



USTELECOM
THE BROADBAND ASSOCIATION

September 3, 2013

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VIA HAND DELIVERY AND ECFS

Ms. Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: *Rebuttal of the American Cable Association Ex Parte Filing in the Virtual Workshop in Response to the Public Notice (DA 13-1136) on the Connect America Cost Model, WC Docket No. 10-90*

Dear Ms. Dortch:

On behalf of the ABC Coalition (“Coalition”), USTelecom submits the attached letter in response to the American Cable Association Ex Parte filing dated June 12, 2013. USTelecom’s letter includes an attachment containing Confidential Information subject to the Third Protective Order (DA 12-1418) in the above-referenced proceeding.

Pursuant to the terms of the Third Protective Order, one copy of the filing containing Confidential Information and two copies of the Redacted version are being filed with the Office of the Secretary. The Redacted version is also being filed electronically through the Commission’s Electronic Comment Filing System. In addition, two copies of the Confidential version are being delivered to Katie King of the Wireline Competition Bureau.

Should you have any questions concerning this filing, please do not hesitate to contact the undersigned.

Sincerely,

Robert Mayer
Vice President
Industry and State Affairs



September 3, 2013

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EX PARTE

Ms. Marlene Dortch
Secretary
Federal Communications Commission
445 12th Street, S.W.
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Re: Rebuttal of the American Cable Association Ex Parte Filing in the Virtual Workshop in Response to the Public Notice (DA 13-1136) on the Connect America Cost Model, WC Docket No. 10-90

Dear Ms. Dortch:

In the Virtual Workshop proceeding, one of the topics bore on how to choose the cost benchmarks parameters for the final model run. The FCC offered a number of revenue-based choices as well as a couple of cost-based options.

In the following pages, the ABC Coalition responds to the ACA's propositions regarding using a revenue approach in the event that the FCC eventually chooses to use a revenue benchmark. The Coalition feels, however, that given all of the frailties around determining an average revenue per unit (ARPU) (e.g., which voice and broadband service offerings to include, what service mix, what mix of promotional rates, what take rates), each of which could require specific study, that the cost-based options the FCC suggested would be a simpler approach. In particular, using the Order's guidance of not exceeding a level of Alternative Technology subscribers (not to exceed 1%), we feel that a target between 0.5% and 1%, while targeting \$1.8B in total funding, results in a lower cost benchmark that is clearly sufficiently high-cost such that it would meet the FCC's revenue objective and result in a reasonable selection of targeted census blocks (CBs).

ACA Asserts: "The FCC should not use one take rate for estimating costs and a different take rate for estimating expected revenues. Doing so would not only contradict widely accepted principles of network-planning and business case modeling, it would also over-compensate operators receiving Connect America Fund (CAF) Phase II funds."¹

The Connect America Cost Model (CAM) is not a network-planning model or a business case model, even though CAM relies on real-world engineering rules, equipment capacities and spatial realities. For example, CAM takes a scorched node approach for a new fiber to the

¹ See Ex Parte Letter of American Cable Association, WC Docket No. 10-90, (June 12, 2013) at 3.

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premise (FTTP) broadband network built to a steady state. These build assumptions are consistent with the *USF/ICC Transformation Order*² and the *Connect America Phase II Cost Model Platform Order*.³ In the *Platform Order*, the Bureau adopted a model platform that estimates “the full average monthly cost of operating and maintaining an efficient, modern network.”⁴ The Bureau found that the platform will “estimate the cost of providing service in the way that best approximates the discipline of the competitive market.”⁵ However, these assumptions intentionally do not correspond to the network planning or business-case modeling by which incumbent local exchange carriers (ILECs) will likely undertake to determine whether to accept all of the state-level commitments associated with the model-derived support. For example, network planning and business-case modeling will ordinarily start modeling based on the actual network existing in a particular area rather than presuming the existing network is irrelevant. Nevertheless, the Coalition agrees that the FCC should not use one take rate for estimating costs and a different take rate for estimating expected revenues. Here, the recognition of using the same take rate in developing costs and recognizing potential revenues does not rely on unique principles of network-planning modeling or business case modeling. Instead, it relies on a consistent comparison of costs and revenues.

In this context, ACA’s concern that CAM will over-compensate an ILEC accepting CAF II funding based on CAM is misplaced. In fact, the Coalition views that under-compensation is a much more likely outcome, particularly when the fund provides support for a maximum of five years, but the costs are levelized over much longer periods based on the economic lives of plant and equipment. Clearly, a support mechanism that covers costs only for a small portion of the lives of assets does not over-compensate participating ILECs. In addition, the forward-looking wireline network design used by CAM relies on an estimate of passing all potential demand points—not just locations where service may actually be provided at specific times, *i.e.*, costs are based on sizing a forward-looking broadband network based on every housing unit and every business location.⁶ When CAM uses locations to calculate cost per unit, the total costs cannot be covered unless revenue per revenue-generating unit is much greater than the cost per potential location, since revenues will not be generated for all locations. Also, at any one time some portion of those units are vacant, *i.e.*, contain no household or operating business. No revenues are generated from vacant units, but the model recognizes forward-looking costs so that a carrier has a network fully capable⁷ of serving all potential customer locations based on the take-rate,

² Report and Order and Further Notice of Proposed Rulemaking, *Connect America Fund, et al.*, WC Docket No. 10-90, et al., FCC 11-161, released November 18, 2011 (*USF/ICC Transformation Order*).

³ Report and Order, *Connect America Fund*, WC Docket No. 10-90, and *High-Cost Universal Service Support*, WC Docket No. 05-337, DA 13-807, released April 22, 2013 (*Connect America Phase II Cost Model/Platform Order* or *Platform Order*).

⁴ *Platform Order* at ¶11.

⁵ *Ibid.*

⁶ CAM does include special access demand locations in developing a forward-looking network design. However, CAM does not include costs attributable to such locations in its final cost calculations. See the Bureau’s Virtual Workshop queries on “Community Anchor Institutions” and “Business Locations,” and the Coalition’s responses submitted to the Virtual Workshop on July 18th and appearing shortly thereafter.

⁷ The CAM take-rate determines the number of locations that are actually connected to the network by a drop and optical network terminator.

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even if some are currently vacant. Next, the number of households and businesses that actually subscribe and pay revenue for services is some fraction of the occupied housing units and active business locations. The take rate used in CAM should reasonably accommodate the difference between all potential locations for which costs are developed and revenue-generating locations for which costs may be recovered.

To understand these comments better, consider the following example. Suppose that a company has 100 locations, which are all housing units, in an area with a monthly cost of \$50 each. Then, the total monthly cost for the area would \$5,000. Next, suppose that there is a 10% vacancy rate. Hence, there would be a maximum of 90 locations from which to cover the total monthly cost. Expanding this example, suppose that the take rate for a service provided to the occupied locations is 80% of households, then there are only 72 locations with revenue-generating customers. Therefore, the effective take rate associated with all locations is 72%, and the monthly cost per revenue-generating location is \$5,000 divided by 72 revenue-generating locations or \$69.44. In this example, the take rate to use in CAM would be 72%.

ACA Asserts: “In a typical network investment, the fixed cost of the network up to the curb of potential subscribers is incurred upfront, while the variable (“success-based”) costs of a drop, network interface device and customer premise equipment are not incurred until locations subscribe to the operator’s service.”⁸

The Bureau addressed this issue in the Platform Order when they adopted a model that estimates “*the full average monthly cost of operating and maintaining an efficient, modern network.*” Specifically, the model will begin by estimating all capital and operating expenses associated with the modern network. Those variously-timed expenditures will be converted to an average monthly cost...⁹ The Bureau found that a forward-looking model, rather than a business case model, best approximates the discipline of the competitive market. A forward-looking model of a hypothetical network is not a typical network installed by a provider over time. Over the *long-run* in economic terms, every location will be passed by the network and the take-rate for the service determines the percentage of locations passed that include drop and optical network terminator investment. Thus, the “success-based” locations to which ACA refers are recognized in the CAM take-rate application. CAM does not recognize timing of success-based locations as a business model does, since only long-run forward-looking economic cost may be included. In the *long run*, all costs are avoidable and should be included in the study “to estimate the full average monthly cost of operating and maintaining an efficient, modern network.”¹⁰ Levelized costs do not provide over-compensation, since the costs are levelized over the life of the plant, whereas, the compensation period of CAF II funding is only five years—much shorter than the life of any of the plant components in the model.

⁸ See Ex Parte Letter of American Cable Association, WC Docket No. 10-90, (June 12, 2013) at 4.

⁹ Platform Order at ¶11.

¹⁰ Ibid.

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ARPU Discussion

ACA presents a recommendation for an “ARPU-based” benchmark that the Coalition cannot replicate. The ACA methodology is based on prices for services that are not defined. For example, ACA states that it found and used the lowest non-promotional, non-contract price advertised for broadband that had at least 4 Mbps downstream and 1 Mbps upstream and voice packages with unlimited local and long distance minutes, if available. Many Price Cap carriers do not offer a 1 Mbps upstream speed, and it is not a common cable offering. Did ACA take the price of a broadband service that provided at least 1 Mbps upstream, which in some cases is associated with a 20 Mbps downstream and 5 Mbps upstream service or did they take the price of a 7 Mbps downstream, 896 Kbps upstream service as close enough to 1 Mbps upstream? Did the voice package include a consistent set of features across the spectrum of providers? ACA did not provide any details necessary to replicate ACA’s recommendation and did not provide sufficient specificity to permit others to develop needed details. So, the ACA recommendation should not be relied upon.

Setting the benchmark at a reasonable ARPU must recognize that not all customers purchase a package that includes both voice and broadband. There is a substantial percentage of customers who purchase stand-alone broadband and a large percentage of customers who purchase voice service alone. Additionally, at any point in time ARPU for voice and broadband customers reflects a mix of promotional rates and month-to-month rates as well as a variety of rates varying on speed of the service. The mix of these revenue sources must be recognized if the Commission is to find the census blocks where the cost of service is likely to be higher than can be supported through reasonable end-user rates alone. Data to provide an accurate ARPU is not currently available, since all providers of high speed internet, not just Price Cap carriers are necessary to fully assess average revenue per customer.

What data are available are current rate surveys of major providers of high-speed internet service collected by third-party companies, such as Telogical Systems. Telogical Systems is allowing USTelecom to provide its “High Speed Internet Services” National View for July 2013 of high speed internet prices to the FCC as Confidential Information (See Attachment) pursuant to the terms of the Commission’s Third Protective Order in this docket.¹¹

From the Telogical Systems survey data, USTelecom has summarized rates by carrier for services closest to the FCC’s 4 Mbps download and 1 Mbps upload standard. USTelecom chose

¹¹ This report provides a national view summary comparison of key competitors' High Speed Internet service offerings in 30 major U.S. markets. These markets have been carefully selected based on their size and on the variety of the competitive dynamic in each market. The list of competitors comprises major DSL, Cable and Fiber Internet Access providers. Collaborating information has been filed with the FCC consistent under the Third Protective Order. 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 a Unified Intercarrier Compensation Regime, Federal–State Joint Board on Universal Service, Lifeline and Link-Up Universal Service Reform–Mobility Fund*, WC DOCKET NOS. 10-90, 07-135, 05-337, 03-109, GN DOCKET NO. 09-51, CC DOCKET NOS. 01-92, 96-45, WT DOCKET NO. 10-208. (DA 12-1418) (“Third Protective Order”).

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the High Speed Internet (HSI) service level from each provider (cable, DSL, and fiber to the home (FTTH)) that offered the lowest download speed of at least 4 Mbps, without regard to upload speed. The promotional rates were summarized separately from the month-to-month rates. HSI services were then assumed to have an 80 percent take rate.

The price for voice service—including the local rate, federal Subscriber Line Charge (SLC), Access Recovery Charge (ARC), and local Extended Area Service (EAS) charge—was assumed to be \$30 per month. Voice service was assumed to have a 60 percent take-rate to account for wireless only and over-the-top voice service households. Rates for both HSI and voice services were averaged across all companies with no weighting factors.

Chart 1

Summary	Promo Rate	MtM Rate
Average Rates - HSI + Voice	\$ 58.54	\$ 76.03
Assumed Voice Rate	\$ 30.00	\$ 30.00
Average Rate - HSI	\$ 28.54	\$ 46.03
Average HSI Rate @ HSI Take	\$ 22.83	\$ 36.83
Average Voice Rate @ Voice Take	\$ 18.00	\$ 18.00
Average (Voice&HSI) Adj Rate	\$ 40.83	\$ 54.83

Assumptions

Take Rate	
Voice	60%
HSI	80%
Voice Rate \$	30.00

Based on the Telogical Systems survey, a range of reasonable rates for a service similar to the FCC's 4/1 HSI service falls between \$29 and \$46 per month, depending on the percentage of the customers receiving promotional rates versus month-to-month rates. Of course, these raw HSI rates must be adjusted for the take-rate, which is optimistically assumed to be 80 percent in the unserved areas. After adjusting for the HSI take-rate, the rate range falls to approximately \$23 to \$37 per month. Next, the assumed voice rate of \$30 is adjusted for the voice take rate of 60 percent. The assumed voice rate with a 60 percent take rate is \$18 per month. Thus, a reasonable range for an end user rate for a combination of voice and HSI service at 4/1 ranges between approximately \$41 and \$55 per month based on the Telogical Systems HSI survey data and the USTelecom assumptions.

Sincerely,



Robert Mayer
Vice President
Industry and State Affairs

Attachment (Redacted)

cc: Katie King (Two Copies of the Confidential Version)

US Telecom 4/1 HSI Rate Analysis

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**"CONFIDENTIAL INFORMATION - SUBJECT TO PROTECTIVE ORDER IN
WC DOCKETS NOS. 10-90, 07-135, 05-337, 03-109, GN DOCKET NO. 09-51,
CC DOCKET NOS. 01-92, 96-45, WT DOCKET NO. 10-208
BEFORE THE FEDERAL COMMUNICATION COMMISION"**



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High Speed Internet Report - National View - July 2013

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High Speed Internet Report - National View - Introduction - July 2013

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High Speed Internet Report - National View - DSL Pricing Charts - July 2013

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High Speed Internet Report - National View - Cable-Fiber Pricing Charts - July 2013

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e-Fiber Package Summary Table - July 2013

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Report - National View - DSL Package Summary Table - July 2013

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High Speed Internet Report - National View - Pricing Details - July 2013

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High Speed Internet Report - National View - Promotions Summary - July 2013

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High Speed Internet Report - National View - Analyst Notes - July 2013

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