

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C.

In the Matters of

Universal Service Contribution Methodology

A National Broadband Plan For Our Future

WC Docket No. 06-122

GN Docket No. 09-51

JOINT REPLY COMMENTS OF UNDERSEA CABLE OPERATORS

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SUMMARY AND INTRODUCTION

The record in this proceeding supports retention of the “international-only” exemption and the limited interstate revenues exemption (“LIRE”) or its functional equivalent. No commenter has made a credible legal argument for elimination of either exemption, and no commenter supporting the elimination of one or both exemptions has given any consideration to the economic distortions to the international undersea cable capacity market that would result from the elimination of either exemption. In fact, the disproportionate nature of resulting Universal Service Fund (“USF”) contributions due on revenues from sales of international undersea cable capacity in relation to the purported benefits of U.S. PSTN connectivity would violate the Export Clause of the United States Constitution. The Undersea Cable Operators¹ therefore continue to urge the Commission to reject these FNPRM proposals.

¹ The Undersea Cable Operators include: Global Crossing Americas Solutions, Inc., GT Landing II Corp., Level 3 Communications LLC, Office des postes et télécommunications de

I. THE RECORD DOES NOT SUPPORT THE ELIMINATION OF THE INTERNATIONAL-ONLY EXEMPTION OR THE LIRE

As the Undersea Cable Operators demonstrated in their initial comments, and as the record makes evident, the clear language of the statute, its legislative history, and the Commission's consistent statutory interpretation, in concert with the decision of the only court to have considered the question, all require the Commission to retain the international-only exemption and the LIRE. Supporters of the FNPRM's proposals to eliminate the exemptions offer weak, results-driven justifications that address neither the legal infirmities of the FNPRM's proposals nor the new and substantial economic distortions they would create.

A. No Commenter Has Made a Credible Legal Argument for the Elimination of These Exemptions

No commenter in this proceeding has made a credible legal argument that would support elimination of the international-only exemption or the LIRE.² As the Undersea Cable Operators explained in their initial comments, Section 254(d) requires the Commission to retain the

Polynésie française, Pacific Carriage Limited, PPC-1 Limited, PPC-1 (US), Inc., and Southern Cross Cables Limited.

² See, e.g., Comments of BBG Communications, Inc., WC Docket No. 06-122 & GN Docket No. 09-51, at 2-9 (filed July 9, 2012) ("BBG Comments"); Comments of Cable & Wireless Americas Operations, Inc., WC Docket No. 06-122 & GN Docket No. 09-51, at 1-3 (filed July 6, 2012) ("CWAO Comments"); Comments of Harris CapRock Communications, Inc., WC Docket No. 06-122 & GN Docket No. 09-51, at 1-4 (filed July 9, 2012) ("Harris CapRock Comments"); Joint Comments of International Carrier Coalition, WC Docket No. 06-122 & GN Docket No. 09-51, at 4-6 (filed July 9, 2012) ("Int'l Carrier Coalition Comments"); Comments of Logical Telecom, L.P., WC Docket No. 06-122 & GN Docket No. 09-51, at 2-8 (filed July 9, 2012) ("Logical Telecom Comments"); Comments of NobelTel, LLC, WC Docket No. 06-122 & GN Docket No. 09-51, at 2-8 (filed July 6, 2012) ("NobelTel Comments"); Comments of Pacnet Services Corporation Limited, WC Docket No. 06-122 & GN Docket No. 09-51, at 2-7 (filed July 9, 2012) ("Pacnet Comments"); Comments of PC Landing Corp., WC Docket No. 06-122 & GN Docket No. 09-51, at 3-10 (filed July 9, 2012) ("PC Landing Comments"); Comments of the Satellite Industry Association, WC Docket No. 06-122 & GN Docket No. 09-51, at 8-18 (filed July 9, 2012) ("SIA Comments"); Comments of Telstra, Incorporated and Australia-Japan Cable (Guam) Limited, WC Docket No. 06-122 & GN Docket No. 09-51, at 2-9 (filed July 9, 2012) ("Telstra Comments").

international-only exemption, as it grants the Commission jurisdiction over interstate providers only.³ Extending the Commission’s jurisdiction to international-only services would require Congress to amend the statute, which it has repeatedly declined to do.⁴ Since Congress enacted Section 254(d) in 1996, the Commission has consistently interpreted Section 254(d) to preclude the Commission from requiring providers of exclusively foreign telecommunications to contribute to the USF.⁵

Similarly, supporters of the FNPRM’s proposal to eliminate the LIRE offer no credible justification for ignoring *Texas Office of Public Utilities Counsel v. FCC*.⁶ As the record here demonstrates, the Fifth Circuit’s decision in *TOPUC* and the language of Section 254(d) require the Commission to retain the LIRE or its functional equivalent.⁷ The *TOPUC* decision rejected the Commission’s “contamination” theory of jurisdiction, *e.g.*, that providing any interstate service would subject a provider to USF contributions for all its end-user revenues in either interstate or foreign communications, as failing to satisfy the “equitable and nondiscriminatory” requirements of Section 254(d). No commenter supporting elimination of the international-only exemption or the LIRE has even attempted to explain why the weak jurisdictional nexus between

³ Joint Comments of Undersea Cable Operators, WC Docket No. 06-122 & GN Docket No. 09-51, at 5-14 (filed July 9, 2012) (“Undersea Cable Operators’ Comments”).

⁴ See Undersea Cable Operators’ Comments at 8-13; PC Landing Comments at 3-5.

⁵ See Undersea Cable Operators’ Comments at 5-6; CWAO Comments at 1-2; Int’l Carrier Coalition Comments at 4; Logical Telecom Comments at 2-3; NobelTel Comments at 2-3; Pacnet Comments at 2-3; PC Landing Comments at 3-10; SIA Comments at 8-10; Telstra Comments at 7-9..

⁶ 183 F.3d 363 (5th Cir. 1999) (“*TOPUC*”).

⁷ See Undersea Cable Operators’ Comments at 14-17; BBG Comments at 2-3; CWAO Comments at 1-2; Harris CapRock Comments at 4-5; Comments of iBasis, Inc., WC Docket No. 06-122 & GN Docket No. 09-51, at 2-7 (filed July 9, 2012); Int’l Carrier Coalition Comments at 4-6; NobelTel Comments at 4-6; SIA Comments at 11-12; Telstra Comments at 2-6.

revenues from international undersea cable capacity sales—for transport mostly outside the United States, often provided to a customer located outside the United States—satisfies the Commission’s proposed “benefit” rationale for extending USF contribution obligations to all foreign-communication end-user revenues. Neither has any commenter supporting elimination of the international-only exemption or the LIRE attempted to explain why the FNPRM’s proposals would be consistent with the Commission’s own pronouncements in connection with its settlement-rate benchmarks proceeding, namely that one country’s carriers and consumers should not be forced to subsidize unfairly the universal service programs of another country.⁸

B. Commenters Supporting the Elimination of the International-Only Exemption and the LIRE Have Summarily Failed to Address the Policy Implications of Such Elimination on Undersea Cable Systems

No commenter supporting the FNPRM’s proposals addresses the economic distortions that would result from the elimination of the international-only exemption or the LIRE. Indeed, the record is clear that the FNPRM’s proposals would reintroduce the same kinds of economic distortions and practical problems caused by the capacity-based methodology for annual regulatory fees (“IBC fees”) on undersea cable operators, which the Commission replaced in 2009. At most, supporters suggest that eliminating these exemptions would eliminate any

⁸ Undersea Cable Operators’ Comments at 23-25. *See also International Settlement Rates*, Report and Order on Reconsideration and Order Lifting Stay, 14 FCC Rcd. 9256, 9260 ¶ 14 (1999) (“Foreign governments are free to choose their own policies, but international law does not require U.S. consumers to subsidize those [universal service] policies.”); *International Settlement Rates*, Report and Order, 12 FCC Rcd. 19,806, 19,848 ¶ 86 (1997) (stating that “we disagree that foreign termination services from certain countries should be required to finance a disproportionate share of network costs, or that foreign carriers should have the ability to impose hidden, discriminatory universal service obligations on termination services for foreign-originated calls.”), *aff’d*, *Cable & Wireless P.L.C. v. FCC et al.*, 166 F.3d 1224, 1230 (D.C. Cir. 1999) (holding that the Commission could not justify adoption of the FNPRM proposals by asserting (as it did with settlement-rate benchmarks) that it does not exceed its authority “simply because a regulatory action has extraterritorial consequences”).

“unfair advantage” that qualifying providers might have over non-qualifying competitors.⁹ But the FNPRM’s proponents offer no evidence that an “unfair advantage” currently exists in the market for undersea cable capacity or is sufficiently problematic to require such a dramatic “solution.” In fact, the record supports the Undersea Cable Operators, as international cable system providers such as Cable & Wireless Americas Operations, Pacnet Services Corp., and Pacific Crossing Landing Corp. identify the same kinds of policy concerns regarding the likely market-distorting effect of the FNPRM’s proposals.¹⁰

At most, proponents of eliminating the international-only exemption and the LIRE contend that these exemptions distort competition by favoring international providers over domestic providers, thereby harming consumers.¹¹ The record amply contradicts such conclusory assertions. The international-only exemption and the LIRE protect international providers offering no or incidental interstate services from improperly subsidizing U.S. domestic universal service programs with contributions for activities conducted exclusively or mostly in foreign jurisdictions or in areas beyond the limits of any nation’s jurisdiction. The LIRE also ensures that providers offering incidental provision of interstate services may compete effectively and need not incur a loss to do so,¹² particularly as the LIRE’s 12-percent threshold has fallen below the actual contribution factor over the last several years.¹³

⁹ See Comments of COMPTTEL, WC Docket No. 06-122 & GN Docket No. 09-51, at 31-33 (filed July 9, 2012) (“COMPTTEL Comments”).

¹⁰ See CWAO Comments at 2; Pacnet Comments at 5-6; PC Landing Comments at 10-11.

¹¹ See, e.g., Comments of Verizon, WC Docket No. 06-122 & GN Docket No. 09-51, at 31-32 (filed July 9, 2012); COMPTTEL Comments at 31-33.

¹² See CWAO Comments at 2.

¹³ See Undersea Cable Operators’ Comments at 16; Telstra Comments at 5-6.

II. USF ASSESSMENTS ON PROVIDERS OF EXCLUSIVELY OR PREDOMINANTLY FOREIGN COMMUNICATIONS WOULD TAX EXPORTS IN VIOLATION OF THE EXPORT CLAUSE OF THE U.S. CONSTITUTION

A number of commenters have noted the FNPRM's faulty assumption that providers of exclusively or predominantly foreign communications benefit equally from PSTN connectivity as do providers of purely domestic interstate communications, thereby justifying the proposals to eliminate the international-only exemption and the LIRE and to assess USF contributions on all foreign communications inbound to, or outbound from, the United States.¹⁴ The Undersea Cable Operators believe that the lack of correlation between the resulting USF contributions and the benefits that such providers would receive also create a constitutional problem. By eliminating the international-only exemption and/or the LIRE and thereby assessing USF contributions on providers of exclusively or predominantly international services, the Commission would tax exports of telecommunications services and other telecommunications in violation of the Export Clause of the United States Constitution.

The Export Clause states, "No Tax or Duty shall be laid on Articles exported from any State."¹⁵ The Export Clause was originally proposed by delegates from the Southern States to the Federal Convention out of concern that the Northern States would control Congress and use this control to impose taxes and duties on Southern exports, thus raising a disproportionate share of federal revenues from the Southern States.¹⁶ The language of the Export Clause, however, is broad and absolute, leading the U.S. Supreme Court to conclude that "the Framers sought to

¹⁴ See, e.g., NobelTel Comments at 9-10; Telstra Comments at 8-9; Undersea Cable Operators' Comments at 24.

¹⁵ U.S. CONST., art. I, § 9, cl. 5.

¹⁶ See *United States v. Int'l Bus. Machs. Corp.*, 517 U.S. 843, 859 (1996) (citing 2 M. Farrand, *The Records of the Federal Convention of 1787*, 95, 305-08, 359-63 (rev. ed. 1966)).

alleviate . . . concerns [that the Northern States would tax exports to the disadvantage of the Southern States] by completely denying to Congress the power to tax exports at all.”¹⁷

A. The Export Clause Prohibits Taxes on the Exportation of Services as Well as Goods

Although the U.S. Supreme Court has had “few occasions to interpret” the Export Clause, its cases “have broadly exempted from federal taxation not only export goods, but also services and activities closely related to the export process.”¹⁸ Specifically, the Court has held that the Export Clause “categorically bars Congress from imposing any tax on exports,”¹⁹ including both goods and services, “during the course of exportation.”²⁰ The U.S. Supreme Court has accordingly struck down taxes levied on a broad range of exports, including insurance policies,²¹ sporting goods,²² and certain stamp taxes.²³

Although the few U.S. Supreme Court cases to consider the Export Clause have largely discussed the exportation of physical goods or services closely linked to tangible goods (*e.g.*, insurance policies on goods in transit, etc.), neither the Export Clause nor the case law limits the applicability of the Export Clause to physical goods only.²⁴ The concept of an “export” is not

¹⁷ *United States v. U.S. Shoe Corp.*, 523 U.S. 360, 368 (1998) (quoting *IBM*, 517 U.S. at 861).

¹⁸ *IBM*, 517 U.S. at 846.

¹⁹ *U.S. Shoe*, 523 U.S. at 363.

²⁰ *IBM*, 517 U.S. at 848.

²¹ *Id.* at 863.

²² *A.G. Spalding & Bros. v. Edwards*, 262 U.S. 66 (1923).

²³ *Fairbank v. United States*, 181 U.S. 283 (1901).

²⁴ *See, e.g., IBM*, 517 U.S. at 863-81 (Kennedy, J., dissenting) (arguing that the challenged statute constituted a tax on a service related to an export, not to an export, and contending that the Export Clause applies only to items actually being exported). Justice Kennedy’s dissent does not suggest that services cannot be exported, but rather that export-related services that are not themselves subject to export do not fall within the scope of the Export Clause.

limited to physical goods.²⁵ Other courts have referred to “goods” as a kind of short-hand for “exports” in an effort to distinguish between “items in commerce” covered by the Export Clause.²⁶ But the language of the Export Clause itself sweeps more broadly, protecting “articles” in transit, not just tangible goods. The term “article” is not confined to physical or tangible goods, and indeed such a limited definition would undermine the meaning of statutory provisions referring to services in export. The U.S. Government recognizes in many contexts that services can be exported, just as goods.²⁷

Consequently, the U.S. Supreme Court has struck down as unconstitutional taxes on exports fees imposed on insurance premiums and taxes designed to support harbor maintenance services.²⁸ It has likewise rejected generally applicable, nondiscriminatory taxes on ship charters and marine insurance, holding that each was “in substance a tax on the exportation; and a tax on the exportation is a tax on the exports.”²⁹ Even though a tax on policies insuring exports “is not,

²⁵ See Black’s Law Dictionary, 660 (9th Ed. 2009) (defining the verb “export” as “[t]o send, take, or carry (a good or commodity) out of the country; to transport (merchandise) from one country to another in the course of trade” or “[t]o carry out or convey (goods) by sea”); *Canton R.R. Co. v. Rogan*, 340 U.S. 511, 515 (1951) (noting that “[t]o export means to carry or send abroad”).

²⁶ See, e.g., *Carnival Cruise Lines, Inc. v. United States*, 200 F.3d 1361, 1364 (Fed. Cir. 2000) (rejecting argument that Harbor Maintenance Tax applied to cruise passengers violated the Export Clause because “[t]he passengers on Carnival’s cruise ships are neither ‘articles’ nor ‘goods.’ They are people. The application of the Harbor Tax to them would not involve the laying of any tax upon ‘Articles’ exported from any state. ‘Articles’ and ‘goods’ relate to items of commerce, not people.”).

²⁷ See, e.g., 22 U.S.C. § 2778(a)-(b) (prohibiting, as part of the Arms Export Control Act, the export of defense articles and defense services on the United States Munitions List that cannot be exported without a license); 15 U.S.C. § 4721(b) (providing that a purpose of the U.S. Commercial Service is the promotion of the export of goods and services from the United States); 31 C.F.R. §§ 560.204 *et seq.* (prohibiting exportation, reexportation, sale, or supply of goods, technology, or services to Iran).

²⁸ See, e.g., *U.S. Shoe*, 523 U.S. at 369; *IBM*, 517 U.S. at 843.

²⁹ See *United States v. Hvoslef*, 237 U.S. 1, 17 (1915); see also *Thames & Mersey Marine Ins. Co. v. United States*, 237 U.S. 19 (1915).

precisely speaking, the same as a tax on exports,” the Court has held that “they are functionally the same under the Export Clause.”³⁰

B. To Avoid Characterization as an Impermissible Tax, a Charge on Exports Must Correlate the Value of Services, Facilities, or Benefits Provided to the Exporter with Respect to Those Exports

The Export Clause does not bar all government-imposed assessments. The Export Clause permits certain permissible user fees that reflect a fair approximation of services, facilities, or benefits to the exports, “provided that the fee lacks the attributes of a generally applicable tax or duty and is, instead, a charge designed as compensation for Government-supplied services, facilities, or benefits.”³¹ When “determining what constitutes a bona fide user fee,”³² the Court requires that a user fee must reflect a close connection between the service the Government renders and the compensation it receives for the service. Fees that vary in proportion to the quantity or value of the good or service are unlikely to pass scrutiny. In *Pace*, the Court upheld an export-stamp charge that remained fixed, regardless of the size or value of the package at issue, and that was not excessive in light of the fraud-prevention service it performed.³³ In upholding the stamp charge, the Court concluded that it was, in fact, “compensation given for services properly rendered.”³⁴

The Court has struck down *ad valorem* taxes as impermissible taxes on exports.³⁵ In *U.S. Shoe*, the Court rejected the application of the Harbor Maintenance Tax (“HMT”) to exports. The Customs Service collected the HMT for use in harbor maintenance and development

³⁰ *IBM*, 517 U.S. at 854-55 (discussing *Thames & Mersey*, 237 U.S. 19).

³¹ *U.S. Shoe*, 523 U.S. at 363.

³² *Id.* at 369.

³³ *See Pace v. Burgess*, 92 U.S. 372, 375-76 (1875).

³⁴ *Id.* at 375.

³⁵ *See U.S. Shoe*, 523 U.S. at 369.

projects, and related expenses. The HMT obligated exporters, importers, and domestic shippers to pay 0.125 percent of the value of the commercial cargo they shipped through U.S. ports. For exports, shippers paid the HMT at the time of loading, meaning before the shipments traveled through U.S. ports. When U.S. Shoe Corp. objected to paying the HMT, the Customs Service responded that it was a statutorily mandated user fee, not a tax on exports.³⁶ The Supreme Court disagreed, rejecting the government’s argument that the HMT—despite its name³⁷—constituted a permissible user fee.

Applying *Pace*, the Court concluded that the “value of export cargo . . . does not correlate reliably with the federal harbor services used or usable by the exporter” and that the HMT did not “fairly match the exporters’ use of port services and facilities.”³⁸ The HMT, unlike the stamp charge in *Pace*, was determined entirely on an *ad valorem* basis. As a result, “the connection between a service the Government renders and the compensation it receives for that service must be closer than [was] present here.”³⁹ Accordingly, the Court rejected the HMT as an unconstitutional tax on exports.

C. USF Assessments on Providers of Exclusively or Predominantly International Undersea Cable Services Would Constitute an Impermissible *Ad Valorem* Tax on the Export of International Telecommunications

Here, the FNPRM’s proposed USF assessments on providers of exclusively or predominantly international services would constitute an impermissible *ad valorem* tax on the export of telecommunications, rather than a user fee. Undersea cable operators export

³⁶ *Id.* at 363-64.

³⁷ *Id.* at 367 (noting that courts “must regard things rather than names” and identifying the “crucial question” as “whether the HMT is a tax on exports in operation as well as nomenclature or whether, despite the label Congress has put on it, the exaction is instead a bona fide user fee”).

³⁸ *Id.* at 370.

³⁹ *Id.* at 369.

telecommunications services and other telecommunications from the United States to foreign countries because they provide a communication or transmission from the United States to a foreign country.⁴⁰

The United States has long recognized that services, including telecommunications, can be exported from (and imported into) the United States. In the General Agreement on Trade in Services (“GATS”), the United States and its trading partners codified this understanding that a variety of services—including basic telecommunications, value-added telecommunications, financial, accountancy, legal, construction, and myriad other services—could be exported and traded, just as physical goods are traded.⁴¹ The Fourth Protocol to the GATS—which includes the United States’ schedule of specific commitments in basic telecommunications services, a term that covers both “telecommunications services” as defined in the Communications Act and “other telecommunications” as defined by the Commission—expressly codified obligations regarding trade in basic telecommunications services.⁴² The United States considers the schedule of telecommunications commitments part of its WTO obligations, and has further implemented its scheduled commitments in Commission regulations.⁴³

The FNPRM’s proposed assessments are not correlated with the value of the services provided to the payor. Instead, the FNPRM’s proposals to assess USF contributions on

⁴⁰ See, e.g., 47 U.S.C. § 153(21) (defining “foreign communications”).

⁴¹ General Agreement on Trade in Services, WTO Agreement, Annex 1B, The Results of the Uruguay Round of Multilateral Trade Negotiations: The Legal Texts 325 (GATT Secretariat 1994), *reprinted in* 33 I.L.M. 1167 (1994).

⁴² Agreement on Telecommunications Services, Fourth Protocol to the General Agreement on Trade in Services, S/L/20, (Apr. 30, 1996), *reprinted in* 36 I.L.M. 354, 366 (1997).

⁴³ See *Rules and Policies on Foreign Participation in the U.S. Telecommunications Market*, Order, FCC 98-10, 13 FCC Rcd. 6219 (1998); see also Laura B. Sherman, “Wildly Enthusiastic” About the First Multilateral Agreement on Trade in Telecommunications Services, 51 Fed. Commc’ns L.J. 61, 97-99 (1998).

international-only services and on the services provided by a provider with only limited interstate revenue would constitute an impermissible *ad valorem* tax on exports. As in *U.S. Shoe*, the proposed USF assessment would be determined entirely on an *ad valorem* basis, in this case, the value of the revenues from the services provided. Like the HMT, the assessment would not fairly match the exporters' use of the PSTN services and facilities. This is so because undersea cable operators provide transport services using their facilities located largely or mostly outside the United States, often to customers located outside the United States,⁴⁴ and often for purposes of Internet backbone connectivity and access to Internet content.⁴⁵ Undersea cable system capacity is often sold on a ring-configuration or protected basis. The actual traffic carried on the system therefore may or may not touch the United States, even though the customer would purchase the right to carry U.S.-inbound or U.S.-outbound traffic. The USF contribution is not assessed in connection with the value of services provided to the payor, in this case the undersea cable operator. The total contribution assessment varies in proportion to the revenues (e.g., the value) of the services provided and nothing demonstrates that the contribution factor correlates reliably with the PSTN connectivity—if any—used by the undersea cable system. The FNPRM's proposal to subject such exports to USF contribution assessments would therefore tax exports, in violation of the Export Clause of the U.S. Constitution.

⁴⁴ See Undersea Cable Operators' Comments at 5, 23-25; see also, e.g., PC Landing Comments at 6.

⁴⁵ See Undersea Cable Operators' Comments at 21-23.

CONCLUSION

For the reasons stated above and in their initial comments, the Undersea Cable Operators urge the Commission to retain the “international-only” exemption as well as the LIRE or its functional equivalent.

Respectfully submitted,



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