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

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
Local Exchange Carrier Rates	)	WC Docket No. 07-135
	)	
Universal Service	)	WC Docket No. 05-337
	)	
Lifeline and LinkUp	)	WC Docket No. 03-109
	)	
National Broadband Plan	)	GN Docket No. 09-51
	)	
Universal Service	)	CC Docket No. 96-45
	)	
Intercarrier Compensation	)	CC Docket No. 01-92
	)	
Mobility Fund	)	WT Docket No. 10-208

COMMENTS OF THE
NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION

The National Cable & Telecommunications Association (NCTA) supports the Commission's efforts to establish an updated rate of return for use in calculating access charges and universal service support levels. The Commission should expeditiously implement the recommendations made by the Wireline Competition Bureau (Bureau) in its recent report regarding represcription of the authorized rate of return.[1]

INTRODUCTION

In the *CAF Order*, the Commission found "compelling evidence that our presently applied interstate rate of return, 11.25 percent, is no longer reflective of the cost of capital" and

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[1] PRESCRIBING THE AUTHORIZED RATE OF RETURN, Wireline Competition Bureau Staff Report, WC Docket No. 10-90 (rel. May 16, 2013) (Staff Report).

sought comment on prescribing a new authorized rate of return for incumbent local exchange carriers (LECs) that are subject to rate of return regulation.[2] The Commission noted that it had last conducted a rulemaking on this question in 1990 and that updating the cost of capital was necessary to ensure that incumbent LECs make economically sound investments.[3]

To assist the Commission in addressing the issues identified in the *CAF Order*, the Bureau prepared the Staff Report. The Staff Report finds that weighted average cost of capital (WACC) has fallen significantly since the 11.25 percent rate of return was established. Based on an exhaustive analysis, the Staff Report recommends that the Commission establish a rate of return between 8.06 and 8.72 percent.[4]

NCTA fully supports the Commission's decision to solicit comment on this issue and the Bureau's hard work in developing the record. As the Staff Report confirms, there is a significant gap between the debt and equity costs that incumbent LECs face in the marketplace and the much higher rate of return that they receive under the Commission's rules. It is long past time for the Commission to reassess, and reduce, the 11.25 percent rate of return that it adopted 23 years ago.

I. REPRESCRIPTION OF THE AUTHORIZED RATE OF RETURN IS LONG OVERDUE AND THE COMMISSION SHOULD QUICKLY IMPLEMENT THE RECOMMENDATIONS IN THE STAFF REPORT

Under traditional ratemaking principles, regulated carriers are entitled to the opportunity to earn a reasonable return on their investments in facilities that are used and useful in the provision of regulated services. While the Commission gradually has moved away from the use

[2] *Connect America Fund*, WC Docket No. 10-90 *et al.*, Report and Order and Further Notice of Proposed Rulemaking, 26 FCC Rcd 17663, 18052, ¶ 1047 (2011) (*CAF Order*).

[3] *Id*.

[4] Staff Report at ¶ 143 ("[G]iven historically low interest rates and the infrequency of represcription, we conclude that the rate of return should be in the upper half of that zone of reasonableness, from 8.06 percent to 8.72 percent.").

of traditional rate of return ratemaking over the last few decades, the Staff Report explains that the authorized rate of return continues to play an important role in the Commission's administration of the access charge and high-cost universal service regimes.[5]

In the *CAF Order*, the Commission recognized that marketplace conditions had changed significantly in the decades since it prescribed the 11.25 percent rate of return and that it was long past time to establish a new authorized rate of return.[6] Accordingly, the Commission sought comment on the various components of the WACC (cost of debt, cost of equity, capital structure) and reached a preliminary conclusion that the authorized rate of return "should be no more than 9 percent."[7]

The Staff Report provides extensive analysis that supports the Commission's preliminary conclusion. The Bureau finds that the cost of debt is 6.19 percent and the range of reasonableness for the cost of equity is between 10.54 and 11.58 percent.[8] Both of these are dramatically lower than was the case in 1990.[9] Based on these conclusions, and the Bureau's assessment of the appropriate capital structure, the Staff Report recommends that the Commission establish a rate of return between 8.06 and 8.72 percent.

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[5] *Id*. at ¶ 6 (Rate of return must be high enough so that a carrier "can maintain its credit-worthiness and attract capital" but be no higher than necessary for this purpose "because this would result in unreasonably high prices for consumers and excessive demands on USF.").

[6] *CAF Order*, 26 FCC Rcd at 18051-52, ¶¶ 1046-47.

[7] *Id*. at 18055, ¶ 1057.

[8] Staff Report at ¶¶ 48, 108. The Bureau notes that the two parties that commented on the cost of debt – NECA and Ad Hoc – both recommended even lower rates for the cost of debt. Id. at ¶ 50

[9] In 1990, the Commission found that the cost of debt was 8.8 percent and the cost of equity was 13.19 percent. *Id*. at ¶ 110.

Although not addressed in detail in the Staff Report, it is apparent that the Commission could have, and should have, reduced the authorized rate of return many years ago.[10] Allowing incumbent LECs to earn an additional 250 to 320 basis points above their actual cost of capital results in a massive windfall to those companies. As a result of the Commission's inaction, the access charges that are paid to LECs and the universal service contributions assessed on consumers have been much higher than they should have been for a very long time. With the analysis the Bureau has presented in the Staff Report, the Commission has no excuse for continuing to allow this overearning to take place at the expense of consumers.

CONCLUSION

Twenty-three years is far too long for the Commission to go without recalibrating its authorized rate of return. For the reasons explained above, the Commission should expeditiously implement the recommendations in the Staff Report.

Respectfully submitted,

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[10] For example, Appendix B shows how interest rates have been below the 1990 rate for the last two decades. *Id.*, App. B; *see also CAF Order*, 26 FCC Rcd at 18051-2, ¶ 1046 ("[T]he interest rate on the three month Treasury Bill has fallen from 7.83 percent in 1990 to 0.15 percent in January 2011.").