Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	

To: The Commission

COMMENTS OF COBANK, ACB

CoBank, ACB[1] ("CoBank") hereby submits these comments in response to the Wireline Bureau's request for comment on the Rate of Return Represcription Staff Report.[2] CoBank is concerned about specific references to CoBank in the Staff Report that are incorrect and seeks to correct the record.[3]

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[1] CoBank is a $95 Billion national cooperative bank serving vital industries across rural America. The bank provides loans, leases, export financing and other financial services to agribusinesses and rural power, water and communications providers in all 50 states.

CoBank is a member of the Farm Credit System, a nationwide network of banks and retail lending associations chartered to support the borrowing needs of U.S. agriculture and the nation's rural economy. In addition to serving its direct retail borrowers, the bank also provides wholesale loans and other financial services to affiliated Farm Credit associations serving approximately 70,000 farmers, ranchers and other rural borrowers in 23 states around the country.

Headquartered outside Denver, Colorado, CoBank serves customers from regional banking centers across the U.S. and also maintains an international representative office in Singapore.

[2] *Wireline Competition Bureau Seeks Comment on Rate of Return Represcription Staff Report, Comment Cycle Established* WC Docket Nos. 10-90, 07-135, 05-337, and 03-109, GN Docket No. 09-51, CC Docket Nos. 96-45 and 01-92, and WT Docket No. 10-208 (re. May 16, 2013) (*Public Notice*)

[3] *Prescribing the Authorized Rate of Return: Analysis of Methods for Establishing Just and Reasonable Rates for Local Exchange Carriers*, WC Docket No. 10-90, Staff Report, DA 13-1111 (Wireline Comp. Bur. rel. May. 16, 2013) (*Staff Report*).

CoBank is an experienced and sophisticated banker to the communications sector, with more than $2.8 billion in loan commitments to more than 200 rural communication companies nationwide. These commitments by sector are comprised of wireline (73%), cable television (15%) and wireless (12%). In addition, CoBank has syndicated $2.7 billion in communication loans to the Farm Credit System and commercial banks. CoBank is the lead administrative agent for many key syndicated communications facilities, including financings for Atlantic Tele-Networks, Inc., Frontier Communications, and Northeast Communications of Wisconsin, Inc. Participants in these CoBank-led deals have included other Farm Credit System institutions as well as commercial institutions such as Goldman Sachs, Wells Fargo, and Deutsche Bank.

CoBank is one of the strongest and safest banks in the United States and the world.[4] CoBank's total assets as of March 31, 2013 were $95 billion.[5] Based upon the Federal Financial Institutions Examination Council's list of the Top 50 Bank Holding Companies as of March 31, 2013,[6] CoBank's total assets would put CoBank at position number 28. As of March 31, 2013, CoBank's permanent capital, total surplus, core surplus and net collateral ratios exceeded the

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[4] *Global Finance* April, 2013

[5] CoBank March 31, 2013 Quarterly Report, (available at http://www.cobank.com/Newsroom-Financials/Financial-Reports.aspx), at p. 3.

[6] *Available at* http://www.ffiec.gov/nicpubweb/nicweb/Top50Form.aspx. This list includes only bank holding companies. While CoBank is not a bank holding company and thus not included in the list, the Bureaus cited this list, and agreed that CoBank's total assets as of June 30, 2012 (which exceeded $90 billion) "would put CoBank at position number 28 if it were a bank holding company." *See, Mobility Fund Phase I; Waiver of Section 54.1007(a)(1) of the Commission's Rules*, WC Docket No. 10-90; WT Docket No. 10-208; AU Docket No. 12-25, Order, DA 12-1747 (WCB WTB rel. Nov. 1, 2012) n.26 ("*Waiver Order*").

regulatory minimums.[7] As the Bureaus recently concluded, CoBank's assets make it comparable to banks in the top 50 based on total assets."[8]

CoBank strives to correct the misstatements about CoBank's business practices and to enlighten the Federal Communication Commission (FCC) as to how CoBank evaluates loans to rural Local Exchange Carriers (RLECs).

CoBank is a Market-based Lender

The Staff Report incorrectly states that CoBank does not charge market based interest rates.[9] The following paragraph from the Staff Report is misleading and incorrect:

> 49. We note that it may be necessary to reduce, or cap, the embedded cost of debt due to the availability of government subsidized loans to most, if not all, rate-of-return carriers. When the interest rates carriers face are not market-based but rather subsidized by the government or by non-profit entities (*e.g.*, the Rural Utilities Service (RUS), CoBank, or the Rural Telephone Finance Cooperative (RTFC)), these subsidized rates must be taken into account in calculating carriers' cost of debt. This is because RLECs may have access to loans at below market interest rates; for example, RUS currently offers loans with interest varying from current Treasury rates to no more than five percent. If such extensive funding is readily available to most RLECs from these sources, then even a generous estimate of the cost of debt should be no more than the current highest rate charged by RUS, CoBank, or RTFC. It is unclear, however, whether it would be feasible and/or unduly burdensome for a carrier to finance all of its assets with loans from these lenders, and to refinance older debt at current rates.

Congress specifically directed the Farm Credit System to charge market rates. The Farm Credit Act of 1971 as amended clearly states:

> … Further, it is declared to be the policy of Congress that Farm Credit System institutions take action in accordance with the Farm Credit Act Amendments of 1986 in such manner that borrowers from the institutions derive the greatest benefit practicable from that Act: Provided, that in no case is any borrower to be charged a rate of interest

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[7] CoBank March 31, 2013 Quarterly Report, p. 12.

[8] *Waiver Order*, p. 9.

[9] *Staff Report*, p. 19.

> that is below competitive market rates for similar loans made by private lenders to borrowers of equivalent credit-worthiness and access to alternative credit.[10]

In addition, CoBank's independent regulator, the Farm Credit Administration regulates that CoBank charge market interest rates.[11] According to a General Accounting Office study, Farm Credit System rates were higher than rates at large banks and about the same as rates available from insurance companies.[12] As a factual matter, CoBank does not offer subsidized rates to any of its customers, including in the rural telephone sector. CoBank charges a market rate to telecommunication customers consistent with the creditworthiness of the borrower, with higher risk customers required to pay a higher interest rate consistent with marketplace pricing practices. There is no such thing as a CoBank "subsidized" interest rate for telecommunication borrowers. Moreover, CoBank has no legal authority, governmental requirement, or financial capacity for offering a "subsidized" interest rate. As a result, CoBank must and does charge market interest rates to telecommunications company borrowers.

The other misleading implication from paragraph 49 of the Staff Report is that all RLECs have access to "extensive funding" from CoBank under the existing rate-of-return (RoR) regulations. Regrettably, many RLECs do not meet CoBank's lending standards due to the various caps and limitations on universal service funding and inter-carrier compensation. It is unfortunate that the uncertainty of a stable, predictable cost recovery mechanism is making it

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[10] 12 U.S.C. 2001 Sec. 1.1.(c)

[11] *Loan Pricing by Farm Credit System Institutions,* Farm Credit Administration, February 11, 1999 (*Informational Memorandum) and BL-062 Evaluating Strategies and Risks for Loan Pricing and Structure, Farm Credit Administration May 13, 2010 (Bookletter)*

[12] General Accounting Office, *Farm Credit System: Repayment of Federal Assistance and Competitive Position*, GAO/GGD-94-39 at 139 (1994).

increasingly difficult for CoBank to extend credit for the purpose of deploying ubiquitous rural broadband networks.

We ask the that the Staff Report be corrected to reflect accurately CoBank's requirement to charge a market interest rate to all telecommunication company borrowers and to remove any comments that suggest in any way that CoBank provides subsidized interest rate loans to telecommunication companies. We further ask the paragraph 49 of the Staff Report be removed in its entirety given it is misleading with respect to the availability of funding to RLECs. Finally, we ask that the Staff Report include a paragraph discussing the lack of funding availability for RLECs given that unpredictability in the cost recovery mechanism because of limits and caps on universal service funding and inter-carrier compensation adversely impact RLEC creditworthiness. Essentially, lenders are constrained with respect to prudent and appropriate RLEC lending, consistent with regulatory underwriting and credit administration requirements, when the income capacity of a RLEC borrower is not reasonably predictable and well-established over time. [13]

<u>CoBank Lending Standards</u>

The Staff Report misstates the importance CoBank places on using "TIE = Earnings before Interest and Taxes/Interest Charges" to evaluate loans. On page 46 of the Staff Report it states that CoBank's loan standard is TIE Ratio = 1.5. This is an inaccurate statement. The full picture is that CoBank uses a variety of key ratios for decision-making and risk assessment including:

• Debt/EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization);

[13] See 12 CFR 614.4150 Lending policies and loan underwriting standards.

• Equity/Assets (we frequently adjust this ratio to market, especially if book equity has been depressed by accounting for mergers or net operating losses from non-cash depreciation expense);
• Debt Service Coverage (DSC) which is (EBITDA – taxes / principal payments on long term debt + interest expense); and
• EBITDA/Interest Expense.

As CoBank has commented numerous times, for those communication companies serving high-cost areas, deploying affordable broadband is not economically possible without a sufficient, sustainable, and predictable level of support. CoBank views RoR regulation for RLEC customers as an important component to their ability to continue to service existing debt and obtain future access to debt capital. RoR regulation is an important component of CoBank's evaluation of potential loans. While incentive regulation can work for larger consolidators, the vast majority of RLECs are too small, and operate in areas where subscriber density is too low for price-cap or other incentive regulation to be viable. With the new caps and limitations on Universal Service Fund (USF) and the decrease of Interstate Common Line Support (ICLS) from the *USF/ICC Transformation Order and Further Notice*, any reduction in the prescribed RoR will further decrease the ability of RLECs to obtain debt capital. The authorized RoR is a factor in determining USF support and ICLS, therefore decreasing the RoR will further reduce the cost recovery possible. If RLECs don't have a sufficient, sustainable and predictable level of support, deploying affordable broadband is not economically possible and; therefore, not bankable.

CoBank recognizes that the FCC is examining alternative rural broadband funding mechanisms in a careful and thoughtful manner. While alternative funding mechanisms are being examined, CoBank requests that the authorized RoR not be lowered to provide at least one component of stability for the existing funding mechanisms.

Respectfully submitted,

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June 21, 2012