the Wyoming Office of*

3. The familiar statutory arguments against use of competitive bidding, recycled by some commenters in this proceeding, are also meritless. U.S. Cellular suggests that the Commission lacks all authority to use competitive bidding to distribute high cost support. U.S. Cellular Comments at 20-27. The language of the Act and its legislative history make clear that these arguments are wrong. Section 254(e) provides that "only an eligible telecommunications carrier designated under section 214(e) shall be eligible to receive specific Federal universal service support." 47 U.S.C. § 254(e). An ETC designated pursuant to Section 214(e), however, is indeed merely "eligible" for—*but not entitled to*—support. Words used in a statute are presumed to have their normal meaning.[72] The statutory term "eligible" is understood to mean "fitted or qualified to be chosen or used."[73] The term "eligible" does not connote a particular entitlement. When Congress intended to create an entitlement in the 1996 Act, it did so explicitly by using the term "entitled" rather than the term "eligible." *Compare* 47 U.S.C. §214(e)(1) (carriers "shall be eligible to" receive universal service support in accordance with Section 254) *with id.* § 254(h)(1)(A) (carriers offering service to health care providers "shall be entitled to" the difference between rates to health care providers and other customers in comparable rural areas).

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Consumer Advocate for Supplemental Federal Universal Service Funds for Customers of Wyoming's Non- Rural Incumbent Local Exchange Carrier, Order on Remand and Memorandum Opinion and Order, 25 FCC Rcd 4072, ¶ 3 (2010) ("*Qwest II Remand Order*").

[72] *Review of the Commission's Rules and Policies Affecting the Conversion to Digital Television*, Third Memorandum Opinion and Order on Reconsideration, 17 FCC Rcd 18571, ¶ 6 (2002) (citing *Landreth Timber Co. v. Landreth*, 471 U.S. 681, 685 (1985)) ("Statutory construction must begin with the language employed by the statute and the assumption that the ordinary meaning of the language accurately expresses the legislative purpose.").

[73] *CTIA v. FCC*, 466 F.3d 105, 117 (D.C. Cir. Sept. 26, 2006) (quoting *Webster's Third New International Dictionary of the English Language Unabridged* 736 (1981)).

Additional analysis of Section 254(e) underscores the point. This provision goes on to instruct that "[a] *carrier that receives such support* shall use that support. . ." and requires that "[*a*]*ny* such support should be explicit and sufficient." *Id.* (emphasis added). Use of the word "that" is restrictive, indicating that not all carriers designated as ETCs necessarily will receive support.[74] Moreover, use of the word "any" indicates that subsidies will not be distributed in all instances.

The legislative history of the predecessor provision to Section 214(e) also demonstrates Congress's intent that ETC designation is not a guarantee of funding. The relevant Senate Report explains that ETC designation would "mak[e] that carrier eligible for support payments to preserve and advance universal service, *if* any such payments are established" by the Commission. S. Comm. on Commerce, Science, and Transportation, *Report on Telecommunications Competition and Deregulation Act of 1995*, at 42 (1995) ("*Senate Report*") (emphasis added); *see also id.* at 39 (explaining that ETCs "shall be eligible to receive support payments, *if any*, established by the FCC or a State to preserve and advance universal service.") (emphasis added). Thus, whether a provider receives funding turns not on its ETC designation, but instead on whether it satisfies the criteria of whatever funding mechanism the Commission establishes pursuant to Section 254(e).

Consistent with the statutory language and legislative history, the Commission has never indicated that ETC designation constitutes an entitlement to support. The Commission has, however, recognized that it can indeed create a competitive bidding mechanism that complies

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[74] *See, e.g.*, William Strunk, Jr. and E. B. White, THE ELEMENTS OF STYLE 59 (4th ed. 2000).

with Section 214.[75] The Commission also determined as far back as 1997 that competitive bidding satisfies Section 254—and that market-based USF distribution mechanisms such as competitive bidding have many advantages. *See*, *e.g.*, *Federal State Joint Board on Universal Service*, Report and Order, 12 FCC Rcd 8776, 8951 ¶ 325 (1997) ("[W]e agree with the Joint Board that competitive bidding is consistent with section 254, and comports with the intent of the 1996 Act to rely on market forces and to minimize regulation. . . .").

In addition, as discussed above, the Act does not require the Commission to fund any minimum number of ETCs in a service area. U.S. Cellular Comments at 20-27. The Commission is required to ensure that universal service is preserved and advanced in accordance with the principles enumerated in Section 254(b), but that does not mean that multiple carriers, if any, in a service area must receive funding. In fact, Congress fully anticipated in the Act that the need for universal service funding for all carriers, or all carriers in certain areas, could be eliminated entirely through competition. As the Senate Commerce Committee explained:

> In some areas of the country, particularly in areas that are already subject to competition in the provision of services included in the definition of universal service, the Committee expects that support payments would not be needed in order to provide universal service at just, reasonable, and affordable rates. ***The Committee intends this requirement to provide the flexibility for the FCC to reduce or eliminate support payments to areas where they are no longer needed*….**

Senate Report at 39 (1995) (emphasis added). Finally, U.S. Cellular suggests that the Commission's proposal to define unserved areas and distribute funding for broadband by census blocks or census tracts violates Section 214(e) because census groupings are not coextensive with traditional LEC "service areas." U.S. Cellular Comments at 27. This, too, is off the mark.

[75] *See Federal State Joint Board on Universal Service*, Further Notice of Proposed Rulemaking, 14 FCC Rcd 21177, ¶ 95 (1999) (tentatively concluding to adopt a competitive bidding mechanism in unserved areas).

The Act's definition of a "service area" in Section 214 applies only to the geographic unit used for ETC designation purposes. 47 U.S.C. § 214(e)(5). This definition does not constrain—indeed says nothing about—how the Commission may choose to define an unserved area for purposes of disbursing universal service funding. Section 254(e) does not require the Commission to use any particular distribution methodology and makes no reference to any particular "service area." 47 U.S.C. § 254(e). At bottom, what US Cellular and other parties really seek is "protection from competition" and a "predictable market outcome"—which is "the very antithesis of the Act." *Alenco Commc'ns v. FCC*, 201 F.3d 608, 622 (5th Cir. 2000); *see also Rural Cellular Ass'n, et al. v. FCC*, 588 F.3d 1095, 1102 (D.C. Cir. 2009); RCA Comments at 17-18.

4. Likewise, the Commission should explicitly recognize in this proceeding that high cost USF support is not a carrier entitlement and should be reduced or eliminated when unsubsidized wireless broadband and other unsubsidized next-generation services become available in high cost areas. *Senate Report* at 39 (1995). For too long, some providers have indeed viewed universal service subsidies as a carrier entitlement, one that must be distributed evenly and equitably to those providers that have historically received subsidies. *See, e.g.,* NECA Comments at 81-82. This is fundamentally wrong. The purpose of the universal service program is to ensure that consumers in all areas of the country have access to affordable, and reasonably comparable, services. 47 U.S.C. § 254(b). Wherever possible the market should direct and control the level of necessary subsidies. To that end, universal service support should be reduced or eliminated where mobile broadband and other next-generation technologies make subsidized service unnecessary.

Even without USF subsidies in many cases, the marketplace has expanded broadband service to the vast majority of all Americans, and it is clear that further expansion of competitive broadband service is about to explode. Verizon alone has announced plans to reach at least 147 domestic cities with LTE wireless service by the end of 2011 and will have LTE coverage everywhere that Verizon has 3G coverage by the end of 2013.[76] One month ago today, Ericsson and NetAmerica Alliance announced a technology agreement that will bring 4G/LTE to "people and businesses in smaller markets and rural areas across the United States."[77] Clearwire reports that as of February 2011, its 4G network reached over 119 million Americans.[78] And AT&T, in announcing its acquisition of T-Mobile, has pledged that the combined company would ensure that 97 percent of Americans have access to LTE mobile broadband.[79]

LTE/4G mobile broadband speeds typically exceed the National Broadband Plan's 4/1 minimum thresholds for broadband. Verizon's LTE service has download speeds of 5-12 Mbps and upload speeds of 2-5 Mbps. In addition (as discussed above), satellite broadband service can be very effective at reaching remote locations too expensive to serve with either fixed wireline or traditional wireless services, and satellite deployment is expanding. New satellite broadband speeds are also expected to exceed the National Broadband Plan thresholds.

Ongoing deployment of intermodal broadband services will significantly—and rapidly—change the broadband communications landscape, both from a quality and coverage perspective. It is entirely possible that even without any additional universal service funds, broadband

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[76] http://reviews.cnet.com/8301-12261_7-20046102-10356022.html; http://network4g.verizonwireless.com/#/coverage.

[77] *See* "Bringing mobile broadband services to rural United States" (March 23, 2011), *available at* http://www.cn-c114.net/2503/a590149.html (last visited May 3, 2011).

[78] *See* http://snapvoip.blogspot.com/2011/02/clearwire-reports-solid-q4-and-total.html.

[79] Press Release, "AT&T To Acquire T-Mobile USA From Deutsche Telekom" (March 20, 2011), *available at* http://mobilizeeverything.com/home.php (last visited April 16, 2011).

availability will be virtually ubiquitous in five years or less. NBP at 137. The Commission and providers should prepare for the day when universal service funding is no longer necessary or appropriate because private investment has found a sustainable business case for the expansion of broadband service nationwide. Along the way the Commission should be prepared to reassess, and to reduce, USF support in certain areas as appropriate. The Act requires such reductions, and consumers who pay for the fund are entitled to the benefit of a smaller program. *Senate Report* at 39 (1995); 47 U.S.C. § 254(b)(5) (providing for "sufficient" universal service support, which the courts have interpreted as funding amounts that are no higher than necessary); *see also Rural Cellular Ass'n*, 588 F.3d at 1102.

D. Adding a Broadband Component to Rate-of-Return Regulation Would Make this Unsustainable, Backwards-Looking Regulatory Scheme Even Worse.

Some commenters continue to insist on preserving the long-outdated rate-of-return regulatory scheme—and some even suggest that as a part of universal service reform the Commission should augment guaranteed returns with new components for regulated broadband revenue and middle mile transport costs. *See, e.g.*, NECA Comments at 27-36; State Members May 2 Comments at 33-37; Utah Comments at 1-2. This approach is exactly backwards. Consistent with the recommendation in the National Broadband Plan, the Commission should *eliminate* rate-of-return regulation in favor of incentive regulation. NBP at 147. And under no circumstance should the Commission exacerbate the problems with guaranteed annual returns for a favored class of carriers by adding additional revenues and costs to the regulated base.

The Commission has already made clear that "cost-plus" regulation does not create appropriate incentives for broadband deployment. "Rate of return regulation was not designed to promote efficiency or innovation; indeed, when the FCC adopted price-cap regulation in 1990, it recognized that 'rate of return does not provide sufficient incentives for broad innovations in the way firms do business.'" *Id.* In a competitive environment, it does not make sense to lock in "a stable 11.25 percent return" for a large class of more than 1,000 rate-of-return carriers "regardless of their marketplace performance." *NPRM* ¶ 165. Such a system rewards inefficiency, insulates carriers from competition, and gives these providers a disincentive to innovate.

The suggested model for moving rate-of-return ILECs to incentive regulation—converting them to price cap regulation and shifting to a per-line USF support approach—has worked previously without harming universal service. *Connect America Fund NPRM* ¶ 55 n.123-24. The Commission approved a number of price cap conversion petitions over the past two years, in each instance finding that granting the request was in the public interest. *Id.* ¶ 55 n.123. Allowing carriers to convert from rate-of-return regulation to price cap regulation has benefitted consumers through fewer demands on the USF, lower costs of regulatory compliance, increased operational efficiencies, and enhanced competition.

The Commission should reject the calls in this proceeding to preserve rate-of-return regulation and should begin moving these carriers to incentive-based regulatory schemes as soon as possible. NBP at147 ("Rate-of-return regulation was implemented in the 1960s, when there was a single provider of voice services in a given geographic area that had a legal obligation to serve all customers in the area and when the network only provided voice service."). While the USF subsidies that rate-of-return carriers receive are lucrative and attractive to those carriers, the rate-of-return regulatory model is simply no longer sustainable. And even some parties that propose to preserve rate-of-return regulation recognize that the scheme is out of touch with current marketplace realities. *See, e.g.*, State Members May 2 Comments at 36-37.

In the long-term, rate-of-return is not consistent with meaningful intercarrier compensation and USF reforms that should be designed to produce a rational, market-based system.

V. STATE REGULATION THAT PERPETUATES LEGACY INFRASTRUCTURE IS INCONSISTENT WITH FEDERAL LAW AND POLICY.

Some commenters urge the Commission to defer broadly to and rely on the states to undertake the essential intercarrier compensation and universal service reforms presented in the *NPRM*. *See, e.g.*, NECA Comments at 12-20; State Members May 2 Comments at 154-55; Frontier Comments at 6-8. As a practical matter, for reasons discussed below, that approach will not work. The Commission should exercise its authority to preempt (*see* above) state actions that "stand[] as an obstacle to the accomplishment and execution of the full purposes and objectives" of comprehensive intercarrier compensation and universal service reform. *Concepcion*, 2011 U.S. LEXIS 3367, *33. State actions that run counter to Commission policies to drive down all intercarrier compensation rates to more sustainable levels and to narrowly target efficient universal service subsidies are inconsistent with the "fundamental attributes" of critical, comprehensive reform of these mechanisms. *Id*. at *18.

A. Proposals to Place National Intercarrier Compensation Reform under State Direction Are Fundamentally Misguided and Will Not Solve the Problems.

It is important that this Commission not make decisions in this proceeding based on false impressions of what state regulators have done, are doing, or are capable of doing with respect to intercarrier compensation reform. A number of parties tout the ability of states to carry out the national reforms needed to replace the broken system with a rational one. *See, e.g.*, NECA Comments at 12-20; State Members May 2 Comments at 154-55. The reality, based on extensive experience, is that tasking *state* regulators with responsibility for comprehensive *national* reform would result in inaction, confusion, and disparities in regulatory outcomes. Those outcomes would undercut federal reform objectives and will harm consumers.

A key and necessary outcome of reform is to eliminate the disparity in rates that exist between jurisdictions and between different types of traffic. The current disparities are the framework that produces traffic pumping and arbitrage and are otherwise the basis for debate and disputes. These situations will only be neutralized when uniform rates are adopted for all traffic and all jurisdictions, which cannot be accomplished simultaneously (or uniformly) by the states. Even if there were reason to believe that 50-plus regulatory bodies would be capable of running different proceedings that all reach the same conclusion (there is not), what is needed is a single path to reform—not the continuing prospect of endless proceedings at all levels of government. And as a practical matter allowing states to be "laboratories" for intercarrier compensation reform would likely *exacerbate* existing problems because different states would inevitably undertake reform at different speeds, or undertake no reform at all—thus creating new and constantly shifting rate disparities. Varying state rates and rules could also lead providers to implement state-specific or even exchange-specific prices, which would create confusion among consumers accustomed to any-distance products.

As the Commission observed, "the majority of states have not comprehensively reformed intrastate access charges, and continue to maintain intrastate access charges that far exceed interstate charges, with some intrastate access charges in excess of 13 cents per minute." *NPRM* ¶ 54. That is because, despite often having the best intentions, indecision often prevails when regulatory bodies at all levels are confronted with the difficult issues associated with switched access intercarrier compensation reform. While some states (a minority) have required their largest carriers to mirror interstate rates, few have required "midsized" or smaller carriers similarly to reduce their intrastate switched access rates.[80] Indeed, very few states with substantial RLEC operations have undertaken meaningful reform of RLEC switched access rates. Inconsistent state activity regarding intrastate switched access reform has created massive economic distortions and inefficiencies, both by perpetuating high intrastate rates for some carriers and by leaving in place (or worsening) substantial disparities between the rates of different carriers.

Extensive experience demonstrates that the numerous potential vehicles through which intrastate access reform might take place—including legislation, rulemaking, complaints, and generic investigations—have frequently proven unviable. A few case studies illustrate that even where state regulators or legislators acknowledge the importance of reforming switched access rates, results are often elusive.

1. More than *thirteen* years ago the Minnesota Public Utilities Commission ("Minnesota commission") first opened an investigation to examine the intrastate switched access charges of all Minnesota carriers.[81] Three years later, the Minnesota Department of Commerce urged the commission to move forward with intrastate access reform, observing that in the time since the federal Telecommunications Act was passed, "access charge reform is arguably where the least progress has been made."[82] But that investigation, as well as other

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[80] *See, e.g.*, Ex Parte Letter from Brian Benison, AT&T, to Marlene Dortch, FCC, *Developing a Unified Intercarrier Compensation Regime*; *High-Cost Universal Service Support*; *A National Broadband Plan for Our Future*, CC Docket No. 01-92, WC Docket No. 05-337; GN Docket No. 09-51 (Oct. 25, 2010).

[81] *See* Notice Soliciting Comments on Access Charge Reform, *Commission Investigation of Intrastate Access Charge Reform*, Docket No. P-999/CI-98-674 (Minn. Pub. Utils. Comm'n June 4, 1998).

[82] Comments of Minnesota Department of Commerce, *Commission Investigation of Intrastate Access Charge Reform*, Docket. No. P999/CI-98-674, at 9 (Minn. Pub. Utils. Comm'n filed April 20, 2001).

efforts to reform Minnesota's switched access regime, closed without any commission action.[83] Access reform technically remains on the commission's agenda in the form of a proposed rulemaking initiated in 2007; however, after two rounds of comments, the docket has been dormant for more than three years.[84]

Notably, there is no ambiguity in Minnesota about the benefits of switched access reform for consumers and the state's economy. A comprehensive 91-page staff white paper written in 2003 set forth the numerous public policy benefits of reform – and it dispelled each of the fallacies asserted by opponents of reform.[85] The Minnesota staff estimated the average subsidy implicit in RLEC intrastate switched access rates to be more than *7 cents per minute* for terminating traffic (and over six cents for originating traffic) – while RLEC local rates were held to an average of only *$12.07 per month*.[86] The analysis confirmed substantial headroom for RLECs to rebalance without implicating any universal service concerns: if RLECs' high intrastate rates were reduced to interstate levels, they could fully recover all lost access revenue while still charging an average local residential rate of $18.31 per month.[87] Yet despite the

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[83] For a summary of the various access reform dockets that the Minnesota commission has opened and closed in the past ten years, *see* Comments of the Office of the Attorney General, *Request for Comments of the Minnesota Public Utilities Commission Relating to a Rule to Modify Telephone Access Charges*, Docket No. P-999/R-06-51, at 1-2 (Minn. Pub. Utils. Comm'n filed Mar. 15, 2007).

[84] *See generally Request for Comments of the Minnesota Public Utilities Commission Relating to a Rule to Modify Telephone Access Charges*, Docket No. P-999/R-06-51 (Minn. Pub. Util. Comm'n).

[85] *See* Access Reform and Universal Service in Minnesota: Staff White Paper, *Commission Investigation of Intrastate Access Charge Reform*, PUC Docket No. P-999/CI-98-674 (Minn. Pub. Utils. Comm'n Nov. 14, 2003).

[86] *Id.* at 55, 58.

[87] *Id.* at 58.

empirical evidence repudiating the scare tactics employed by opponents of reform, the Minnesota commission has been unable to make progress on access reform.

2. Similarly, the Arizona Corporation Commission ("Arizona commission") is now in its eleventh year considering access reform issues, and most carriers' switched access rates have not been adjusted in decades.[88] Most RLECs charge, on average, intrastate access charges that are more than ten cents per minute.[89] The result of the legacy cross-subsidy policy is artificial local rate suppression, with the statewide average rate for basic residential service below $13.00 per month.[90]

And if the Arizona commission does decide to move forward with access reform in the future, there is an additional wrinkle: for many years parties have questioned the commission's statutory and constitutional authority to order *any* changes to intrastate access charges without first conducting particularized "fair value" proceedings into each ILEC's costs.[91] That threshold legal question remains unresolved.

3. Despite extensive activity before the Public Service Commission of Wisconsin ("Wisconsin commission"), most carriers' access charges have generally been frozen for the

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[88] *See* Residential Utility Consumer Office Closing Brief, *Investigation of the Cost of Telecommunications Access*, Docket No. T-00000D-00-0672, at 1-4 (Ariz. Corp. Comm'n filed July 9, 2010) ("RUCO Brief").

[89] *See* Direct Testimony of Douglas Duncan Meredith on Behalf of the Arizona Local Exchange Carrier Association, *Investigation of the Cost of Telecommunications Access*, Docket No. T-00000D-00-0672, at 6 (the average difference between members' intrastate and interstate rates is more than nine cents) & 7 (the average interstate rate is $0.0166 per minute) (Ariz. Corp. Comm'n filed Dec. 1, 2009).

[90] *See* Reply Testimony of Douglas Duncan Meredith on Behalf of the Arizona Local Exchange Carrier Association, *Investigation of the Cost of Telecommunications Access*, Docket No. T-00000D-00-0672, at 7 (Ariz. Corp. Comm'n filed Feb. 5, 2010).

[91] *See* RUCO Brief at 7.

better part of two decades.[92] For many years, Verizon and others have asked the commission to reevaluate the intrastate switched access rates it established in 1993, but the decisions have been mostly non-substantive.[93] For example, more than a year ago, in response to evidence in various proceedings, the commission ordered relatively minor switched access "reductions" that would occur over five years, but would not begin until *2012*, with the final (and most significant) reduction avoidable if certain broadband deployment thresholds are achieved.[94] And after receiving extensive comments about the need for comprehensive access charge reform in 2008 in the course of a generic investigation, the commission shifted the issue of switched access rates to another proceeding.[95] That proceeding, which was initiated in October 2009 and has involved

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[92] *See* Findings of Fact, Conclusions of Law, and Final Order, *Investigation of Intrastate Access Costs and Intrastate Access Charge,* Docket No. 05-TR-103 (Wis. Pub. Serv. Comm'n Mar. 25, 1993). The Wisconsin commission started off strongly, finding that consumers and the state's economy receive numerous benefits from intrastate access rates that are reasonable and uniformly priced, and established a series of benchmarks based on the switched access rates of access rates of Wisconsin Bell (now AT&T) and GTE (now Frontier). *Id.* at 12-17. However, although AT&T and Frontier subsequently reduced their intrastate rates to interstate levels, the mirroring requirement has not been updated since 1993. Some minor adjustments have occurred in the context of carrier-specific alternative regulation plans.

[93] *See, e.g.*, Verizon's Comments, *Investigation into the Level of Regulation for Telecommunications Providers*, Docket No. 05-TI-1777, at 39 (Wis. Pub. Serv. Comm'n filed Mar. 25, 2008).

[94] *See, e.g.*, October 19, 2009 Orders in PSCW Docket Nos. 2815-TI-105; 2930-TI-104 and 4260-TI-103; and the April 2, 2010 orders in PSCW Docket Nos. 1910-TI-103; 2050-TI-102; 3070-TI-102; 4590-TI-102; 5530-TI-102; and 6040-TI-102. In Docket No. 2815-TI-104, it was asserted that Verizon inconsistently presses for access reductions in some states while defending its own intrastate access rates. In fact, Verizon advocates the same approach to intrastate switched access reform throughout the country: it urges state commissions to remedy competitive distortions by moving towards a single, reasonable rate for all providers. *See* Verizon's Response to CenturyTel's "Summary of Position", *Application of CenturyTel of the Midwest-Kendall, Inc. for Approval of an Alternative Regulation Plan*, Docket No. 28-TI-104, at 4-7 (Wis. Pub. Util. Comm'n filed Apr. 18, 2008). Verizon also consistently emphasizes the importance of authorizing (and requiring) carriers to recover more revenue from their end users if necessary to recover their network costs.

[95] *See generally Investigation into the Level of Regulation of Telecommunications Providers*, Docket No. Docket No. 5-TI-1777. The investigation was closed without any action.

extensive comments and workshops, was recently suspended for six months in light of the possibility of FCC action.[96]

4. Even where parties avail themselves of statutory rights to invoke complaint processes to address unjust and unreasonable switched access rates, regulators have been inconsistent in their willingness to adjudicate such complaints. While not an efficient way to achieve comprehensive reform, such targeted proceedings have in some states helped at least address the most pressing switched access problems. But many state commissions have rebuffed efforts by access rate payers to invoke their right to avoid paying unjust and unreasonable rates.

For example, Verizon filed a complaint in 2007 before the Kentucky commission requesting adjudication of the reasonableness of Windstream's intrastate switched access rates.[97] For years, the case sat unadjudicated on the commission's docket. The commission ultimately closed the case without addressing the reasonableness of Windstream's rates, folding that individual complaint proceeding into a broader, industry-wide investigation of intrastate switched access rates. That broader proceeding is still in the discovery stage and no hearing date has been set. As a result, no action has been taken to date to adjudicate Verizon's complaint,

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(Continued . . .)
See Order to Close the Investigation, *Investigation into the Level of Regulation of Telecommunications Providers*, Docket No. 5-TI-1777 (Wis. Pub. Serv. Comm'n Feb. 4, 2011).

[96] *See* Order Suspending Docket, *Investigation on the Commission's Own Motion into the Intrastate Access Charges Assessed by Incumbent and Competitive Local Exchange Carriers in Wisconsin*, Docket No. 5-TR-105 (Wis. Pub. Serv. Comm'n Feb. 11, 2011). The commission staff has proposed that payers of access be entitled to pay reduced access rates only if they make "voluntary" contributions to a broadband fund. *See* Staff Strawman Proposal, http://psc.wi.gov/apps35/ERF_view/viewdoc.aspx?docid=139743 (Wis. Pub. Serv. Comm'n Oct. 10, 2010). Under the proposal, firms that decline to contribute "voluntarily" to the broadband fund would have no recourse to ask the commission to address the level of the switched access charges they pay. *Id.* at 5.

[97] *See* Petition of Verizon to Reduce Windstream's Switched Access Charges, *MCImetro Commc'ns Servs., Inc., et al. v. Windstream Kentucky West, Inc., et al.*, Case No. 2007-00503 (Ky. Pub. Serv. Comm'n filed Dec. 5, 2007).

despite the fact that the rates complained of are at least ***several hundred percent higher*** than what the state's largest ILEC is authorized to charge.[98]

Similarly, the Minnesota commission has taken no action to adjudicate complaints Verizon filed more than three years ago alleging that the switched access rates of Embarq and CenturyLink are unjust and unreasonable.[99] With respect to Embarq, the commission acknowledged in March 2008 that there were reasonable grounds to investigate Verizon's complaint, served the complaint on Embarq, and established a comment period.[100] That comment period closed on April 21, 2008, but the docket has since been dormant.[101]

Sprint has experienced similar inaction in North Carolina, where it filed a petition in November 2009 asking the commission to investigate ILEC intrastate switched access charges, which it stated are between six and twelve times higher than interstate rates.[102] Rather than initiate an investigation, the North Carolina commission required parties on all sides of the issue to convene a working group to "examine the matter comprehensively and make

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[98] *Id.* ¶ 9.

[99] *See Verizon's Verified Complaint to Reduce the Intrastate Switched Access Charges of Embarq Minnesota*, Docket No. P-3012, et al./C-07-1198 (Minn. Pub. Utils. Comm'n filed Sept. 12, 2007); *Verizon's Verified Complaint to Reduce the Intrastate Switched Access Charges of CenturyTel of Minnesota, Inc.,* Docket No. 08-983 (Minn. Pub.Utils.Comm'n filed Aug. 19, 2008).

[100] *See* Order Serving Complaint, Requiring Answer, and Authorizing Comments, *Verizon's Verified Complaint to Reduce the Intrastate Switched Access Charges of Embarq of Minnesota, Inc*. Docket No. P-3012, et al./C-07-1198 (Minn. Pub. Utils. Comm'n. Mar. 10, 2008).

[101] With respect to the complaint against CenturyTel, the commission has declined to formally serve the complaint on CenturyLink, which is the first (purely procedural) step needed to begin adjudication of a complaint proceeding. *See* Minn. P.U.C. Docket No. 08-983.

[102] *See* Sprint's Petition to Reduce Intrastate Switched Access Rates of Incumbent Local Exchange Carriers, *Sprint Commc'ns Co., L.P.'s Petition to Reduce the Intrastate Switched Access Rates of Rural Incumbent Local Exchange Carriers Operating in North Carolina*, Docket No. P-100, Sub 167, at 4-5 (N.C. Utils. Comm'n filed Nov. 23, 2009).

recommendations to the Commission as to how it should proceed."[103] After a series of face-to-face meetings and conference calls, the working group filed a final report some nine months later.[104] As Sprint states in its motion requesting that the commission establish a procedural schedule, sixteen months after the docket was initiated "the undeniable fact is that…we are no closer to determination of the appropriate level of ILEC intrastate access charges in North Carolina than when Sprint filed its Petition."[105]

5. Nor have rulemakings proven to be viable reform vehicles. The South Dakota commission, for example, recently issued proposed rules after a six-year proceeding regarding intrastate switched access rates. However, the commission made no determination regarding ILEC switched access charges, which are among the highest in the country, and instead adopted a rule capping CLEC rates at a remarkably high ***six cents per minute***.[106]

In 1998, the Washington commission took a dramatic step towards intrastate access reform by promulgating a rule requiring all carriers to charge cost-based terminating switched access rates.[107] Pending evaluation of universal service issues, however, the commission

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[103] *See* Order Establishing Access Charges Working Group, *Sprint Commc'ns Co., L.P.'s Petition to Reduce the Intrastate Switched Access Rates of Rural Incumbent Local Exchange Carriers Operating in North Carolina,* Docket No. P-100, Sub 167 (N.C. Utils. Comm'n April 14, 2010).

[104] *See* Sprint's Motion for Procedural Schedule, *Sprint Commc'ns Co., L.P.'s Petition to Reduce the Intrastate Switched Access Rates of Rural Incumbent Local Exchange Carriers Operating in North Carolina,* Docket No. P-100, Sub 167 (N.C. Utils. Comm'n filed Mar. 25, 2011) (detailing procedural history).

[105] *Id.* ¶ 5.

[106] *See* Midcontinent's Comments, *Revisions and/or Additions to the Commission's Switched Access Rules Codified in ARSD 20:10:27 Through 20:10:29*, Docket No. RM5-002 (S.D. Pub. Utils. Comm'n filed Jan. 28, 2011) (describing the history of the proceeding and nature of proposed rules).

[107] *See* Order Adopting Rules Permanently, *Adopting WAC 480-120-540*, Docket No. UT-970325 (Wash. Pub. Util. & Transp. Comm'n Sept. 23, 1998).

authorized firms to recover 100 percent of their lost revenue through "interim universal service rates."[108] For most carriers, those "interim" terminating rates—authorized more than twelve years ago—remain in place today.[109] One result of continued high access rates in Washington is the continued artificial suppression of local retail rates, which in dozens of rural exchanges are $10.15 or less per month.[110]

6. When legislators step in, the results are similarly mixed – and often result in statutes that place commissions in straightjackets. Some state legislatures have pursued switched access reform responsibly, whereas others have failed to act or have even created obstacles to reform. For example, in Missouri, where the commission had been unable to reform ILEC switched access rates for more than a decade,[111] the legislature recently passed an access reform bill. But given the very high levels of intrastate switched access charges in Missouri, the relief was relatively insignificant: it requires just the three largest ILECs to reduce their intrastate switched access rates by only 18 percent of the (large) difference between intrastate and interstate rates—and at the same time locks in those high rates by limiting the authority of the commission to undertake more substantial reform.[112]

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[108] *Id.* at 25.

[109] *See* Report Reviewing State Telecommunications Policies of Universal Service, Docket No. UT-100562, at 11-12 (Wash. Util. & Transp. Comm'n Nov. 29, 2010).

[110] *See* Testimony of Timothy W. Zawislak, *Verizon Select Servs. Inc. v. United Tel. Co. of the Northwest*, Docket No. UT-081393, Exhibit TWZ-3 (Wash. Util. & Transp. Comm'n filed June 5, 2009).

[111] In 2000, the Missouri commission opened a proceeding to address both CLEC access issues as well as "all other issues relating to access service." It closed that proceeding without addressing ILEC issues, which it never subsequently addressed. *See* Report and Order, *Investigation of the Actual Costs Incurred in Providing Exchange Access Service and the Access Rates to be Charged by Competitive Local Exchange Telecommunications Companies in the State of Missouri*, Docket No. TR-2001-65, at 17 (Mo. Pub. Serv. Comm'n Aug. 26, 2003).

[112] Mo. Rev. Stat. § 392.605.

And in the wake of the Wisconsin commission's nearly two-decade long history of inaction, the Wisconsin legislature stepped in this year and passed access "reform" legislation.[113] However, the access reform (and other) portions of the bill are so watered down and distorted such that, when the governor signs it into law, it will literally do more harm than good. For example, it not only *exempts* all "small" ILECs (defined to be under 150,000 lines) and "small" CLECs (defined to be under 10,000 lines) from any access reform, it additionally insulates their access rates from commission review for the next four years and three years, respectively.[114] It also *requires* (unless otherwise provided by federal law) the commission to apply the legacy switched access regime—including the high access rates that are insulated from commission review—to interconnected VoIP traffic.[115]

Not only is such state legislation bad public policy, but it illustrates the impossibility that this Commission could work in coordination with the states to achieve comprehensive national reform. By setting in stone their states' access charge regimes and by limiting their commissions' authority to modify those regimes, state legislatures can make it impossible even for willing commissions to engage in meaningful access reform—let alone to work cooperatively with this Commission to that end. Even if all fifty state commissions were capable of partnering with this Commission to implement comprehensive reform (and history shows many are not), the

[113] *See* Re regulation of telecommunications utilities and alternative telecommunications utilities; telecommunications provider of last−resort obligations; telecommunications intrastate switched access rates; interconnected voice over Internet protocol service; and use of transmission equipment and property by video service providers, AB 14/SB 13, https://docs.legis.wisconsin.gov/2011/related/enrolled/jr1_sb13.pdf (2011).

[114] *Id.*, § 196.212(4).

[115] *Id.*, § 196.206(3). Missouri statute states that interconnected VoIP service is "subject to appropriate exchange access charges" without specifying what those "appropriate" charges are. *See* Mo. Rev. Stat. § 392.550(2). The validity of the statute is currently being challenged in federal court.

existence of fifty-plus state legislatures creates additional uncertainty about the prospects of a productive partnership.

Further, when states attempt access reform, they are typically met with pressure to simply replace the lost access revenues with dollar-for-dollar universal service state funding. However, merely shifting all implicit subsidies to explicit subsidy funds, and shifting the funding obligation to other customers, is not true reform and does not provide tangible benefit to consumers. To the contrary, as discussed in Section C below, state efforts to create dollar-for-dollar recovery mechanisms conflict with the federal USF policies.

B. State Service Obligations Cannot Be Permitted to Hold Back the Transition to Next-Generation Technologies.

Some parties argue that the Commission should refrain from substantially modifying the broken intercarrier compensation system because some ILECs may rely on subsidies implicit in access rates to fulfill state-imposed service obligations, including whatever remains of state COLR obligations. *See, e.g.*, FairPoint Comments at 7; NASUCA Comments at 103-04. Some cite COLR obligations as a reason why ILECs purportedly need subsidies in the form of preferential status ("right of first refusal") for new broadband-based universal service funding. *See, e.g.*, FairPoint Comments at 20-22; Windstream Comments at 38-39; NECA Comments at iii. Those arguments are backwards. Instead of permitting incumbents to hide behind state regulatory burdens in order to perpetuate the status quo, the right approach is to relieve ILECs of any asymmetrical regulation. In the technology-neutral, level playing field contemplated by the NPRM, the *only* legitimate basis to impose a service obligation on one company that does not apply to its competitors is where the company accepts the obligation in return for universal service disbursements.

There can be no debate that legacy state regulation imposes highly burdensome asymmetrical obligations on incumbent carriers. Appendix C to the NECA Comments, for example, lists over 50 different ILEC-centric state regulatory obligations. Such obligations (such as requirements that incumbents provide "Line quality capable of facsimile transmission," "Dual-tone multi-frequency touchtone and rotary pulse dialing operability," and "Telecommunications relay service to facilitate communications between teletypewriter users and non-teletypewriter users") (*id.*) are relics of the bygone era when the copper plant was a monopoly asset. And those outdated requirements are just the tip of the iceberg in terms of regulation that impedes ILECs from restructuring their operations so that they can participate in the broadband-focused, technology-neutral landscape envisioned by the National Broadband Plan and *NPRM*. State-imposed ILEC-specific regulation can be extensive, including how ILECs must interact with customers, how they must market their products, how they must collect and report financial and operational data, and how they must configure their computer systems.

As unregulated and lightly regulated competitors have continued to take market share from ILECs, eliminating such artificial competitive disadvantages has become urgent. Some states, including Florida and Indiana, have taken action to strengthen their communications sectors by eliminating such outdated regulation.[116] Many states, however, continue to regulate ILECs as though they were utility companies providing monopoly services. Not only do such legacy regulations make no sense today, but they affirmatively delay the transition to next-

[116] *See* Chapter 2011-36, Laws of Florida; Ind. Code § 8-1-2.6. Similarly, in Texas, a comprehensive deregulatory bill was signed into law last week, to take effect in September 2011. *See* An Act Relating to communications services and markets, SB 980 (Tx. Legislative Session 82(R), May 20, 2011) (the enrolled version can be reviewed at http://www.legis.state.tx.us/tlodocs/82R/billtext/pdf/SB00980F.pdf#navpanes=0). The Michigan Legislature is also considering a deregulatory bill, which passed the House and is now before the Senate. *See* Substitute HB 4314 (which passed the House on April 26, 2011).

generation technologies, and they are inconsistent with the targeted, technology-neutral approach to universal service that the *NPRM* contemplates. *NPRM* ¶¶ 24, 31, 82. Saddling ILECs with burdensome regulation their competitors do not face is not only bad public policy, but it can frustrate federal broadband and universal service objectives in a variety of ways. Any state regulation that requires an ILEC to maintain a copper network, or that otherwise impedes its ability to transition to an IP network or to participate in the federal USF regime, directly conflicts with this Commission's stated USF and broadband goals. *See* Section IV-C, *supra*; AT&T Comments at 62-64.

It is encouraging that various states are currently examining their legacy service regimes, and many are likely to join leaders like Indiana and Florida in eliminating these impediments to the transition to IP networks. As AT&T observes, this Commission "has an important role to play in encouraging states to reform their existing obligations," and could consider creating incentives for states to undertake reform. AT&T Comments at 61. But to the extent states continue to impose obsolete service obligations that conflict with federal law and policy promoting the transition to next-generation technologies, this Commission should exercise its preemption authority. *Id.* at 62-71.

C. State USF Mechanisms Should Not Be Permitted to Thwart Federal USF Policies.

As discussed above, to the extent state regulation impedes migration from legacy infrastructure, it should be eliminated as inconsistent with national universal service and broadband policies. Layering certain state USF policies over the federal ones could frustrate those same federal universal service and broadband objectives by distorting carefully balanced federal USF mechanisms. The point of a retargeted comprehensive federal USF regime is to create appropriate incentives for firms to relinquish reliance on legacy technologies and associated subsidy flows, and to encourage broad participation in the new technology-neutral competitive bidding processes. Any state action that perpetuates such legacy technologies or subsidy flows, or that reduces the competitiveness of the reverse auction process, is inconsistent with federal universal service and broadband policy.

As discussed above and in Verizon's initial comments, to the extent a transitional access replacement fund is necessary any such funding should be structured to avoid perpetuating dependence on the very subsidy streams that are being phased out. That means the transitional fund should sunset at a date certain, disburse less than 100 percent of lost access revenue, and avoid disbursing any funds for revenue the carrier could earn by charging its end users a reasonable retail rate. To the extent a state were to undercut those key elements, such as by extending the period during which carriers can receive disbursements or by providing the carrier with "make-up" recovery from state universal service fund, such a state policy would directly conflict with the balanced incentive structure of federal USF policy. The Commission should work in cooperation with the states to avoid such conflicts. And in appropriate cases the Commission should exercise its preemption authority to ensure that state USF policies do not undercut federal ones.

VI. CONCLUSION.

For these reasons and those discussed in Verizon's initial comments, the Commission should act as soon as possible to step down all intercarrier compensation rates to a single, low terminating rate of $0.0007 for all traffic and all technologies. At the same time the Commission should repurpose the Universal Service Fund for broadband by first adopting its proposal to cap the fund and eliminate remaining CETC support.

Respectfully submitted,

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May 23, 2011

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