



## TO DETERMINE USF SUPPORT IS NOT FEASIBLE

The comments filed for the most part agree that whatever the academic attractiveness of competitive bidding as a means of determining support, in the real world the practical obstacles are too great. The few parties supporting competitive bidding generally gloss over or ignore the practicalities. Several comments agreed with RICA's point that any competitive bidding process for a complex good or service requires extensive preparation, administration and supervision beyond the capabilities of regulators.<sup>1</sup> In the absence of such preparation and supervision, the inevitable result will be a "race to the bottom" by operators who will make an absolute minimum of investment in rural areas, meanwhile stranding the investment of carriers that have worked hard to ensure that advanced services are available everywhere.<sup>2</sup>

The very existence of RICA member CLECs that have gained substantial market share in rural areas underserved by large carriers is a result of historical and current disincentives to large carriers to invest in rural areas. Prior to adoption of the Universal Service Fund in the 1980s, large carriers serving both urban and rural areas were expected by state commissions to set local rates no higher, and often lower than urban rates. With higher costs and lower revenues, such carriers worked to minimize their rural investment. This financial pressure was eased in some areas in the 1980s with the introduction of the USF, but only in those areas where the study area average cost of the large company was significantly above national average. Financial pressure to ignore rural areas was increased by the 1996 Telecommunications Act, which brought the large companies urban areas under competitive pressures. Finally, the Commission's model based support system for large carriers eliminated any USF support in all but a few states.

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<sup>1</sup> WTA at 19-27; GVNW Consulting at 11-15; NECA at 8; TDS at 5-9.

<sup>2</sup> CenturyTel at 13.

The result of this long history of regulatory incentives to ignore rural areas was that the rural portions of large company service areas became communications backwaters. When local competition became possible in 1996, many of these underserved communities turned to neighboring rural telephone companies who had excellent reputations for providing modern, high quality service. The rural telephone companies responded by overbuilding the large companies' outdated, and ill maintained facilities with modern communications plant capable of providing the services needed to allow these communities to keep up with the rapidly changing world.

The financial ability of rural CLECs to meet the service demands of rural areas has been limited, however, by the general absence or inadequacy of USF support. Because CLEC support remains tied to the support of the large ILEC as described above, the USF mechanism does not recognize the need for support in smaller, high cost areas. Changing to a competitive bidding system would create a new incentive for large carriers to avoid investing in rural areas while at the same time providing a means to eliminate pesky CLECs that have substantially eroded their market share in the few areas in which they operate. A large ILEC with old, fully depreciated plant and facing competition in only a few of its rural exchanges, will always be able to underbid a small company serving only high cost exchanges.

Further practical issues are described at length in Professor Dale Lehman's paper attached to the NTCA comments.<sup>3</sup> Dr. Lehman points out that competitive bidding has been used occasionally in developing countries where there was no significant existing infrastructure, but where substantial investment has already taken place, it is extremely difficult to create a

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<sup>3</sup> Dale E. Lehman, *The Use of Reverse Auctions for Provision of Universal Service*, attached to Comments of NTCA, October 10, 2006. ("Lehman")

transition mechanism that both permits recovery of prudent investment, but is not biased in favor of any current provider.<sup>4</sup>

The paper also discusses the potential for carriers to submit unrealistically low bids, and then seek to renegotiate support levels under threat of bankruptcy.<sup>5</sup> This is a phenomena observed on occasion in this country with respect to cable television franchising. Franchise authorities that awarded franchises to the applicants based on promises to provide the most service at the lowest cost to consumers frequently found the franchisee back in a year or two seeking to increase rates, reduce service or approve a transfer to another entity that would not be bound by the promises of the first.

## II ALTERNATIVE MEASURES TO CONTROL GROWTH OF THE USF SHOULD NOT DISCRIMINATE AGAINST RURAL CLECS

Several commenting parties that opposed competitive bidding, suggested that a better method to control growth of the USF would be to restrict support to competitive ETCs.<sup>6</sup> RICA's comments pointed out that, at least in the area of non-rural telephone companies, the structure of Section 214(e) does not permit the Commission or the states to limit the number of ETCs designated in a particular area. It follows, therefore, that a support mechanism that denied support to all but one carrier would defeat the intent of this provision of the act and would not stand.

In addition to the legal impediments, restricting designation or support to the ILEC, even if a separate mobility eligibility were created, would mean that the ILECs would often then be

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<sup>4</sup> In addition to the proposal included with the Public Notice that would provide ILECs a monopoly on USF support for 10 years, several parties promote such bias as desirable, and advocate making support for competitive carriers only subject to competitive bidding. Fairpoint at 16.

<sup>5</sup> Lehman at 21.

free from wireline facilities-based competition in their rural exchanges, and, as a practical matter, relieved of any pressure to improve service in rural exchanges.<sup>7</sup> In most areas where RICA members have ETC designation, they are the only facilities based competitive wireline service provider with ETC designation, although there may be multiple wireless ETCs receiving support in any given area. Any rule changes that are intended to reduce the number of ETCs receiving support must recognize that substantial harm to subscribers could result from eliminating support to rural CLECs.

Further, the criticisms of providing support to CETCs are largely not applicable to CLECs.<sup>8</sup> For example, CMRS providers receive “access replacement” support components, even though they did not have access charges reduced. Rural CLECs, however, did have their access charges reduced by the MAG plan, and received no offsetting support. Rural CLECs also bear the higher switching expenses associated with rural exchanges for which rural ILECs receive local switching support, but do not receive that support because they generally compete with large carriers that are ineligible for such support.<sup>9</sup>

For several years RICA has made the point that the current “portability” rule has no rational basis and does not provide “sufficient” support, i.e., support is either too little or too much. RICA members are prepared to cost justify their support requirements, but they should

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<sup>6</sup> Frontier at 8; Embarq at 18; OPASTCO at 12.

<sup>7</sup> RICA recognizes that many of the comments favoring restriction on support for CETCs is aimed at, or the result of, the support currently received by wireless ETCs, which accounts for approximately 97% of the CETC support. Balhoff & Rowe/Independent Telephone and Telecommunications Alliance (“BR/ITTA”) at 21.

<sup>8</sup> The BR/ITTA comments recognize that the growth problem to be addressed is related to wireless CETCs. BR/ITTA at 45, fig. 13.

<sup>9</sup> As described above, RICA members are able to obtain the very substantial market penetration they do because the large carrier has long neglected the area, creating unmet demand for quality service. Generally, small rural ILECs provide excellent service, so that a competitor

not be excluded from receiving USF support where it is necessary to meet the goals of the Act, because of problems with support for wireless carriers.

### **III CONCLUSION**

The comments demonstrate that at a minimum there would be enormous challenges to implementing a competitive bidding system that would function as well as, to say nothing of better than, as the present cost based system. The problems with the current system can be addressed with much less expenditure of resources and uncertainty and in an internally consistent manner by referencing all support to an appropriate measure of cost. Any solution must recognize that rural CLECs have made substantial investments in areas neglected by large incumbent ILECs to meet the public policy goals of ubiquitous deployment of advanced services.

Respectfully submitted,

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November 8, 2006

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is unlikely to obtain the market share necessary to support an overbuild.