



March 28, 2012

Ms. Marlene H. Dortch  
Secretary  
Federal Communications Commission  
445 12th Street, SW  
Portals II, Room TW-A325  
Washington, DC 20554

**RE: Universal Service Contribution Methodology, WC Docket No. 06-122;  
Federal-State Board on Universal Service, CC Docket No. 96-45; and  
A National Broadband Plan for Our Future, GN Docket No. 09-51**

Dear Ms. Dortch:

The Commission needs a more workable universal service contribution system. The National Broadband Plan appropriately recognizes that updating the way we “fund the fund” to reflect dramatic changes in the communications market over the last several years is as important as repurposing Universal Service Fund (USF) distributions for broadband. Now that the Connect America Fund is established and on its way to being implemented, USTelecom and its member companies understand that the Commission is actively working on improvements to the universal service contribution system. We applaud that effort. Problems with the current interstate-revenue based contribution mechanism are many, and they go beyond the size of the base or the dizzying height of the contribution factor.<sup>1</sup> The current USF contributions system is also rife with outdated methods and procedures that create waste, inefficiency and destabilizing competitive discrepancies. Merely broadening the base will not fix these procedural issues, but rather will simply result in spreading these problems to other services.

We write to highlight many of the problems with the current USF contribution system, and to explain the reasons for and results of those problems. USTelecom and its members encourage the Commission to seek input on comprehensive solutions that can transform USF contributions for the future. We also recognize that this process is not likely to happen quickly,

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<sup>1</sup> The Commission, itself, has recognized as much. *See, e.g., Federal-State Joint Board on Universal Service*, CC Docket No. 96-45 (and related proceedings), 17 FCC Rcd 24952, ¶ 3 (2002):

Although the interim measures we adopt today will improve the current contribution methodology, they do not address our concerns regarding the long-term viability of any revenue-based system. . . [I]nterstate telecommunications revenues are becoming increasingly difficult to identify as customers migrate to bundled packages of interstate and intrastate telecommunications and non-telecommunications products and services. This has increased opportunities to mischaracterize revenues that should be counted for contribution purposes . . . [which] may result in decreases in the assessable revenue base . . . Customers are also migrating to mobile wireless and Internet-based services.

and that the current problems with USF contributions will continue to fester, plaguing competition, facilitating waste, and driving inefficiency. Therefore, USTelecom suggests today some potential common sense solutions that the Commission should act on immediately.

### **Fundamental Problems with the Current System**

Today's interstate telecommunications revenue-based USF contribution mechanism may sound simple to those who are not required to implement it. However, in reality the utter lack of bright-line rules results in myriad ambiguities involving the fundamental principles of the Commission's contribution mechanism. It has been clear for years that not all contributors are resolving these ambiguities in a consistent fashion. The three threshold issues that muddy the current contribution methodology are:

- **Classification distinctions.** The distinction between assessable telecommunications revenues and non-assessable non-telecommunications revenues underpins the current system. However, this distinction is increasingly impossible to make during the transition to an all-IP environment where a wide array of converged services is offered by many competing providers over broadband platforms. With the rapid introduction of these new broadband IP-based services into the market, the dividing line between telecommunications or telecommunications services on one hand, and information services on the other, is becoming increasingly blurred. And the traditional Commission mechanisms for providing guidance about the contribution obligations for these services – rulemakings or declaratory rulings – simply cannot keep pace. Indeed, it took the Commission *more than three years* to resolve a controversy over the contribution obligations for prepaid calling cards.<sup>2</sup> This problem worsens every day as consumers purchase more and more sophisticated IP-based products, which are frequently bundled with other services and offered for a single price. These difficulties hinder the roll-out of new and innovative services and bundles of services that consumers want as providers grapple with difficult classification and USF assessment questions, while also creating significant competitive inequities as competing providers come to different conclusions about their contribution obligations.
- **Jurisdictional distinctions.** The current system is also based on the historical idea that services are either intrastate or interstate in nature, that providers can readily distinguish revenues associated with each jurisdiction, and that consumers purchase different, jurisdiction-based services. These things are no longer true. Stand-alone wireline IXC's no longer exist, most wireless services are based on national pricing models, and state boundaries are simply irrelevant to how consumers select and buy communications

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<sup>2</sup> See *AT&T Corp. Petition for Declaratory Ruling Regarding Enhanced Prepaid Calling Card Services*, WC Docket No. 03-133 (filed May 15, 2003); *AT&T Corp. Petition for Declaratory Ruling Regarding Enhanced Prepaid Calling Card Services*, WC Docket No. 03-133, Order and Notice of Proposed Rulemaking, FCC 05-41 (released Feb. 23, 2005); *Regulation of Prepaid Calling Card Services*, WC Docket No. 05-68, Report and Order, FCC 06-79 (released June 30, 2006). Of course, as we note below, there are other prepaid calling card contributor disputes that have been pending at the Commission for almost six years.

services. Across markets, consumers purchase bundles, or even unlimited capacity, of any-distance voice, data, and other services—increasingly over IP platforms. Thus, from the financial perspective of most consumers, but for USF fees, a “long distance call” is meaningless.

- **Resale/Wholesale Distinctions.** The universal service processes surrounding wholesale-reseller situations are burdensome and ineffective. The current system effectively turns wholesale providers into enforcement agents of the Commission, requiring them to collect certifications from reseller customers attesting to USF contributions. Service providers therefore become subject to or exempt from contribution obligations based on who has the proper certifications, rather than whether the revenues earned by the service providers in question fit the definition of assessable telecommunications revenues. The Commission has even looked to wholesalers to “make up” reseller contributions if it turns out that a reseller did not contribute to the fund, despite the wholesaler’s inability to recover those contributions from its reseller. On the reseller side, these providers must navigate many varying wholesale provider certification procedures.

These three ambiguities result in significant competitive inequities of at least two types. First, service providers have the incentive to minimize their contribution obligations by reading the rules and administrative instructions in a fashion to support that outcome. Second, the current system only captures contributions from a few among many providers that offer competing voice services, which unfairly penalizes traditional voice providers (and ultimately their customers) and artificially skews the market. For example, voice service providers such as Google Voice, Skype,<sup>3</sup> and Magic Jack do not contribute to the fund directly—either because their business models do not generate any end-user revenue or because they contend that the IP-nature of their services makes them non-assessable. These services, however, compete directly with traditional voice services offered by providers that must contribute to the fund. Such services also use and benefit from the same network to complete calls and generate revenue. Other providers that offer voice and data services over IP platforms also contend that those services are not assessable. These inequities worsen as the contribution factor increases since a greater contribution factor produces a larger distortion in the marketplace between contributors and non-contributors.

### **Longstanding Uncertainty Undermines Compliance and Collections**

The result of these problems with the current USF system is significant confusion—and sometimes gamesmanship—among universal service contributors and consumers. For the Commission, the current system has also produced dozens of appeals of contribution decisions made by the Universal Service Administrative Company (USAC) and requests to the full Commission for review of Wireline Competition Bureau (Bureau) decisions on those appeals.

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<sup>3</sup> Skype does publicly report some earned revenue and may or may not contribute to the fund on some portion of that revenue. Skype is not, however, currently listed in the Commission’s online Form 499A database as a USF contributor using the legal or trade name “Skype.” *See* <http://fjallfoss.fcc.gov/cgb/form499/499a.cfm> (last visited March 28, 2012).

The Commission's rules require it to resolve USAC appeals within 90 days.<sup>4</sup> The Commission misses this deadline repeatedly. Instead, USF contribution-related appeals languish at the Commission for years (some are never resolved), especially those that involve the most vexing and significant contribution issues. In certain instances, the Commission's failure to act on pending contributor appeals can have the effect of picking winners and losers in the marketplace. Pending USAC contribution appeals include:

- Cingular Interactive Appeal<sup>5</sup> – filed in January 2004: This appeal, left unaddressed for 8 years, raises rudimentary telecom/information service ambiguities
- SBC AFR<sup>6</sup> – filed in January 2005: SBC argues that the application of disparate deadlines depending on whether Form 499 revisions are favorable or unfavorable to the contributor is arbitrary and capricious. As enforced, it is a substantive revision of the Commission's rules and/or orders that was adopted in violation of APA requirements for notice and comment.
- Cingular Appeal<sup>7</sup> – filed in March 2006: Cingular appeals a USAC decision that Cingular was not entitled to apply the wireless safe harbor to “mobile toll” revenues, and that Cingular was therefore required to jurisdictionalize these revenues.
- IDT Appeal<sup>8</sup> – filed in April 2006 and AT&T Corp. Appeal<sup>9</sup> – filed in October 2006): *Compare* IDT's appeal of a USAC audit finding regarding IDT's classification of virtually all of its prepaid calling card revenue as wholesale revenue that is exempt from USF contribution *with* AT&T's appeal, in which AT&T explains how it reports its prepaid calling card wholesale revenue in its contribution base because it does not have a reasonable basis to conclude that its wholesale customers are making direct USF contributions. The Commission's failure to act on these appeals for almost six years has provided at least one prepaid calling card provider with an unfair competitive advantage in the marketplace.
- AT&T Corp. Appeal<sup>10</sup> – filed in October 2006, Global Crossing Appeal<sup>11</sup> – filed in June 2007, Grande Appeal<sup>12</sup> – filed in December 2009, and XO Appeal<sup>13</sup> – filed in December 2010: These parties appealed USAC's reclassification of reseller revenues as end-user

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<sup>4</sup> 47 C.F.R. § 54.724.

<sup>5</sup> See <http://apps.fcc.gov/ecfs/document/view?id=6515683562>.

<sup>6</sup> See <http://apps.fcc.gov/ecfs/document/view?id=6516887169>.

<sup>7</sup> See <http://apps.fcc.gov/ecfs/document/view?id=6518332519>.

<sup>8</sup> See <http://apps.fcc.gov/ecfs/document/view?id=6518333417>.

<sup>9</sup> See <http://apps.fcc.gov/ecfs/document/view?id=6519809365>.

<sup>10</sup> See <http://apps.fcc.gov/ecfs/document/view?id=6519809365>.

<sup>11</sup> See <http://apps.fcc.gov/ecfs/document/view?id=6519535778>.

<sup>12</sup> See <http://apps.fcc.gov/ecfs/document/view?id=7020355007>.

<sup>13</sup> See <http://apps.fcc.gov/ecfs/document/view?id=7021025154>,

<http://apps.fcc.gov/ecfs/document/view?id=7021025155>, <http://apps.fcc.gov/ecfs/document/view?id=7021025156>, <http://apps.fcc.gov/ecfs/document/view?id=7021025157>, <http://apps.fcc.gov/ecfs/document/view?id=7021025158>.

revenues simply because resellers did not contribute (rather than on the basis of reasonable expectations that said resellers would contribute).

- XO Appeal<sup>14</sup> – filed in December 2010: XO appeals a USAC decision that reclassified certain XO Multi-Protocol Label Switching-enabled service revenue from information service revenue to telecommunications service revenue, and imposed additional requirements to determine the jurisdiction of private line circuits.

Even when the Commission has attempted to resolve contribution issues, little progress has been made. In September of 2009, the Bureau sought comment on a number of long pending contribution issues that USAC had brought to the Commission for resolution during the course of audits. Despite receiving comments and replies from over 20 different parties (covering an overwhelming majority of the contribution base) that, in their disparate opinions, confirmed the desperate need for Commission clarification, no such clarification has been forthcoming on the hardest issues. While it is impossible to estimate the contributions that are or are not being made as a result of ongoing confusion on these issues, given the potential revenues involved they are likely to be significant.

### **The Commission Should Consider Reform to Transform USF Contributions for the Future**

Ultimately, the only solution to these problems is fundamental and comprehensive reform that takes account of changes in the market and can be administered efficiently and with competitive neutrality. There are several principles that should guide fundamental reform including but not limited to: the contribution base should be stable and predictable; all providers should contribute in a competitively neutral manner; consumer impacts should be equitably distributed and minimized consistent with the public interest benefits of USF; and administrative efficiency should be maximized. These principles are not served by the classification issues that are intrinsic to the current USF contributions methodology.

### **Immediate Administrative Reforms That Should Be Made**

USTelecom and its members encourage the Commission to seek input on comprehensive solutions that can transform USF contributions for the future. We also recognize that this process is not likely to happen quickly, and that the current problems with USF contributions will continue to fester, plaguing competition, facilitating waste, and driving inefficiency. Therefore, USTelecom suggests today some potential common sense solutions that the Commission should act on immediately. As the Commission considers whether and how to transform the USF contribution system, and even if it is left fundamentally unchanged, the irrational and inefficient administrative processes that plague the current mechanism must be eliminated. At a minimum, the Commission should also seek expedited comment on solutions to

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<sup>14</sup> See <http://apps.fcc.gov/ecfs/document/view?id=7021025154>, <http://apps.fcc.gov/ecfs/document/view?id=7021025155>, <http://apps.fcc.gov/ecfs/document/view?id=7021025156>, <http://apps.fcc.gov/ecfs/document/view?id=7021025157>, <http://apps.fcc.gov/ecfs/document/view?id=7021025158>.

the following issues, and preferably adopt tentative conclusions that will expedite the needed reform. These measures will allow the Commission to act promptly to stabilize USF contributions and establish a foundation for comprehensive, lasting reform.

- **Notice and comment on Form 499 instruction changes.** There is, by now, no question that the Form 499A Worksheet Instructions matter—and they matter a lot. Because the USF contribution factor is so significant, how contributors report their revenues and the specific decisions they make in filling out the Form 499 drives market behavior. Regrettably, in the past the Commission has used changes in the Form 499 instructions to put in place substantive requirements without adherence to standard notice and comment procedures under the Administrative Procedures Act. The solution is simple. The Commission should identify, on an annual basis, any proposed changes to the Form 499A or its instructions, explain the reasons for those changes, and seek comment on the revised form and instructions each year. The Commission should also clarify that any changes to the instructions apply only on a going-forward basis. The Commission follows a similar annual process when publishing the E-Rate eligible services list.
- **Amnesty for good faith interpretations.** The Commission should invite carriers to meet with Commission staff to explain how they have, in good faith, interpreted certain 499 instructions and ask the Commission to confirm or modify the 499 instructions accordingly. If the Commission disagrees with how the carrier has interpreted the instructions – so long as the carrier was not clearly acting in bad faith – there would be no adverse consequence to the carrier (i.e., no referral to Enforcement Bureau and no USAC audit finding on that issue). This process would enable staff to identify areas that lacked clarity and make modifications to the instructions so that there would be no further confusion by other carriers. Again, staff would have to put out for comment any resulting 499 modifications.
- **Symmetric contribution liability and refund periods.** The Commission should repeal the asymmetrical one-year deadline for providers to re-file their Form 499As if form amendments would reduce their contributions. The one-year deadline to seek a refund conflicts with the Bureau-set, open-ended obligation to re-file forms that would increase contributions. The one-year deadline is procedurally defective and wrong as a matter of policy. There often are very good reasons why a carrier cannot meet the deadline for amending a Form 499A. For example, government agencies—such as state public service commissions, taxing authorities, and even the Commission itself—and internal and external auditors may make decisions that require restatements extending beyond one year. A symmetrical limitations period (e.g., three years) to restate revenues in either direction would be more equitable to contributors and provide greater certainty for the Commission.
- **Reduced volatility in the contribution factor.** A more stable USF contribution factor from quarter-to-quarter would reduce consumer frustration and administrative burdens. As it stands, there are often significant swings in the contribution factor throughout the year, which makes it difficult for consumers to budget and requires contributors to make

billing and other administrative adjustments on a continuous basis. The current system of revenue projections and true-ups also unfairly penalizes contributors that are unable to project their revenues with precision. The Commission should consider an annual contribution factor—which the Telecommunications Relay Service and other Commission programs use -- and other process changes to enhance program stability. The Commission and USAC have ample experience and information to show that over the course of a year, the volatility in the factor tends to average out, which proves that an annual contribution factor would be reasonable as well as administratively more efficient.

- **Reseller exemption process changes.** As discussed above, the current process that turns wholesale providers into Commission enforcement agents and at the same time subjects resellers to myriad certification procedures and uncertainty must improve. It is unreasonable to place wholesale providers in the position of policing their competitors while requiring them to bear the financial risks associated with any disputes arising from the Commission’s rules. These requirements appear only in the Form 499 Worksheet Instructions and have never been subject to notice and comment. Distinguishing between “reseller” and “end-user” revenue can be difficult —and the consequences for drawing the line in the wrong place under the current system make little sense. At the very least the Commission should fully vet this process in a rulemaking context. One way to improve the situation may be to eliminate the provider-to-provider certifications in favor a bright-line rule based on widely accessible information in a Commission-maintained database.
- **Reassess reporting safe harbors.** The publicly available Form 499 industry roll-up data make clear that relatively little USF revenue is assessed based on the jurisdictional “safe harbor” percentages set by the Commission. For example, it appears that the vast majority of wireless revenue is subject to contributor-specific traffic studies that approximate the percentage of revenue that is interstate. Safe harbors that are set too high are not useful as a reporting tool because—for competitive reasons—contributors cannot afford to subject a greater portion of their revenues to universal service assessments than other providers. The Commission should recall that the purpose of the safe harbor was to reduce contributor burdens, rather than (by setting it too high) simply to force contributors to conduct a traffic study. The Commission should revise the safe harbor percentages based on the historical data it now has available to it. In addition, the Commission should determine whether safe harbor reporting makes sense for wireline services as well.
- **Realistic prepaid calling card reporting requirements.** Like the reseller certification procedures, the prepaid calling card revenue reporting requirements have evolved in a piecemeal fashion through ambiguous changes to the Form 499 instructions. Providers interpret these requirements differently. The current requirement that providers must report the “face value” of a card as assessable revenue—not the amount actually paid by

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the carrier's end-user customer—is particularly unrealistic. Many cards do not have a face value, and in any event contributing providers often do not know and have no control over the retail price of a calling card. The FCC should adopt a reporting mechanism for these services that addresses the unique characteristics of these services.

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USTelecom and its members, look forward to working with the Commission to improve the universal service contribution system. Should you have any questions about the issues discussed herein, please contact us.

Sincerely yours,



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USTelecom – The Broadband Association

cc: Carol Matthey  
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