Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	)	
	)	
Connect America Fund	)	WC Docket No. 10-90
	)	
A National Broadband Plan for Our Future	)	GN Docket No. 09-51
	)	
Establishing Just and Reasonable Rates for Local Exchange Carriers	)	WC Docket No. 07-135
	)	
High-Cost Universal Service Support	)	WC Docket No. 05-337
	)	
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	
Federal-State Joint Board on Universal Service	)	CC Docket No. 96-45
	)	
Lifeline and Link-Up	)	WC Docket No. 03-109

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INTRODUCTION AND EXECUTIVE SUMMARY

In the *National Broadband Plan*, the Commission articulated an ambitious goal: ensuring that *all Americans* have access to, and use, broadband and IP-enabled services.[1] That goal is within reach, but achieving it will require a bold new vision for advancing universal service and a sharp break from the antiquated policies of the past.

The existing universal service and intercarrier compensation regime is teetering on the brink of collapse. Adopted in the era of local exchange monopolies, that regime is no longer adequate to the task of rationally preserving universal service even on the legacy, public switched telephone network ("PSTN"). And it is utterly incapable of advancing universal service on the all-IP communications network of the future. Indeed, as discussed below, the Commission's existing policies are actively *hindering* broadband investment and adoption in high-cost areas, denying millions of Americans the benefits of next-generation technology.

Achieving the Commission's broadband goals will require far more than incremental changes to the current system. That system is irretrievably broken and, in any event, is ill-suited to the characteristics of Internet Protocol ("IP") networks and the competitive environment in which they are deployed. Instead, what is needed is sweeping reform that jettisons the inefficient regulatory mandates and mechanisms of the existing regime and replaces them with an efficient, market-driven approach to interconnection, interprovider compensation, and universal service that empowers providers to deploy broadband networks and offer IP-enabled services throughout the nation.

The existing universal service and intercarrier compensation regime is an outdated relic of a bygone era. Today's universal service and intercarrier compensation policies were

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[1] FCC, *Connecting America: The National Broadband Plan*, at xi (2010) ("*National Broadband Plan*").

adopted as part of a “regulatory compact” between public-utility regulators and local exchange carriers. Under that compact, regulators required carriers to serve all customers in a given geographic area at regulated rates, but granted carriers an exclusive franchise and a guaranteed rate of return on their investment. Carriers recovered the costs of local exchange service through a variety of “implicit subsidy” mechanisms designed to keep retail rates affordable and thereby ensure universal service. Policymakers kept “basic local” rates in rural, high-cost areas artificially low by permitting carriers to charge above-cost rates for a variety of services, including, among others, business services and vertical features. And “basic local” rates for all customers were subsidized by above-cost long distance service. After the divestiture of AT&T in 1984, the long-distance subsidy was maintained by imposing access charges on interexchange carriers for origination and termination of long-distance traffic. This regime played an important role in ensuring universal service in the monopoly, wireline telecommunications marketplace that predominated for much of the last century.

But the communications marketplace of today is far different from the one that regime was designed for. Incumbent carriers no longer enjoy exclusive franchises, but must compete with a variety of intra- and intermodal competitors to retain their customers. And because regulators did not deregulate rates and services after opening the market to competition, implicit subsidies continue to inflate incumbents’ rates for low-cost and business customers, making it easy for competitors (who are not required to serve high-cost customers at below-cost rates) to undersell the incumbents. Moreover, carriers also confront a dramatic drop in access revenues as consumers abandon traditional telecommunications services for alternative means of communicating. Finally, many carriers serving high-cost areas receive little or no support from federal and state universal service mechanisms, leaving them with an unfunded mandate to serve

customers at below-cost rates without the implicit subsidies that once made those rates possible. These combined pressures have rendered the legacy universal service and intercarrier compensation regime untenable even with respect to traditional circuit-switched services; replicating any part of this regime for IP-enabled services would severely undermine the nation's broadband goals.

The Commission should sweep away the legacy obligations of the past and adopt a new "regulatory compact" that is appropriate for IP communications. To achieve universal service in an all-IP world, the Commission must adopt a *new* regulatory compact—one that abolishes monopoly-era prescriptive regulations and relies instead on a procurement model for universal service and a market-driven approach to interconnection and interprovider payments. Only through such a fundamental reimagining of its regulatory role can the Commission fully realize its broadband goals.

Elimination of legacy carrier-of-last-resort and similar service obligations is an essential element of the new regulatory compact. These obligations, which require incumbent providers to serve every customer in their designated service areas, made sense only in the monopoly era when regulators foreclosed competition and *guaranteed* carriers sufficient revenues to offset the costs of providing service. With the advent of competition, there are no such guarantees. Competition has eroded the implicit subsidies on which carriers once relied to fund universal service. And the federal universal service fund and its state counterparts have not begun to provide the full complement of *explicit* support needed to close the enormous and still growing gap between costs and revenues for many carriers in high cost areas. These combined challenges will grow even more insurmountable as the Commission eliminates access charges and transitions legacy universal service support to a broadband-only mechanism.

In this environment, legacy service obligations that require incumbents to offer obsolete services in high-cost areas at below-cost rates make it more difficult for those providers to devote the capital necessary to deploy broadband and advanced services in high-cost areas. Equally important, legacy service obligations can, as a practical matter, require providers to continue providing service through a circuit-switched, TDM architecture, and they perpetuate the artificial division between "local" and "long distance" voice service. Thus, such obligations can serve as a legal obstacle to completing the transition to all-IP networks. But maintaining both a circuit-switched *and* a packet-switched network is costly and inefficient—and each dollar that a carrier is forced to invest in the former is one less dollar that can be invested in deployment of next-generation broadband facilities and services. Moreover, these harms are not offset by any countervailing benefit. There is no longer any need for a carrier of last resort when virtually every habitable area of the country has access, or soon will have access, to affordable wireless voice service—not to mention other competitive alternatives, including over-the-top VoIP. Given this, there is no valid policy justification for burdening any provider with a mandatory obligation to serve any and all customers with a 20th-century network and business model.

Instead of continuing to rely on service obligations that perversely *undermine* 21st-century universal service objectives, the Commission should adopt a new regime that promotes deployment of IP networks in high-cost areas. Specifically, the Commission should create a new universal service funding mechanism for broadband that provides targeted support to areas that are otherwise uneconomic to serve. This funding should be distributed through a procurement model, under which providers incur service obligations *only* to the extent they agree to perform them in explicit agreements with the Commission. Under this regime, carriers could not be compelled to serve high-cost areas, but would instead agree to serve those areas in exchange for

a specific amount of universal service funding. Providers' service obligations would be geographically and temporally defined, and regulators could not unilaterally abrogate the terms of the parties' "contract," as they have for legacy telecommunications services by opening markets to competition while failing to replace implicit subsidies with explicit support. These reforms would create certainty about the costs and benefits of participating in the Commission's broadband universal service program—and thereby encourage more providers to help accomplish the goal of ensuring that *all* Americans have access to broadband and IP-enabled services, at the lowest cost to all.

The Commission also should eradicate the antiquated intercarrier compensation system, which was part and parcel of the legacy universal service model, and impose a transitional regime to expedite the migration to converged IP networks, where prescriptive interconnection and intercarrier compensation rules will be as unnecessary in ten years as they have been for the past twenty. The exchange of packet-switched communications on the Internet has always been governed by market forces rather than prescriptive regulatory mandates. That regime—which has functioned well for decades and has adapted to astonishing changes in technology and traffic flows, all without government intervention—has efficiently facilitated the transmission of millions of VoIP-to-VoIP calls over the Internet. There will be no greater need to regulate such arrangements once *all* voice communications migrate from the PSTN to IP networks. To the contrary, engrafting a system of interconnection and interprovider compensation onto the Internet ecosystem would subject the Internet to a hornet's nest of intractable regulatory controversies similar to those that have roiled the PSTN for thirty years and could constrain the ability of that ecosystem to adapt and expand to meet the needs of consumers and the nation's economy.

The Commission should provide for a prompt but orderly transition to the all-IP end state. Comprehensive reform of the universal service and intercarrier compensation regime cannot be achieved overnight. Instead, the Commission should provide a glide path from the existing, highly regulated framework of today to the market-oriented framework of the future.

To ensure a smooth transition, the Commission must be clear from the outset about its end state and the timetable for reform. To that end, the Commission should establish a date certain—January 1, 2017—on which the transition to the new regime will be complete. As of that date, all legacy high-cost funding and all state and federal legacy service obligations should be terminated, and only the broadband support mechanism should remain. Similarly, as of that date, all interconnection and intercarrier compensation obligations on the PSTN should be terminated, and providers should be relieved of any obligation to provide legacy, circuit-switched, telecommunications services.

The Commission also should establish clear interim steps along the path to this end state. For intercarrier compensation, the Commission should unify, reduce, and ultimately eliminate intercarrier charges while providing opportunities for carriers to recover their lost revenues through gradual increases to artificially low end-user charges and through targeted universal service support. For universal service, the Commission should eliminate all legacy support over the course of five years and transition that support to a Connect America Fund ("CAF") for fixed broadband service and an Advanced Mobility Fund for mobile wireless broadband service. Further, the Commission should not delay progress by implementing the proposed Phase I mechanism, but should instead move directly to establishing and transitioning to the "long term" CAF. Finally, as the Commission ratchets down high-cost support, it should encourage states to free providers from their carrier-of-last-resort and other legacy service obligations and, to the

extent necessary, preempt such obligations. By establishing such interim steps, the Commission can prevent marketplace disruptions while the industry transitions to the minimally regulatory end state outlined above.

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In Part I below, we detail the flaws in the existing intercarrier compensation regime and explain why regulated intercarrier charges should be unified, phased down, and ultimately eliminated. We also explain why *any* prescriptive regulation is unnecessary once all voice traffic transitions to IP networks and urge the Commission not to disrupt the free-market framework that governs the exchange of IP traffic—including VoIP-to-VoIP traffic—today. Finally, we identify several independent sources of legal authority for the Commission to adopt comprehensive intercarrier compensation reform for all traffic transiting the PSTN, including traffic currently classified as intrastate access traffic.

In Part II, we discuss state carrier-of-last-resort obligations and their federal counterpart, ETC obligations. We explain why these obligations are fundamentally incompatible with the Commission's broadband goals and explain how they should be modified so that they advance, rather than hinder, broadband deployment. Finally, we explain that, to the extent states do not eliminate these antiquated and discriminatory service obligations themselves, the Commission has authority to preempt them.

In Part III, we discuss the Commission's proposal to transition legacy universal service funding to a new mechanism designed to promote deployment of broadband and IP-enabled services. We discuss the end state for reform and outline the intermediate steps that the Commission should take on its way to that end state. Finally, we explain why the Commission

has ample authority to support broadband services with universal service funding, but why the Commission cannot compel providers to offer broadband services.

DISCUSSION

I. FUNDAMENTAL REFORM OF THE COLLAPSING INTERCARRIER COMPENSATION REGIME IS NECESSARY TO ACHIEVE THE COMMISSION'S BROADBAND GOALS.

The nation's communications providers are in the midst of a revolutionary transition from the circuit-switched networks of the past to the all-IP architecture of the future. That transition is well underway, but further progress is faltering on the outdated intercarrier compensation regime, which has been crumbling for more than a decade and each day becomes increasingly unstable. Indeed, the collapse of that system is *inevitable*, regardless of what actions the Commission takes in this proceeding. The only question is whether the Commission will provide for an orderly transition from the public switched telephone network ("PSTN") and plain-old telephone service ("POTS") to broadband and IP-enabled communications, or whether it will cling to legacy mechanisms that are unsuited to that world and impede the transition to it.

Below, AT&T proposes a framework for comprehensive intercarrier compensation reform. Under that framework, intercarrier charges on the PSTN will be reduced and eventually eliminated, as will the subsidies implicit in those charges. To ensure that providers have the resources they need to deploy broadband and IP-enabled services, the proposed framework establishes a reasonable timetable for reform and provides mechanisms—including modest increases in certain end-user charges and explicit universal service funding—that give carriers an opportunity to recover some of their lost revenues. Most importantly, the framework provides a glide path to an all-IP end state where government regulation of intercarrier compensation is a thing of the past and all exchanges of traffic are governed by market forces rather than inefficient regulatory mandates.

A. The Intercarrier Compensation Regime Is an Unsustainable Relic of the Past and Is Hindering the Transition to the All-IP Network of the Future.

The intercarrier compensation regime is a regulatory relic that is no longer capable of promoting universal service, and, indeed, is harming competition in today's fast-evolving marketplace. That regime is part of a collapsing patchwork of implicit subsidies that is being eroded by competition. It also relies on arbitrary regulatory distinctions that promote arbitrage and spawn countless disputes among carriers. And it is premised on assumptions about cost-causation that have proven inaccurate even with respect to legacy, circuit-switched phone calls and certainly have no application to IP-enabled communications. Unless the Commission reforms this outdated and increasingly inefficient system, it will continue to pose a significant obstacle to achievement of the Commission's broadband goals.

1. The Existing Regime Is Collapsing Due to Competitive Pressures and Regulatory Arbitrage.

Today's intercarrier compensation system originated as an important part of the "regulatory compact" between public-utility regulators and local exchange carriers.[2] Under that compact, regulators granted carriers an exclusive franchise and guaranteed them a reasonable rate of return on their investment. In exchange, the carriers agreed to serve all customers in their designated franchise areas, often at rates below the costs of providing service. Carriers subsidized these below-cost rates through a patchwork of implicit subsidies, including above-cost rates charged to urban and business customers and above-cost access charges imposed on long-distance providers. This system was instrumental in ensuring universal service for all

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[2] Sixth Report and Order, Report and Order, Eleventh Report and Order, *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Low-Volume Long Distance Users; Federal-State Joint Board on Universal Service*, 15 FCC Rcd 12962, 12971-72 ¶ 23 (2000), *aff'd in part, rev'd in part, & remanded in part, Texas Office of Pub. Util. Counsel v. FCC*, 265 F.3d 313 (5th Cir. 2001).

Americans, including those in high-cost areas.[3] But competition has made the existing regime unsustainable. Forced to charge above-cost rates to some customers in order to support below-cost rates to others, carriers are losing access *lines* to competitors at an astonishing rate.[4] In addition, carriers are losing access *minutes* as consumers increasingly turn from traditional, circuit-switched long-distance services to alternative communications technologies. Such competitive developments have dramatically reduced the revenues that carriers derive from access charges and have precipitated the collapse of the POTS business model.

These competitive pressures take a variety of forms. For example, cable companies offering "triple play" services have cut sharply into ILEC market share in many areas. Circuit-switched networks deployed primarily for voice service are rapidly yielding to packet-switched networks over which voice is just one of many applications, offered by many different over-the-top VoIP providers.[5] Wireless phone services are available to more than 99.6 percent of the

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[3] *See Qwest v. FCC*, 258 F.3d 1191, 1195-96 (10th Cir. 2001) ("*Qwest I*").

[4] *See* Comments of AT&T, Inc. on the Transition from the Legacy Circuit-Switched Network to Broadband, *International Comparison and Consumer Survey Requirements in the Broadband Data Improvement Act; A National Broadband Plan for Our Future; Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion*, GN Docket Nos. 09-47, 09-51, 09-137, at 9 (filed Dec. 21, 2009) ("*AT&T NBP #25 Comments*") ("Today, less than 20% of Americans rely exclusively on POTS for voice service.").

[5] *See, e.g.*, National Cable and Telecommunications Association, Industry Data, http://www.ncta.com/Statistics.aspx (reporting 23.5 million cable phone customers); Skype S.A, *SEC Amendment No. 2 To Form S-1 Registration Statement*, at 132 (filed on Mar. 4, 2011), http://www.sec.gov/Archives/edgar/data/1498209/000119312511056174/ds1a.htm#rom83085_12 (reporting that Skype has 663 million registered users, up from 474 million in 2009; Skype users made 207 billion minutes of voice and video calls using Skype; and 20% of the world's international long-distance calling minutes are estimated to be made with Skype, up from 13% in 2009); Vonage Holdings Corp., *SEC Form 10-K*, at 2 (filed Feb. 17, 2011), http://ir.vonage.com/secfiling.cfm?filingID=1193125-11-38059 (reporting approximately 2.4 million subscriber lines).

population, and approximately 90 percent of Americans subscribe to one.[6] More than 26 percent of U.S. households have "cut the cord" and abandoned wireline phone service altogether.[7]

As a result of these competitive pressures, incumbents are losing lines with astonishing speed—around 10% each year.[8] Over the past decade, ILECs have lost more than 40 percent of their lines.[9] And today, carriers are losing approximately 700,000 POTS lines *every month*.[10] Yet, due to the high fixed costs of providing POTS service, the costs that incumbents incur to maintain their facilities are declining far more slowly,[11] and thus every customer that abandons an incumbent raises the average cost per line of serving those customers that remain.[12] As incumbents lose more and more customers, they are increasingly left with only the high-cost

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[6] Fourteenth Report, *Implementation of Section 6002(b) of the Omnibus Budget Reconciliation Act of 1993; Annual Report and Analysis of Competitive Market Conditions with Respect to Mobile Wireless, Including Commercial Mobile Services*, 25 FCC Rcd 11407, 11449, 11505 ¶¶ 44, 155 (2010) ("*Fourteenth CMRS Competition Report*").

[7] Stephen J. Blumberg & Julian V. Luke, Division of Health Interview Statistics, National Center for Health Statistics, CDC, *Wireless Substitution: Early Release of Estimates from the National Health Interview Survey, January - June 2010*, at 1-2 (Dec. 21, 2010), http://www.cdc.gov/nchs/data/nhis/earlyrelease/wireless201012.pdf (putting the figure at 26.6 percent as of June 2010) ("CDC Study").

[8] Saul Hansell, *Will the Phone Industry Need a Bailout, Too?*, N.Y. Times, May 8, 2009, http://bits.blogs.nytimes.com/2009/05/08/will-the-phone-industry-need-a-bailout-too/. *See also* Comments of AT&T, Inc., *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, Notice of Inquiry Seeking to Refresh the Record Regarding the Issues Raised by the Tenth Circuit in the Qwest Decision*, WC Docket No. 05-337, CC Docket No. 96-45, at 2-3 (filed May 8, 2009) ("*AT&T 10th Cir. USF NOI Comments*"). AT&T's line-loss figures track this statistic—in the past year alone, more than one in ten residential customers dropped their traditional telephone service.

[9] *See* Attachment A to these Comments.

[10] *AT&T NBP #25 Comments* at 9 (citing Craig Moffett, *Bernstein Research, Weekend Media Blast: The Wireline Problem*, at 2 (May 15, 2009) ("*Moffett, Weekend Media Blast*")).

[11] The number of housing units nationwide has increased almost 13 percent over the last decade. *See* Attachment A to these Comments. And because ILECs generally have carrier-of-last-resort and ETC obligations that compel them to extend their POTS facilities to new housing units in high-cost areas, ILECs' costs of providing POTS service are actually *increasing* in many areas notwithstanding their loss of access lines. *Id.*

[12] Hansell, *Bailout*; *AT&T NBP #25 Comments* at 2; *Moffett, Weekend Media Blast* at 2.

customers that other providers find it uneconomic to serve—while at the same time, they are losing the low-cost customers whose associated revenues have provided the implicit subsidies on which incumbents have relied to fund the provision of service in high-cost areas.

And with each lost subscriber, incumbents lose not just retail revenues, but also the access-charge revenues associated with that subscriber's line. Compounding this problem, incumbents also confront a dramatic decline in access minutes even for those lines that they manage to retain.[13] Consumers are increasingly using wireless and VoIP services for their conversations,[14] or are relying on alternative means of communication—such as email, social networking sites, or text messaging—in place of voice services. As a result of these combined pressures, ILECs have lost almost *47 percent* of their interstate switched access minutes over the past decade.[15] And as access minutes and lines steadily disappear, incumbents are losing their second key source of implicit subsidy revenue. With an outdated product, falling revenues, and rising costs, incumbent wireline telephone companies face a "death spiral" that makes their POTS business model increasingly unsustainable.[16]

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[13] *See* FCC, Industry Analysis & Technology Division, Wireline Competition Bureau, *Trends in Telephone Service*, at Table 7.1, 10.1 (Sept. 2010), http://hraunfoss.fcc.gov/edocs_public/attachmatch/DOC-301823A1.pdf (showing a 14.15% decrease in aggregate interstate switched access minutes *per line* between 2000 and 2008. Calculation using ILEC interstate switched access minutes and ILEC access lines).

[14] CDC Study at 1, 4 (noting that, in addition to the 26.6 percent of customers who have "cut the cord," another 15.9 percent of households received all or almost all calls on wireless telephones despite having a landline).

[15] *See* Attachment A to these Comments.

[16] *See* Toon Van Beeck, *Dying Industries*, IBISworld, at 4 (Mar. 2011), http://www.ibisworld.com/Common/MediaCenter/Dying%20Industries.pdf (stating that the wired telecommunications industry is "close to 55% smaller than it was at its peak; with an additional decline of 37.1% expected in the next six years"); Phil Izzo, *Top 10 Dying Industries*, Wall St. J., Mar. 28, 2011, http://blogs.wsj.com/economics/2011/03/28/top-10-dying-industries/.

This steep decline in local exchange and access revenues is exacerbated by arbitrage schemes that exploit well-known flaws in the intercarrier compensation system. That system relies on arbitrary service-by-service distinctions that are ill-suited to today's communications marketplace. Identical functionalities are priced at radically different levels depending on the end points of the call (*e.g.*, intrastate vs. interstate, local vs. interexchange, intraLATA vs. interLATA, and intra-MTA vs. inter-MTA), or the type of communications provider originating or terminating the call (*e.g.*, wireline vs. mobile wireless).[17] These distinctions reflect defunct industry business models in which (1) different carriers provided different services based on geographic boundaries; and (2) different providers offered entirely distinct and non-competing services using different technologies. But in a world where competing service providers offer distance-agnostic bundles of communications services over competing platforms, such distinctions distort competition and investment while creating opportunities for regulatory arbitrage and outright fraud.

In recent years, such schemes have substantially reduced access revenues for many local exchange carriers.[18] And the transaction costs associated with identifying and eliminating such

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[17] *See, e.g.*, Letter from Robert W. Quinn, Jr., Senior Vice President, Federal Regulatory, AT&T, to Kevin Martin, Chairman, FCC, *Developing a Unified Intercarrier Compensation Regime; Federal-State Joint Board on Universal Service; High-Cost Universal Service Support; Intercarrier Compensation for ISP-Bound Traffic; Establishing Just and Reasonable Rates for Local Exchange Carriers*, CC Docket Nos. 01-92, 96-45; WC Docket Nos. 05-337, 99-68, 07-135, at 3 (July 17, 2008) ("*Quinn Benchmark Ex Parte*").

[18] *See, e.g.*, Notice of Proposed Rulemaking and Further Notice of Proposed Rulemaking, *Connect America Fund; A National Broadband Plan for Our Future, et al.*, WC Docket Nos. 10-90, 07-135, 05-337, 03-109, GN Docket No. 09-51, CC Docket Nos. 01-92, 96-45, FCC 11-13, ¶¶ 620-34 (rel. Feb. 9, 2011) ("*NPRM*") (discussing phantom traffic). Some LECs exploit arbitrage opportunities themselves, concocting elaborate schemes to increase the implicit subsidies they receive for terminating traffic. These include traffic-pumping schemes, under which carriers increase incoming traffic volumes to inefficiently high levels by hosting free chat lines, teleconferencing services, and the like. *See* Comments of AT&T, Inc., *Connect America Fund; A National Broadband Plan for Our Future; Establishing Just and Reasonable Rates for*

schemes have been enormous.[19] Carriers must expend substantial sums to root out arbitrage and fraud and to litigate the disputes that arise when such schemes are uncovered. And every dollar that is lost due to a decline in access charges or is spent to combat arbitrage or fraud is one less dollar that can be invested in upgrading and expanding the carrier's network to provide broadband and IP-enabled services.

In short, the legacy POTS business model is dying, and it is taking with it the complex patchwork of implicit subsidies on which local exchange carriers have relied to sustain and upgrade their networks and to provide affordable service in high-cost areas. These developments make it increasingly difficult for incumbents[20] to invest the capital necessary for upgrading their networks in rural and other high-cost areas to provide broadband and IP-enabled services.

2. The Existing Regime Rests on Flawed Assumptions About Cost Causation.

The existing regime is flawed not only in application (in that it uses obsolete distinctions susceptible to arbitrage), but also in its most fundamental assumptions about cost causation.

Today's regime relies largely on the "calling party's network pays," or "CPNP" principle. That principle assumes that the calling party is both the only cost-causer *and* the sole beneficiary of any given communication and that, accordingly, all costs of transporting the communication

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Local Exchange Carriers; High-Cost Universal Service Support; Developing an Unified Intercarrier Compensation Regime; Federal-State Joint Board on Universal Service; Lifeline and Link-Up, CC Docket Nos. 01-92, 96-45, GN Docket No. 09-51, WC Docket Nos. 10-90, 07-135, 05-337, 03-109, at 8-10 (filed Apr. 1, 2011).

[19] *See NPRM* ¶¶ 636-38 (discussing the expense caused by access stimulation schemes).

[20] This is particularly true for so-called "non-rural" carriers, which are subject to statewide averaging and, typically, price-cap regulation. By contrast, "rural" carriers, which actually serve fewer of the nation's rural and other high-cost lines than "non-rural" carriers, typically are subject to rate-of-return regulation in the interstate jurisdiction, and thus continue receiving federal universal service support for their interstate cost recovery irrespective of whether they lose a line (in that event, their per-line support goes up to ensure that they continue to earn their specified rate of return).

should be imposed on the caller's network (and indirectly on the caller).[21] These assumptions are incorrect.

Many of the costs associated with telecommunications traffic are caused by the decisions of called parties to make their numbers available to callers, to answer incoming calls, and to remain on the line. Indeed, the called party's responsibility for a share of those costs has never been clearer, now that widespread use of caller ID permits end users to screen all calls and the national do-not-call registry has enabled them to declare their phone numbers off-limits to unwanted telemarketers.[22] Likewise, since a completed call involves parties at both ends, it is incorrect to view the caller as the sole beneficiary of a call. While no regime can always capture the precise proportion of costs and benefits attributable to each call participant, it clearly is not the case, as the current CPNP regime assumes, that the calling party is solely responsible for causing 100% of the costs of all calls and derives 100% of the benefits.[23]

Moreover, the existing intercarrier compensation regime relies on a per-minute rate structure that does not track the manner in which carriers actually incur costs. The intercarrier charges imposed under the current system irrationally permit terminating carriers to recover their average network costs, many of which are *non-traffic-sensitive*, from other carriers through

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[21] *See, e.g.*, Notice of Proposed Rulemaking, *Developing a Unified Intercarrier Compensation Regime*, 16 FCC Rcd 9610, 9619 ¶ 19 & n.36 (2001) (noting widespread assumption that the calling party is the sole cost causer of the call); *id.* at 9624-25 ¶ 37 (explaining that "CPNP regimes may be viewed as implicitly embracing the premise that the originating caller receives all the benefits of a call and should, therefore, bear the costs of both origination and termination").

[22] *See* Report and Order, *Rules and Regulations Implementing the Telephone Consumer Protection Act of 1991*, 18 FCC Rcd 14014, 14017 ¶ 1 (2003). Similarly, consumers may choose to have an unlisted number to avoid unwanted calls.

[23] As discussed below in Section I.B.1, the market-driven approach to interprovider compensation used on the Internet today is a far more efficient means of apportioning the costs and benefits of a communication than the existing CPNP regime.

predominantly *traffic-sensitive* usage charges. The result is a mismatch between the way costs are incurred and the way they are recovered, with predictably inefficient consequences.[24] In particular, the per-minute recovery of average costs gives each carrier artificial incentives to terminate as many minutes as possible, because by hypothesis the average network costs on which per-minute revenues are based generally exceed the incremental costs to the carrier of using its network for each additional minute. *Id.*

In sum, the existing intercarrier compensation regime relies on a set of faulty assumptions and is collapsing in the face of competition. Accordingly, it is no longer appropriate even for the circuit-switched PSTN of yesterday. The Commission's failure to reform this antiquated system is already hindering the deployment of broadband and the provision of IP-enabled services. And the Commission would do even greater harm if it were to import the inefficiencies of the existing regime into the all-IP world of the future. Instead, the Commission should provide for an orderly transition to a market-driven system of interprovider agreements. It is to a discussion of that issue that we now turn.

B. The Commission Should Facilitate a Prompt Transition to a Free-Market End State for Intercarrier Compensation and Interconnection.

The ultimate goal of this proceeding should be to facilitate a smooth transition from the existing, highly regulated framework for intercarrier compensation and interconnection to the minimally regulated, market-oriented framework that has always governed traffic exchanges on the Internet. To that end, the Commission should clearly articulate what the end state will look

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[24] Reply Comments of AT&T Inc., *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service; Lifeline and Link Up; Universal Service Contribution Methodology; Numbering Resource Optimization; Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Developing a Unified Intercarrier Compensation Regime; Intercarrier Compensation of ISP-Board Traffic; IP-Enabled Services*, WC Docket Nos. 05-337, 03-109, 06-122, 04-36, CC Docket Nos. 96-45, 99-200, 96-98, 01-92, 99-68, at 12 (filed Dec. 22, 2008) ("*AT&T December 2008 IC/USF Reply Comments*").

like and acknowledge that what is needed is not merely *reform* of existing mechanisms, but *elimination* of those mechanisms altogether. In addition, the Commission should establish a rational framework for transitioning to that end state, including a glide path for eliminating the per-minute charges that apply to traffic exchanged on the PSTN today, while ensuring that carriers have an opportunity for adequate cost recovery during the transition. By articulating both a rational end state and a clear path for getting there, the Commission can hasten, rather than hinder, the transition to the broadband, all-IP network of the future.

1. Interconnection and Interprovider Compensation Are Functioning Extraordinarily Well on the Internet Without Regulation.

On the Internet, interconnection and interprovider compensation have never been governed by prescriptive regulatory mandates. Instead, market forces alone, in the form of negotiated contracts between IP networks, have always produced the efficient exchange of IP communications through a diverse mix of indirect (and, occasionally, direct) interconnection arrangements. The result is the dynamic and explosively successful modern Internet. Those same market forces will continue functioning with equal efficiency as all voice communications move to IP networks and ultimately merge into the data streams exchanged under those existing arrangements.

Unlike on the PSTN, the default method of interconnection on the Internet is *indirect* interconnection. No IP network is required to interconnect with any other,[25] and any two networks on the Internet are far less likely to interconnect directly than indirectly, through "transit" arrangements. Under these arrangements, Network X pays Network Y (a transit provider) to arrange delivery of Network X's packets *to* any destination on the Internet and to

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[25] *See* Michael Kende, *The Digital Handshake: Connecting Internet Backbones*, FCC, Office of Plans and Policy, OPP Working Paper No. 32, at 2 (Sept. 2000), http://www.fcc.gov/Bureaus/OPP/working_papers/oppwp32.pdf ("*Digital Handshake*").

accept delivery of packets destined for Network X's customers *from* any location on the Internet. *Id.* at 7. Generally, Network X buys a robust, enterprise-class Internet access service from Network Y, which supplies the interconnection facilities to the remainder of the Internet. Rates for transit service are not tariffed, but instead are freely negotiated between Network X and Network Y in a robustly competitive marketplace.[26]

Direct interconnection, or "peering" arrangements, occur only when the direct exchange of traffic is mutually beneficial to both IP networks. *Digital Handshake* at 8. Under these arrangements, each network interconnects for the purpose of exchanging packets to be delivered to the other network's end users. Where such direct exchanges of traffic are not mutually beneficial, the parties may enter into a *paid peering* arrangement. Under paid peering, the networks still exchange traffic through high-capacity peering links, but the "non-compliant" network makes payments to the other network. Again, these direct-interconnection arrangements are the exception rather than the rule, as nearly all IP networks use transit providers to deliver traffic to, and receive traffic from, the rest of the Internet.

The diversity of these arrangements stands as a testament to the inherent adaptability and creativity of the Internet ecosystem in addressing interconnection and interprovider compensation issues. A traffic imbalance between two providers, for example, does not result in blocking or disconnection, but rather leads providers to freely negotiate one of the arrangements described above where payments are exchanged to ensure equity in the services each performs. Similarly, if a provider desires a certain quality of service across networks—for VoIP or other

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[26] William B. Norton, DrPeering White Paper, *Internet Transit Prices—Historical and Projected* (Aug. 2010), http://drpeering.net/white-papers/Internet-Transit-Pricing-Historical-And-Projected.php.

types of traffic for which QoS is important—that too can be negotiated under the existing regime.[27]

This type of flexible bilateral cooperation is how the Internet has managed to absorb an exponential growth in traffic over the last few years, and to accommodate the quality-of-service demands of that traffic (*e.g.*, VoIP, video) without any impasse resulting in the "cutting off" of a content or network provider. And as the Internet and the demands of users continue to evolve, so too will the agreements between network providers—because, at the end of the day, they all share a simple goal: ensuring that users can access the content of their choice from *any* point on the Internet. *See, e.g.*, *Digital Handshake* at 3-4 (describing the network externalities that providers enjoy from ensuring universal access to users and content). In short, in this unregulated environment, the market for transit and peering functions with great efficiency.

One of the key reasons for that efficiency is that no Internet service provider has a "terminating access monopoly" to its end users, and thus each has every incentive to reach commercially reasonable agreements with other network operators. This stands in stark contrast to the PSTN, where government-mandated interconnection and tariffing requirements have enabled local exchange carriers to insist on excessive intercarrier charges even in competitive markets. Some parties nonetheless invoke the concept of a terminating access monopoly when urging the Commission to begin regulating Internet transit and peering arrangements.[28] But the PSTN-oriented examples that they cite as evidence of a terminating access monopoly were

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[27] *See* Comments of AT&T Inc., *Preserving the Open Internet; Broadband Industry Practices*, GN Docket No. 09-191, WC Docket No. 07-52, at 51-56 (filed Jan. 14, 2010) ("*AT&T Net Neutrality Comments*") (describing methods that AT&T uses to ensure a specific quality of service for certain traffic).

[28] *See, e.g.*, Letter from Paul Kouroupas, Global Crossing, to Marlene Dortch, Secretary, FCC, *Preserving the Open Internet*, GN Docket No. 09-191, at 2 (Feb. 4, 2011); Letter from John M. Ryan, Level 3, to Chairman Julius Genachowski, FCC, *Preserving the Open Internet*, GN Docket No. 09-191, at 1-2 (Feb 16, 2011).

failures not of the *market*, but of *regulation* itself, and they never would have arisen in the absence of government-mandated interconnection and intercarrier compensation obligations. Because the *NPRM* itself invokes this same "terminating monopoly" concept (at ¶ 524) in discussing the future of intercarrier compensation, it is important to clarify where that concept does and does not apply.

Consider, for example, the so-called "CLEC access charge" controversy of ten years ago, the poster child of "terminating monopoly" abuses.[29] Before the Commission intervened in 2001, a CLEC could charge any long-distance carrier radically inflated rates for terminating access traffic. But it had that power not because of any market failure, but because the Commission had enacted rules that (i) compelled interexchange carriers ("IXCs") to interconnect with any CLEC and hand off all terminating traffic bound for that CLEC's customers; (ii) entitled the CLEC to tariff its termination rates unilaterally; and (iii) required those IXCs to pay the tariffed termination rates in the process, no matter how objectionably high they might be.[30] In addition, Title II rules precluded these IXCs not only from sending the bill to the called parties (*i.e.*, to the CLEC's end users), but also from passing the inflated termination charges through to the specific calling parties who placed these particular calls.[31] The net result of these Title II regulations was to make the CLECs' subscribers completely indifferent to the level of these termination charges, and thus to preclude any market response to them.

The Commission corrected this problem—which it correctly traced to "use of the regulatory process"—by "mandatorily detariff[ing]" CLEC access rates above certain levels and

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29 *See* Seventh Report and Order and Further Notice of Proposed Rulemaking, *Access Charge Reform; Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, 16 FCC Rcd 9923 (2001) ("*CLEC Access Charge Order*").

30 *See id.* at 9924-25 ¶ 2.

31 *See* 47 U.S.C. § 254(g).

forcing CLECs to "*negotiate* [any] higher rates with the IXCs."[32] And it thereby subjected those rates, for the first time, to the discipline of market forces. The Commission took similar steps to fix the flawed "ISP reciprocal compensation" regime, which allowed a CLEC serving dial-up ISPs to force ILECs (whose customers "called" those ISPs) to interconnect and pay inflated "reciprocal compensation" rates set by state commissions[33]—but only because regulation compelled the ILECs to hand off the calls to the CLEC and pay those rates.

The Commission has *never* found any "terminating access monopoly" in the *absence* of Title II interconnection and compensation obligations. And no such "monopoly" can be found anywhere on the Internet today, which has prospered entirely without interconnection obligations. If broadband Internet service providers had a "terminating monopoly," one would expect to see them charging Internet backbone providers high rates for terminating traffic to their subscribers. In fact, however, most broadband ISPs either have some combination of settlement-free peering arrangements and transit arrangements with backbone providers for connectivity to the broader Internet.[34] This is no surprise because, for reasons relating to the basic structure of

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[32] *CLEC Access Charge Order*, 16 FCC Rcd at 9924-25 ¶¶ 2, 3 (emphasis added). The wireless industry provides an instructive contrast. Because wireless carriers have no right to tariff access charges, they have no means of forcing other carriers to pay terminating access fees, as the Commission's *Sprint PCS Order* made clear almost nine years ago. *See* Declaratory Ruling, *Petitions of Sprint PCS and AT&T Corp. for Declaratory Ruling Regarding CMRS Access Charges*, 17 FCC Rcd 13192 (2002) ("*Sprint PCS Order*"), *appeal dismissed sub nom. AT&T Corp. v. FCC*, 349 F.3d 692 (D.C. Cir. 2003). Since then, no wireless provider has seriously tried to unilaterally impose access charges on another carrier; instead, they almost always terminate traffic without charge.

[33] *See* Order on Remand and Report and Order, *Intercarrier Compensation for ISP-Bound Traffic*, 16 FCC Rcd 9151 (2001) ("*ISP Remand Order*"), *remanded but not vacated by WorldCom, Inc. v. FCC*, 288 F.3d 429 (D.C. Cir. 2002); *see also* Order on Remand and Report and Order and Further Notice of Proposed Rulemaking, *High-Cost Universal Service Support* (and related dockets), 24 FCC Rcd 6475 (2008) ("*2008 IC/USF Order and FNPRM*").

[34] *See* P. Faratin *et al*., *Complexity of Internet Interconnections: Technology, Incentives and Implications for Policy*, at 9-11 (Sept. 2007), http://people.csail.mit.edu/wlehr/Lehr-

Internet traffic exchanges, broadband ISPs cannot force backbone networks to interconnect to exchange traffic (in the way that ILECs can force interexchange carriers to exchange traffic on the PSTN today), but rather must negotiate with other network providers (including backbone providers) to ensure that their customers can reach all points on the Internet. Thus, broadband ISPs typically have little bargaining leverage in negotiating the terms of interconnection with backbone networks.

As discussed above, the distributed and packet-switched nature of the Internet makes *indirect* interconnection—through intermediate transit links—the rule for Internet traffic, whereas *direct* interconnection between the calling and called parties' networks is the norm (subject to some exceptions) on the circuit-switched PSTN.[35] That attribute of the Internet is competitively significant because indirect interconnection provides many competitive options that discipline the price that market participants can charge for direct interconnection.

Suppose, for example, that an IP network seeks a direct peering relationship with a broadband ISP in order to deliver data traffic to the latter's customers. If the traffic between the two networks is grossly imbalanced, the ISP may try to condition any direct peering arrangement on the payment of compensation. But if it demands too high a price, the IP network can simply balk, because it has many alternatives for delivering its traffic to the ISP's customers. For example, it could do what IP networks have done for two decades: it could reach end users by

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Papers_files/Clark%20Lehr%20Faratin%20Complexity%20Interconnection%20TPRC%202007.pdf.

[35] This is as true of "three carrier" long-distance calls (for the diminishing class of customers that have different local and long-distance carriers) as of all other calls on the PSTN. In the "three carrier" context, the "calling party's network" is the long-distance provider, with whom the calling party has a direct commercial relationship, and that network typically relies on direct interconnection with the called party's local network to terminate the call.

purchasing intermediate transit services from one of many third-party backbone providers.[36] And that third-party backbone provider may in turn be either (1) a settlement-free peer of the ISP—in which case the ISP would receive no compensation for terminating the traffic—or (2) the ISP's *own* transit provider as well, in which case the ISP may end up *paying* to terminate the traffic.[37] Either way, the ISP would be worse off than if it had agreed to reasonable terms for direct peering. The availability of transit (indirect interconnection) as an alternative to paid peering (direct interconnection) will thus generally keep the price of paid peering below the price of transit. And that is a powerful competitive check: because the transit market is highly competitive, the price of transit has been plummeting for a dozen years straight.[38]

Finally, there is also no counterpart to Section 254(g) on the Internet. If, for example, a broadband ISP somehow succeeded in overcharging another IP network for paid peering, that IP network could pass through the charges to its content-provider customers—who in turn could pass them through to the *broadband ISP's own customers* as the price of receiving the content in question so long as they continue subscribing to that ISP. That dynamic would discipline paid peering rates even if third-party transit were *not* a competitive alternative for the IP network.

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36 *See* Faratin, *Incentives and Implications*, *supra*, at 8-11.

37 Peyman Faratin *et al*., *The Growing Complexity of Internet Interconnection*, 72 Communications & Strategies 51, 63 (4Q 2008) (explaining that if one network denies settlement-free peering privileges to others, those other networks, "if they can control the routing of their traffic," can "cause their traffic to/from the prospective peer to route over the peer's transit connection to raise the peer's transit costs in order to induce it to peer"); Rudolph van der Berg, *How the 'Net works: an introduction to peering and transit*, Ars Technica (Sept. 2, 2008), http://arstechnica.com/old/content/2008/09/peering-and-transit.ars ("Allegedly, a big American software company was refused peering by one of the incumbent telco networks in the north of Europe. The American firm reacted by finding the most expensive transit route for that telco and then routing its own traffic to Europe over that link. Within a couple of months, the European CFO was asking why the company was paying out so much for transit. Soon afterward, there was a peering arrangement between the two networks.").

38 *See* page 25, *infra* (discussing the steep decline in prices for transit services).

These theoretical considerations merely confirm what practical observation confirms: the transit and peering marketplace has functioned efficiently for many years in spite of—and perhaps because of—a complete lack of regulatory interconnection and interprovider compensation obligations. As the circuit-switched PSTN sunsets, so too will the need for interconnection and intercarrier compensation rules. Indeed, as discussed in the next Section, imposing such rules on IP networks would merely subject the Internet to a hornet's nest of intractable regulatory controversies similar to those that have roiled the PSTN for thirty years.

2. As Voice Traffic Increasingly Migrates to IP Networks, Interconnection and Interprovider Compensation on Those Networks Should Continue to Be Governed by Market Forces.

The Commission states that it "may make little sense for providers to maintain different interconnection arrangements for the exchange of VoIP and other forms of Internet traffic," *NPRM* ¶ 679, and AT&T agrees. In fact, such a bifurcated regime would make *no sense at all*.

The transition of telephony from circuit-switched time-division multiplexing ("TDM") technologies to IP will not change the nature of the Internet marketplace. A growth in IP voice traffic will not produce a dramatic increase in network demands,[39] and to the extent that any change in traffic patterns occurs, IP network operators already have both the appropriate incentives and the necessary tools to ensure that all traffic is delivered efficiently. And as the marketplace shifts from POTS to VoIP, there simply will be no need for the Commission to displace efficient market forces with prescriptive rules. To the contrary, the Internet ecosystem has successfully facilitated the transmission of *millions* of VoIP-to-VoIP calls, and there will be

[39] Although voice IP applications require specialized attention from carriers to ensure the maintenance of proper latency thresholds, the marginal demands on carriers from an increase in such traffic would not be substantial. To the contrary, the evidence demonstrates that the rapid rise of streaming video services has posed (and is posing) a much greater challenge, yet the industry has performed admirably in meeting that demand. *See AT&T Net Neutrality Comments* at 183.

no greater need to regulate such arrangements once *all* voice communications migrate from the PSTN to IP networks.

Rules regarding interconnection and interprovider compensation for VoIP services are unnecessary because the marketplace for transit and peering services is robustly healthy. The larger backbones "compete for the transit business of smaller backbones in order to increase their revenues."[40] This competition has driven transit prices down significantly over the last decade, from approximately $1200/Mbps in 1998 to less than $12/Mbps in 2008 and less than $3/Mbps in 2009.[41] Indeed, the Commission recently reaffirmed that the Internet backbone market remains competitive and efficient, and that any given backbone has little incentive or ability to engage in anticompetitive conduct.[42]

Granted, it is conceivable that disputes could eventually arise concerning interconnection and interprovider compensation in the Internet ecosystem. But any such problems can, and should, be addressed through targeted *ex post* measures. The Commission should not adopt *ex ante* regulations in an effort to resolve hypothetical problems that may never arise. Such measures would do more harm than good by undermining the efficiency of the existing regime and, even worse, could lead to the same type of market distortions—and accompanying disputes—that afflict the PSTN.

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40 *See Digital Handshake* at 20.

41 *See* DrPeering, *Why care about Transit Pricing?*, http://drpeering.net/AskDrPeering/blog/articles/Peering_vs_Transit___The_Business_Case_for_Peering.html; DrPeering, *Transit Prices Race to the Bottom*, http://drpeering.net/AskDrPeering/blog/articles/Ask_DrPeering/Entries/2009/4/28_Transit_Prices_Race_to_the_Bottom.html.

42 Memorandum Opinion and Order, *AT&T Inc. and BellSouth Corp. Application for Transfer of Control*, 22 FCC Rcd 5662, 5736-38 ¶¶ 144-49 (2007); Memorandum Opinion and Order, *SBC Communications Inc. and AT&T Corp. Applications for Approval of Transfer of Control*, 20 FCC Rcd 18290, 18354-66 ¶¶ 116-39 (2005) ("*SBC-AT&T Merger Order*").

3. The Commission Should Establish a Minimally Regulatory End State for VoIP Communications.

To hasten the transition from the PSTN to an all-IP end state, the Commission should establish a date certain for completion of that transition.[43] Further, to ensure that legacy regulatory obligations do not needlessly delay the transition, the Commission should make clear that, after that date, providers will no longer be required to provide legacy, TDM-based telecommunications services or to comply with the myriad common-carrier regulations applicable to those legacy services.[44]

As AT&T has detailed many times before, the broadband marketplace is robustly competitive.[45] In this environment, common-carrier regulation of VoIP services is not just unnecessary, but would be affirmatively harmful. The costs of such regulation are substantial, as the Commission has recognized. Tariffs, for one, inhibit competition because they make it difficult for firms to "bargain with their customers over rates or to adjust them quickly to market conditions."[46] As the Commission has explained, tariffs in a competitive market frequently result in "regulated competition … too often becom[ing] cartel management." *Id.* at 454 ¶ 26.

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[43] *See AT&T NBP #25 Comments* at 14-16.

[44] Following the transition, some providers may choose to continue providing TDM-based services, and to interconnect in TDM, but no provider should be *obligated* to do so. Instead, the terms of such interconnection should be governed solely by commercial negotiations.

[45] AT&T has described the competitive nature of the broadband Internet access marketplace on many occasions. Rather than repeat that discussion again here, we incorporate by reference our prior filings on this topic. *See, e.g.*, Comments of AT&T Inc., *A National Broadband Plan for Our Future*, GN Docket No. 09-51, at 100-02, 108-09, 115-19, 128-31 (filed June 8, 2009) ("*AT&T National Broadband Plan Comments*"); *AT&T Net Neutrality Comments* at 5-6, 78-87, 145-56; Comments of AT&T Inc., *Fostering Innovation and Investment in the Wireless Communications Market; A National Broadband Plan for Our Future*, GN Docket Nos. 09-157 & 09-51, at 12-52 (filed Sept. 30, 2009).

[46] Further Notice of Proposed Rulemaking, *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor*, 84 FCC 2d 445, 454 ¶ 24 (1981) ("*Competitive Carrier Further Notice*").

The Commission also has found that *eliminating* tariffs "increase[s] carriers' incentive to reduce prices … and reduce[s] their ability to engage in tacit price coordination."[47]

Price regulation, another hallmark of common-carrier regulation, would also be counterproductive in the context of IP communications. Other firms in this competitive market will discipline the rates charged, and regulatory intervention would only interfere with competitive firms' "ability to price and diversify their services as the market dictates."[48] Likewise, entry regulation harms new competitors by requiring them to "declare their strategies before entry, thus reducing any time-related advantages that a new firm would have over existing firms." *Competitive Carrier Further Notice*, 84 FCC 2d at 455 ¶ 30. Similarly, exit regulations harm competition by discouraging carriers from "entering high risk markets for fear that they may not be able to discontinue service in a reasonably short period of time if [the venture] proves unprofitable." *Competitive Carrier First R&O*, 85 FCC 2d at *34 ¶ 147.

By the end of the transition, such common-carrier regulation should be a thing of the past, and providers should be free to offer minimally regulated broadband information services over which voice is just one of many applications. Such a regime is consistent with the Commission's well-established position that "broadband services should exist in a minimal regulatory environment that promotes investment and innovation in a competitive market."[49]

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[47] Second Report and Order, *Policy and Rules Concerning the Interstate, Interexchange Marketplace*, 11 FCC Rcd 20730, 20752 ¶ 41 (1996). *See also Competitive Carrier Further Notice*, 84 FCC 2d at 454 ¶ 26 (describing how a tariffing requirement for non-dominant carriers "provides an excellent mechanism for inducing noncompetitive pricing" because it allows competitors to easily match prices and thereby reduces the incentive for providers to lower prices in the first place).

[48] *Competitive Carrier Further Notice*, 84 FCC 2d at 455 ¶ 30; First Report and Order, *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor*, 85 FCC 2d 1, *22 ¶ 95 (1980) ("*Competitive Carrier First R&O*").

[49] *See, e.g.*, Declaratory Ruling, *Inquiry Concerning High-Speed Access to the Internet over Cable and Other Facilities*, 17 FCC Rcd 4798, 4802 ¶ 5 (2002) ("*Cable Modem Order*")

Indeed, in the context of the Title II reclassification proceeding, the Commission made clear that it would likely forbear from most common-carrier regulation *even if broadband were classified as a Title II service*.[50] There is no reason why the regulatory scheme should be materially different for VoIP traffic than for all other Internet traffic.[51] Instead, the Commission should apply only those regulatory obligations that are necessary to protect public safety and achieve other important public-interest objectives, such as CALEA, E-911, number portability, and access for persons with disabilities.

Importantly, it is essential that the Commission not apply common-carrier regulation to some providers but not others. In particular, *all voice communications* over IP should receive the

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(citation omitted). *See also* Report and Order, *Appropriate Framework for Broadband Access to the Internet over Wireline Facilities*, 20 FCC Rcd 14853, 14855 ¶ 1 (2005) ("*Wireline Broadband Order*"); Declaratory Ruling, *Appropriate Regulatory Treatment for Broadband Access to the Internet over Wireless Networks*, 22 FCC Rcd 5901, 5901-02, 5908-14 ¶¶ 2, 18-34 (2007) ("*Wireless Broadband Order*") (adopting a "a minimal regulatory environment for wireless broadband Internet access service that promotes our goal of ubiquitous availability of broadband to all Americans").

[50] *See* Notice of Inquiry, *Framework for Broadband Internet Service*, 25 FCC Rcd 7866, 7897 ¶ 74 (2010) ("The forbearance option contemplates a determination not to apply all but the small number of provisions of Title II that provide a solid legal foundation for the Commission to implement its established broadband policies."); Austin Schlick, General Counsel, FCC, *A Third-Way Legal Framework for Addressing the Comcast Dilemma*, May 6, 2010, http://www.broadband.gov/third-way-legal-framework-for-addressing-the-comcast-dilemma.html ("[T]here is a third legal path that fits better with the Commission's settled, deregulatory policy framework for broadband communications services …. Specifically, the Commission could implement the consensus policy approach—and maintain substantively the same legal framework as under Title I—by forbearing from applying the vast majority of Title II's 48 provisions to broadband access services."); Julius Genachowski, Chairman, FCC, *The Third Way: A Narrowly Tailored Broadband Framework*, May 6, 2010, http://www.broadband.gov/the-third-way-narrowly-tailored-broadband-framework-chairman-julius-genachowski.html (noting that the third-way "approach has important virtues").

[51] *See* Memorandum Opinion and Order, *Vonage Holdings Corp. Petition for Declaratory Ruling Concerning an Order of the Minn. Pub. Utils. Comm'n*, 19 FCC Rcd 22404, 22417-18 ¶ 21 & n.78 (2004) ("*Vonage Order*"), *aff'd Minn. Pub. Utils. Comm'n v. FCC*, 483 F.3d 570 (8th Cir. 2007) (noting the FCC's "long-standing national policy of nonregulation of information services" and its unwillingness to apply "public-utility type" regulations to such services).

same regulatory treatment, regardless of whether they are offered by wireline broadband providers, wireless providers, or non-facilities-based providers.[52] An approach that distinguishes among providers—or even worse, imports distinctions made in the legacy PSTN context—would create new opportunities for arbitrage and create substantial competitive distortions. Market forces, and not regulators, are the best arbiters of which services should succeed or fail in a competitive marketplace. The Commission should not intervene in this process and risk encouraging an inefficient provider or discouraging an efficient one. In either case, the Commission's involvement would certainly lead to costly disputes similar to those that plague the PSTN today.

Of course, the Commission's efforts to maintain the existing minimally regulatory environment for IP communications will be thwarted if the states can impose common-carrier regulation of their own. As voice traffic increasingly migrates from the PSTN to the Internet, the model of overlapping (and sometimes competing) federal and state jurisdiction must give way to a regime of coherent federal regulation that is consistent with the any-distance nature of IP communications. That is as true of fixed VoIP services as of nomadic VoIP, and the Commission should conclude in this proceeding that *all* VoIP services are information services over which the Commission has exclusive jurisdiction.[53] Recognition of that principle, now, is

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[52] The Commission has explicitly endorsed the principle of functionally equivalent services receiving identical regulatory treatment by state commissions, and there is no reason why the Commission should not apply the same standard to itself. *See Wireless Broadband Order*, 22 FCC Rcd at 5923 ¶ 64 ("Under 332(c)(7), state or local governments may not unreasonably discriminate among providers of functionally equivalent services and shall not prohibit or have the effect of prohibiting the provision of personal wireless services.").

[53] AT&T has advocated this approach in several prior pleadings, which it incorporates by reference here. *See, e.g.*, *AT&T NBP #25 Comments* at 18-19; Letter from Robert W. Quinn, Jr., Senior Vice President, Federal Regulatory, AT&T, to Kevin Martin, Chairman, FCC, CC Docket No. 96-45, WC Docket Nos. 04-36, 06-122, at 3 (filed July 17, 2008) ("*Quinn VoIP Ex Parte*"). Indeed, even if the Commission concludes—erroneously, in AT&T's view—that some forms of

critical to establishing a proper understanding of the respective roles of the Commission and the states as the industry transitions to broadband and retires the PSTN.

4. The Commission Should Establish a Framework for a Prompt but Orderly Transition to the Minimally Regulatory End State.

Comprehensive reform of the intercarrier compensation regime cannot happen overnight. Instead, the Commission should establish a clear glide path that enables providers to make a prompt but orderly transition to that end state.

In the paragraphs below, AT&T proposes a specific framework for the transition. Under that framework, intrastate and interstate access charges will be unified,[54] then ratcheted down and harmonized with all other intercarrier charges, and ultimately eliminated altogether. The proposed framework also offers opportunities (but provides no guarantees) for carriers to recover their lost revenues through gradual increases to certain, artificially low end-user charges, subject to caps and competitive pressures. Finally, the framework also provides for a new explicit universal service mechanism designed to help mitigate carriers' loss of cross-subsidies implicit in access charges.

Reduction and elimination of intercarrier charges. AT&T proposes that the Commission establish a framework under which originating and terminating access charges (both inter- and intrastate) would be (i) unified and then phased down in equal steps over a period of four years, (ii) harmonized with other intercarrier charges, and (iii) eliminated

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VoIP should be classified as telecommunications services, the Commission should reaffirm its conclusion in the *Vonage Order* that the nature of VoIP service—whether nomadic or fixed—renders state regulation inappropriate. *See Vonage Order*, 19 FCC Rcd at 22420 ¶ 25 n.93.

[54] As discussed below in Section I.C, *infra*, the Commission has authority to use the tools provided in sections 251 and 252 of the Act to reduce all intercarrier rates, including those for intrastate services. Indeed, such action is necessary to ensure that the states do not impede the transition to all-IP networks by maintaining inconsistent intercarrier compensation obligations.

altogether once the existing high-cost universal service mechanisms are replaced by the CAF.

Specifically:

- On January 1, 2012, intrastate access charges will be reduced to the level of interstate access charges. If a carrier's reciprocal compensation charges exceed its interstate access charges, the former will be reduced to the level of the latter at this step, and both will be phased down in accordance with the access-charge schedule outlined immediately below.[55]

- On January 1 of the succeeding four years (that is, 2013, 2014, 2015, and 2016), access charges will be reduced in equal steps until, in 2016, they are harmonized with all other intercarrier compensation charges and reduced to a rate of $0.0007. During this transition, when a carrier's access charges reach the level of its reciprocal compensation charges, the two charges will be unified and reduced together in accordance with the schedule outlined above.

- On January 1, 2017, access rates will be fully detariffed, and all government-mandated intercarrier compensation obligations will be eliminated (*i.e.*, the default rule for intercarrier compensation on the PSTN will be bill and keep).[56] Providers will, however, remain free to negotiate interprovider payments as they do on the Internet today.[57]

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[55] As discussed below in Sections I.C.1 and I.C.2, all forms of intercarrier compensation will be removed from the section 251(g) carve-out and thus will be governed by section 251(b)(5).

[56] The "bill-and-keep" compensation methodology assumes a default point of interconnection ("POI") between two providers' networks that demarcates each provider's *financial* responsibility for carrying calls. And it specifies that if the providers interconnect at that point, neither party is obligated to compensate the other for transport and termination of traffic, but rather each is responsible for recovering its costs from its own end users. Thus, conceptually, a pure bill-and-keep regime establishes a transport and termination rate of zero for all traffic exchanged at the POI.

[57] This framework should apply only to transport and termination of traffic *from the POI* between two providers' networks, and to originating access. It should not apply to any transport services sold to, or self-provided by, a provider to bring traffic to the point of interconnection with another provider's network. While the rates for such transport services should be harmonized in recognition that all traffic (intrastate, interstate, and local) will be subject to the same default interconnection rules, there is no basis for prohibiting providers from charging other providers for transport to the POI. Each provider should be responsible for getting its traffic to the POI, and can self-provide, purchase from another provider, or purchase from the ILEC transport to reach the POI.

- On January 1, 2017, the regulatory superstructure applied to legacy *TDM*-based telecommunications services—including interconnection obligations, service obligations, tariffing, and unbundling—will also be eliminated.

Gradual increases in caps on end-user charges. To help mitigate the impact of these reductions in intercarrier payments, the Commission should gradually raise regulatory caps on interstate SLCs and on other end-user charges.[58] Importantly, increasing the caps on such charges would not guarantee that carriers could successfully *implement* the SLC increases that would be necessary to make them "whole" for reductions in intercarrier compensation. Instead, this regulatory flexibility would give carriers only an *opportunity* to do so—in many areas, competition will prevent carriers from increasing their interstate SLCs up to the new caps. Furthermore, as discussed below, carriers should be permitted to increase their interstate SLCs only *after* exercising any flexibility they have to replace their lost access revenues through increases in *intrastate* end-user charges. *See* pages 33-35, *infra* (discussing benchmark mechanism). If the carrier fails to take advantage of this flexibility, its SLC increases should be limited to the amount of recovery that the carrier would have been entitled to if it *had* exercised that flexibility. (That is, the amount of lost access revenues that the carrier is entitled to recover should be reduced "as if" the carrier exercised whatever flexibility it has at the state level.)

Explicit support to preserve universal service. The Commission also should provide targeted, explicit universal service support to mitigate the impact of reductions in access charges. Again, this funding should not be designed to replace all lost access revenues.[59] Instead, carriers

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[58] Increasing the caps on these end-user charges should help offset the elimination of IAS when a price-cap ILEC does not take CAF support.

[59] *See Quinn Benchmark Ex Parte* at 5 (targeted supplemental universal service support is necessary "to offset a portion of some carriers' reduced access revenues. Although the size of the fund must be controlled, such support is an essential backstop to ensure that end-user rates remain reasonably comparable during the transition from the narrow-band business model and universal service paradigm to the broadband world.").

should be required to turn first to increases in intrastate rates, then to interstate SLC increases, before turning to the "Access Recovery Mechanism," or "ARM."[60]

Benchmark mechanism.[61] The Commission should not permit carriers to recover the full amount of their lost access revenues from interstate sources alone. Rather, it should require providers to look to intrastate sources of recovery before increasing interstate SLCs or drawing support from the ARM. To implement this requirement in an even-handed manner across states, the Commission could implement the following benchmark mechanism.[62]

Specifically, the Commission could set a benchmark rate that it believes is reasonable for intrastate end-user rates. This benchmark could initially be set at a low level, such as $27, and rise gradually to a higher level, such as $30. Before turning to federal sources of revenue recovery, a provider would be expected to exercise whatever regulatory flexibility it has at the state level to raise its intrastate end-user charges to the benchmark level. That said, a provider would ***not actually be required to increase its intrastate rates***—indeed, competition might make it impossible for a carrier to do so. But that carrier's entitlement to recovery from *interstate* sources of revenue would be calculated "as if" the carrier did take advantage of state regulatory flexibility. In essence, if the carrier's intrastate end-user rates remained below the benchmark,

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[60] The amount of ARM funding available to a carrier should be based on that carrier's lost access revenues, not its costs, and should not take into account revenues other than lost intercarrier access revenues—at least for price-cap carriers. Price-cap carriers' access charges have been set for years without regard to cost, and (as the Commission recognizes) contain significant implicit subsidies. Indeed, that is why reform is needed in the first place. Consequently, it would make no sense to base a carrier's entitlement to ARM funding on that carrier's costs.

[61] It may be necessary to adopt a different approach to recovery of access-charge losses for rate-of-return carriers.

[62] AT&T has discussed this "benchmark" concept in prior pleadings. *See generally Quinn Benchmark Ex Parte.*

any amount between those rates and the benchmark would be deducted from the amount of access losses that the carrier could recover in the interstate jurisdiction.

If any access-charge losses remain after the carrier has increased its intrastate rates (or after it has forgone those rate increases and had them imputed against its access-charge losses), the carrier should be permitted to turn to interstate SLCs. The carrier should be allowed to increase its SLCs by the amount of its remaining access-charge losses, up to the cap. And those caps gradually would increase over time. Again, no carrier would be required to *actually* increase its SLCs, but its entitlement to ARM funding would be calculated "as if" it had done so.

Finally, only after a carrier has increased intrastate and interstate end-user charges (or had the amounts available from those sources imputed against it) should a carrier be entitled to turn to the ARM mechanism. That mechanism should enable a provider to recover all of its remaining access-charge losses.

To the extent the Commission is concerned about the size of rate increases in any given year, it could allow carriers to limit end-user recovery to a particular level, such as $3.00 per year. This limitation also would apply to the maximum amounts imputed to carriers in the "as if" calculation described above. Of course, if the Commission allows carriers to limit their end-user rate increases, it would need to allow carriers to recover from the ARM the difference between any such cap on end-user rates and the benchmark.

By adopting the access-recovery regime described above, the Commission can ensure that carriers have a reasonable opportunity to recover sufficient revenues to enable them to continue serving their customers, and to deploy broadband and IP-enabled services. At the same

time, the requirement that providers look to their end users for a significant portion of their lost access revenues will ensure that the size of the ARM is not excessive.[63]

No requirement to off-set end-user charges or ARM payments for access-cost reductions. In prior proceedings, some parties have argued that the Commission should create a mechanism to ensure that ILECs affiliated with long-distance or wireless carriers "off-set" any increase in end-user charges, or any payments from the ARM, by the amount of their affiliates' access-charge savings. Under one such proposal, an ILEC would be precluded from raising its SLCs to compensate for a loss of access revenues if it has a long-distance or wireless affiliate that enjoys a cost savings due to access-charge reform.[64] Under another, an ILEC would be required to reduce its recovery from the ARM to off-set its affiliates' access-charge savings. Adoption of such a proposal would be neither economically sensible nor administratively feasible.

The principal flaw in such proposals is that they assume that any wireless or long-distance company will "keep" the cost savings attributable to access-charge reductions and use them to increase its profits. That is incorrect. Long distance and wireless services are among the most fiercely competitive in the industry. Under elementary principles of economics, affiliates offering those services will thus be forced to pass through their intercarrier compensation savings *to their customers*, whether in the form of lower rates, accelerated investment in improved service quality, and/or wider deployment of innovative technology used to provide, for example,

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[63] The Commission should establish an additional transition period, *e.g.*, 3 years, to phase out the ARM.

[64] This proposal was attached as Appendix D to the Commission's *2008 IC/USF Order and FNPRM.*

next-generation broadband services.[65] Thus, barring an ILEC from raising its SLCs to competitive levels or from recovering lost access revenues through the ARM because of the supposed "savings" of its affiliates would leave the ILEC *much worse off* in the aggregate than before the transition, and also much worse off than stand-alone companies competing in the same markets. It also would deprive ILECs of the revenues and capital they need to meet their service obligations and invest in broadband during the transition to all-IP networks.

Further, an "off-set" mechanism assumes that ILEC customers, rather than long distance or wireless customers, should be the ones to benefit from reductions in access-charge costs. But there is no legitimate policy justification for that assumption. It makes no sense to require a company to redirect cost savings from one group of customers to a second group of customers, when they subscribe to entirely different services and, indeed, are located in different service territories. Essentially, such an off-set would amount to a *subsidy* running from long distance and wireless customers scattered across the country, to local exchange customers concentrated in those areas where the ILEC provides local exchange service. But such subsidies are directly contrary to the market-disciplined regime that the Commission is attempting to create, and, indeed, would simply replicate the implicit subsidies in access charges that are no longer tenable in today's hyper-competitive communications marketplace, and which the Commission rightly seeks to eliminate.

Moreover, implementing a regulatory mechanism to calculate the appropriate *amount* of any off-set would be extraordinarily complicated. At a minimum, the Commission would need

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[65] *See, e.g.*, Richard N. Clarke & Thomas J. Makarewicz, *Economic Benefits from Missoula Plan Reform of Intercarrier Compensation*, at 18-19 (Feb. 1, 2007), attached as Ex. 1 to Reply Comments of AT&T Inc. on the Missoula Plan for Intercarrier Compensation Reform, *Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92 (Feb. 1, 2007) (explaining why access-charge reductions will be passed on to customers).

to inspect the books of each affected wireless and long-distance company to calculate the cost savings that each company derives from reductions in access charges. And the Commission would then need to determine, based on that analysis, exactly how large of an off-set should be imposed in each of the ILEC's many service areas. Such an analysis would be a monumental undertaking.

Finally, it would make no sense to subject ILECs to differing regulatory treatment depending on their corporate relationships with non-dominant wireless and long-distance affiliates. To the contrary, such an approach could create perverse incentives for ILECs to structure their operations so as to avoid an "affiliate penalty." That makes no sense. Consumer welfare is maximized when ILECs structure their operations in the most efficient manner possible.[66] Thus, an off-set requirement would discourage efficiency, to the detriment of consumers, by imposing competitive burdens on ILECs and wireless carriers that elect to consolidate and by conferring competitive benefits on companies that choose to splinter into unrelated ILEC and wireless (or long-distance) entities.

C. The Commission Has Jurisdiction to Impose Comprehensive Intercarrier Compensation Reform.

The Commission has jurisdiction to mandate the intercarrier compensation reforms outlined above. Section 251(b)(5) encompasses—and section 201(b) thus authorizes the Commission to regulate—all classes of intercarrier compensation involving traffic that originates

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[66] *See, e.g.*, Memorandum Opinion and Order, *Applications of AT&T Wireless Services, Inc. and Cingular Wireless Corporation for Consent to Transfer Control of Licenses and Authorizations*, 19 FCC Rcd 21522, 21599-611 ¶¶ 201-36 (2004) (discussing potential public-interest benefits from merger of AT&T with Cingular); *see generally* R.H. Coase, The Firm, the Market, and the Law (Univ. of Chicago Press 1990); Oliver E. Williamson, The Mechanics of Governance (Oxford Univ. Press 1996).

or terminates on the circuit-switched PSTN.[67] The only class of charges for which there might be any question as to the Commission's authority is intrastate access charges. And the better reading of section 251(b)(5)—a reading supported by the carve-out in section 251(g) and by Commission precedent—is that the 1996 Act empowered the Commission to regulate all forms of intercarrier compensation for *any* exchange of "telecommunications" traffic on the PSTN, including intrastate access. In any event, the "impossibility" exception of *Louisiana Public Service Commission v. FCC* independently authorizes the Commission to regulate intercarrier compensation for *all* classes of PSTN traffic to effectuate its responsibilities under sections 201 and 251.[68] Finally, no one disputes that the Commission has powerful tools at its disposal to encourage voluntary state adoption of comprehensive intercarrier compensation reform.

1. Section 251(b)(5) Applies to All Telecommunications Traffic on the PSTN.

Section 201(b) of the Communications Act authorizes the Commission to "prescribe such rules and regulations as may be necessary in the public interest to carry out the provisions of this [Act]." 47 U.S.C. § 201(b). As the Supreme Court confirmed in *Iowa Utilities Board*, the Commission's section 201(b) rulemaking jurisdiction is not limited to jurisdictionally interstate matters. *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 377-86 (1999). Rather, it extends to all provisions of the Communications Act, including those added by the 1996 Act that encompass matters that, before 1996, fell within the exclusive jurisdiction of the states. *Id.* It is thus

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[67] After the transition to all-IP networks, voice services will be provided through VoIP. And the Commission, "not the state commissions," has the authority to regulate jurisdictionally mixed VoIP service. *Vonage Order*, 19 FCC Rcd at 22404-05 ¶ 1; *see id.* at 22432 ¶ 46 (noting that "[t]o the extent other entities, such as cable companies, provide VoIP services, we would preempt state regulation to an extent comparable to what we have done in this Order"). *See also* pages 29-30, *supra* (discussing regulatory classification of VoIP). Accordingly, the Commission will have jurisdiction to eliminate all intercarrier compensation and interconnection regulation when all calls are IP-to-IP and do not transit the PSTN.

[68] 476 U.S. 355 (1986) ("*Louisiana PSC*").

undisputed that the Commission may adopt intercarrier compensation rules with respect to all traffic—interstate and intrastate—falling within the scope of section 251(b)(5). And as discussed below, that provision applies to, and thus authorizes the Commission to regulate, intercarrier compensation for *any* exchange of telecommunications traffic on the PSTN.

Congress drafted section 251(b)(5) expansively to bring national consistency to questions of intercarrier compensation. By its terms, that provision extends to all compensation issues relating to the transport and termination of "*telecommunications*" involving at least one LEC—*i.e.*, one circuit-switched "telecommunications carrier" providing local exchange services—at one end of the call.[69] Section 251(b)(5) makes no distinctions among traffic on the basis of jurisdiction ("local," "toll," "intrastate," "interstate") or service definition (*e.g.*, "exchange access," "information access," or "exchange service"). Thus, the Commission was entirely correct to conclude in the *ISP Remand Order* that "[w]e were mistaken [in the *Local Competition Order*] to have characterized" section 251(b)(5) as limited to local traffic, given that "'local' … is not a term used in section 251(b)(5) or section 251(g)."[70] The Commission has since reaffirmed that conclusion a number of times.[71] Given the plain text of the statute, the Commission would face substantial litigation risks were it to reverse course now on the scope of

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[69] Section 251(b)(5) covers intercarrier compensation issues on the originating end of a call and not just the terminating end. As the Commission recognized in the *Local Competition Order*, because section 251(b)(5) provides for intercarrier compensation only for "transport and termination" of traffic and does not authorize charges for origination of traffic, that provision precludes LECs from charging CMRS providers or other carriers for any LEC-originated traffic encompassed by section 251(b)(5). *See* First Report and Order, *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, 11 FCC Rcd 15499, 16016 ¶ 1042 (1996) ("*Local Competition Order*").

[70] *ISP Remand Order*, 16 FCC Rcd at 9166-67, 9172-73 ¶¶ 34, 45. The D.C. Circuit left this conclusion intact on review, although it took issue with other aspects of the *ISP Remand Order*. *See WorldCom, Inc. v. FCC*, 288 F.3d 429 (D.C. Cir. 2002).

[71] *See, e.g.*, *NPRM* ¶¶ 512-15; *2008 IC/USF Order and FNPRM*, 24 FCC Rcd at 6480 ¶ 8.

section 251(b)(5): "Even under the deferential *Chevron* standard of review, an agency cannot, absent strong structural or contextual evidence, exclude from coverage certain items that clearly fall within the plain meaning of a statutory term."[72]

Further, section 251(b)(5) applies not just to the exchange of traffic between two LECs, but also to the terms on which LECs receive terminating traffic from non-LECs (such as IXCs). The Commission has repeatedly concluded that section 251(b)(5) extends to the exchange of *any* traffic involving a LEC at one end.[73] Though the *obligation* to establish reciprocal compensation arrangements for the transport and termination of telecommunications falls on LECs, Congress did not limit the class of potential *beneficiaries* of that obligation to other LECs.

Finally, the statutory structure as a whole belies the argument that Congress somehow meant to deprive the Commission of authority to address intercarrier compensation issues for traffic that is deemed to be neither "local" (and covered by section 251(b)(5)) nor "interstate" (and covered by section 201(a)). Efforts to carve up the Commission's rulemaking authority on the basis of such legacy jurisdictional categories are strikingly similar to the unavailing attacks in the 1990s on the Commission's jurisdiction to implement sections 251 and 252 more generally. Here, as in that context, the attempt to "produce[] a most chopped-up statute" along jurisdictional lines is flawed both because it violates the statutory text and because it is "most unlikely that Congress created such a strange hodgepodge."[74] Indeed, it would have been perverse for

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[72] *United States Telecomm Ass'n v. FCC*, 359 F.3d 554, 592 (D.C. Cir. 2004) ("*USTA II*"). The statutory context in which the D.C. Circuit enforced that principle is closely analogous to that here. Just as the court rejected the Commission's argument that long distance services are not "telecommunications services" for purposes of section 251(d)(2), so too should the Commission reject the argument that long distance services are not "telecommunications" for purposes of section 251(b)(5). *Id.*

[73] *See, e.g.*, *Local Competition Order*, 11 FCC Rcd at 16016 ¶ 1041; *NPRM* ¶ 513; *2008 IC/USF Order and FNPRM*, 24 FCC Rcd at 6480-81 ¶ 10.

[74] *Iowa Utils. Bd.*, 525 U.S. at 381 n.8.

Congress to have authorized the Commission to reform intercarrier compensation rules relating to "local" and "interstate" traffic but not the rules applicable to the one class of traffic—intrastate access—that is subject to the *highest* above-cost charges and that is generally thought to be most laden with unsustainable implicit support.

2. Section 251(g) Confirms the Breadth of the Commission's Jurisdiction Under Section 251(b)(5).

Additional support for this interpretation of the statute appears in section 251(g). That provision, which expressly preserves intercarrier compensation regimes that predate the 1996 Act, makes clear that the Commission has plenary jurisdiction to address intercarrier compensation for all "telecommunications" under section 251(b)(5), including access traffic.

Section 251(g) singles out access traffic for special treatment and *temporarily* grandfathers the pre-1996 rules applicable to such traffic, including rules governing "receipt of compensation," until the Commission exercises its discretion to "supersede[]" these legacy rules with generally applicable rules promulgated under section 251(b)(5).[75] There would have been no need for Congress to have preserved those legacy rules against the effects of section 251 if section 251(b)(5) did not in fact address the "receipt of compensation" for the traffic covered by section 251(g)—*i.e.*, access traffic. *See NPRM* ¶ 514.

Nothing in the Commission's precedent precludes this interpretation of section 251(b)(5). Granted, in the *ISP Remand Order*, the Commission noted that services falling within the scope of section 251(g) "remain subject to Commission jurisdiction under section 201 (or, to the extent they are *intra*state services, they remain subject to the jurisdiction of state commissions)."[76] But this does not foreclose the Commission from exercising jurisdiction over intrastate access

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[75] 47 U.S.C. § 251(g).

[76] *ISP Remand Order*, 16 FCC Rcd at 9169 ¶ 39.

charges. There is no question that section 251(g) temporarily preserves the regulatory status quo for all traffic within that provision's scope. There is also no question that intrastate access traffic falls within that scope: As the Commission has repeatedly confirmed, the "section 251(g) carve-out includes intrastate access services."[77] The only dispute is whether, as the Commission has proposed, it can and should "supersede that carve-out" by "replac[ing] intrastate access regulation with some alternative mechanism" of the Commission's design as part of a comprehensive approach to intercarrier compensation.[78]

The only logical answer is yes. The sole reason that the "section 251(g) carve-out includes intrastate access services," *id.*, is that, if it did *not* include them, section 251(b)(5) would have operated to eliminate those access charges immediately. Once the Commission removes this or any class of traffic from the scope of section 251(g), that traffic becomes subject to section 251(b)(5)—as it would have been from the beginning if Congress had not temporarily grandfathered such traffic from the effects of section 251 to begin with. And because the

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[77] Further Notice of Proposed Rulemaking, *Developing a Unified Intercarrier Compensation Regime*, 20 FCC Rcd 4685, 4722 ¶ 79 (2005) ("*FNPRM*"). *See NPRM* ¶ 514; *ISP Remand Order*, 16 FCC Rcd at 9169-70 ¶ 39. This conclusion is correct: no less than its interstate counterpart, the intrastate access charge regime falls within the temporary grandfathering mechanism in section 251(g) for "equal access and nondiscriminatory interconnection … obligations (including receipt of compensation) … under any court order, consent decree," or FCC order. Before 1982, compensation for interexchange access was generally derived through an AT&T-administered system of settlements and division of revenues. Second Supplemental Notice of Inquiry and Proposed Rulemaking, *MTS and WATS Market Structure*, 77 FCC 2d 224, 227-28, 234 ¶¶ 15-19, 47 (1980). The AT&T consent decree replaced that system with a regime of federal *and* intrastate access charges. *See United States v. AT&T Co.*, 552 F. Supp. 131, 227, 233 (D.D.C. 1982); Third Report and Order, *MTS and WATS Market Structure*, 93 FCC 2d 241, 246 ¶ 11 (1983). The court order accompanying the consent decree made clear that the decree required access charges to be used in both the interstate and intrastate jurisdictions: "Under the proposed decree, state regulators will set access charges for intrastate interexchange service and the FCC will set access charges for interstate interexchange service." *AT&T*, 552 F. Supp. at 169 n.161. Thus, both interstate and intrastate access charges were born of the same "consent decree," and both are preserved under section 251(g).

[78] *FNPRM*, 20 FCC Rcd at 4722 ¶ 79.

Commission has plenary authority under *Iowa Utilities Board* to implement section 251(b)(5), it has plenary authority to address compensation issues involving intrastate access traffic.

3. The *Louisiana PSC* "Impossibility" Exception Independently Authorizes the Commission to Regulate All PSTN Intercarrier Compensation.

Because the Commission's *Iowa Utilities Board* authority under sections 201(b) and 251(b)(5) extends broadly to all intercarrier rates, the Commission need invoke no further authority to adopt comprehensive intercarrier compensation reform. Nonetheless, in addition to that authority, the Commission has—and should assert—independent pre-1996 Act jurisdiction under section 201 to take the steps needed to ensure a nationally consistent intercarrier compensation regime as to both originating and terminating traffic.

Traditionally, section 2(b) of the Communications Act has precluded the Commission from regulating all jurisdictionally intrastate intercarrier compensation.[79] It is a fair question whether this provision should have *any* application today as the industry rapidly transitions from the legacy, circuit-switched services of the past to the all-distance, IP services of the future. Section 2(b) provides that the Commission does not have "jurisdiction with respect to … charges, classifications, practices, services, facilities, or regulations for or in connection with *intrastate communication service* by wire or radio[.]" 47 U.S.C. § 152(b) (emphasis added). Importantly, the statute does not focus on *traffic* (*i.e.*, individual calls), but on *services*, and it assumes that there will be some services that are intrastate, and some that are interstate. This assumption is fundamentally at odds with today's communications landscape, where a large and rapidly increasing percentage of voice calls are made using all-distance services, such as wireless

[79] 47 U.S.C. § 152(b); *see Louisiana PSC*, 476 U.S. 355 (1986).

or VoIP, for which legacy jurisdictional distinctions are simply irrelevant.[80] Indeed, even legacy telecommunications services are often provided on an "all-you-can-eat" basis, offering consumers unlimited local and long distance (both inter- and intrastate) for one monthly fee. It makes no sense to continue to force the archaic jurisdictional split of "intrastate" versus "interstate" service on a marketplace that increasingly is not susceptible to such distinctions. And, as the Commission and the courts already have noted in the VoIP context, it certainly makes no sense to force providers of all-distance services to artificially divide (or to continue dividing) their offerings into separate intrastate and interstate components merely to ensure a continued role for state regulators.[81] Instead, the Commission should conclude that section 2(b) applies only to wholly intrastate *services*, and not to individual *calls* that happen to originate and terminate within the same state. Further, it should conclude that states cannot force service providers to divide their offerings into separate interstate and intrastate services rather than unified, all-distance (and thus interstate) services subject only to federal jurisdiction.

Nonetheless, even if section 2(b) remains a meaningful constraint on the Commission's authority to regulate historically "intrastate" calls (rather than services), the Commission has ample authority to regulate intrastate access charges as part of its comprehensive reform of intercarrier compensation. Since 1996, two basic developments have significantly undermined the notion that the Commission lacks authority to regulate traffic that originates and terminates in

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[80] *See* Federal Communications Commission, Wireline Competition Bureau, Industry Analysis & Technology Division, *Local Telephone Competition: Status as of June 30, 2010*, at 2 (Fig. 1) (Mar. 2011), http://www.fcc.gov/Daily_Releases/Daily_Business/2011/db0321/DOC-305297A1.pdf ("*FCC Local Telephone Competition Report*") (reporting that retail switched access lines have decreased over 13% between 2008 and 2010 (from approx. 141 million to 122.3 million), while the number of interconnected VoIP subscriptions has increased nearly 33% during the same period (from approx. 21.7 million to 28.9 million)); CTIA, *U.S. Wireless Quick Facts*, http://www.ctia.org/media/industry_info/index.cfm/AID/10323 (wireless subscriptions have increased over 45% from 207.9 million in 2005 to 302.9 million in 2010).

[81] *See Vonage Order*, 19 FCC Rcd at 22422-43 ¶ 29; *Minn. PUC*, 483 F.3d at 578.

the same state. First, in the 1996 Act, Congress authorized the FCC to regulate intercarrier compensation for traffic that, even under the *narrowest* interpretation of section 251(b)(5), indisputably includes most intrastate calls (*i.e.*, all local calls). Second, the industry has seen rapid growth in services, such as wireless and VoIP, that the Commission has authority to regulate without regard to whether the particular traffic in question is "interstate."[82] As a result of these changes, the Commission now has clear jurisdiction to prescribe intercarrier compensation rules for all major categories of traffic on the PSTN: interstate (sections 201 and 251(g)), intrastate transport and termination (section 251(b)(5)), wireless (section 332), and VoIP (section 201[83]).

No one disputes that these recent developments have superseded the traditional limits on FCC jurisdiction and that, despite section 2(b), the Commission may now regulate intercarrier compensation for most calls that originate and terminate in the same state. The only class of traffic as to which there is any serious debate about the Commission's jurisdiction is wireline, circuit-switched, intrastate interexchange traffic. Such traffic constitutes a still-significant but declining percentage of services overall. The only question is whether section 2(b) fences off this arbitrarily defined class of calls from the FCC's otherwise comprehensive regulatory authority—even though these are the calls for which intercarrier compensation reform is most needed, and even though it is "most unlikely that Congress" meant to produce such "chopped-up statute"[84] by permitting the FCC to regulate intercarrier compensation for all calls except these.

Section 2(b) would not require that bizarre result even if section 251(b)(5) did *not* encompass intrastate access traffic. The "impossibility" exception set forth in footnote 4 of

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82 *See* footnote 80, *supra.*

83 *See Vonage Order*, 19 FCC Rcd 22404.

84 *Iowa Utils. Bd.*, 525 U.S. at 381 n.8.

Louisiana PSC authorizes the Commission to regulate matters traditionally left to the States when such regulation is necessary to protect a valid federal regulatory objective.[85] Here, genuine reform for *any* class of traffic, including traffic over which the Commission has undisputed jurisdiction, cannot succeed unless the reforms encompass *every* substantial class of traffic, including intrastate access traffic; otherwise, artificial rate disparities for functionally substitutable services will continue to destabilize the industry as a whole. Federal involvement is therefore necessary to prevent methodological inconsistencies from "thwart[ing] the lawful exercise of federal authority over interstate communications."[86]

The case for preemption here is much stronger than it was in *Louisiana PSC*. There, the only question was whether it was feasible, as an accounting matter, for the federal government and the states to prescribe different depreciation rates for the same equipment. The Court held that it was, and no harm came to the industry as a whole.[87] In this case, the question is whether the FCC must stand idly by while radical regulatory disparities create worsening fraud and arbitrage opportunities that, if left unchecked, will undermine the industry's stability in general and universal service in particular. The damage threatened by further federal inaction cannot be compartmentalized into "interstate" and "intrastate" spheres; it would affect every corner of this industry, every type of telecommunications service, and the most basic federal policy objectives ranging from universal service to deregulation to competition. Only by replacing the ineffective patchwork of intercarrier compensation rules with a comprehensive and unified approach can the Commission remedy these urgent problems.

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85 *See Louisiana PSC*, 476 U.S. at 376 n.4; *see generally Vonage Order*, 19 FCC Rcd at 22418-24 ¶¶ 23-32 (discussing case law and applying it to VoIP jurisdictional disputes).

86 *Vonage Order*, 19 FCC Rcd at 22412 ¶ 15; *see also Nat'l Ass'n of Regulatory Util. Comm'rs v. FCC*, 880 F.2d 422, 429 (D.C. Cir. 1989) ("*NARUC III*").

87 *See* 476 U.S. at 358-59, 375-76.

No more need be shown to trigger the Commission's jurisdiction under the "impossibility" exception. Nothing in footnote 4 of *Louisiana PSC* confines the "impossibility" exception to cases in which it is *technically* impossible to compartmentalize the interstate and intrastate subjects of regulation. To the contrary, the *Louisiana PSC* Court indicated that section 2(b) is inapplicable where jurisdictional compartmentalization is technically possible but separate state regulation would "negate" federal policy goals by forcing providers to divide their services arbitrarily and inefficiently into interstate and intrastate components.[88] Here, the Commission may assert plenary jurisdiction over intercarrier compensation to protect federal policy objectives whether or not it will be feasible for carriers on a technical level to distinguish between "interstate" and "intrastate" traffic for compensation purposes.

In any event, the Commission could readily conclude that, in today's telecommunications landscape, separation of individual calls into distinct "interstate" and "intrastate" jurisdictions *is* technically infeasible. In the *Vonage Order*, the Commission recognized that carriers cannot easily keep track of the geographic endpoints of VoIP calls for compensation purposes.[89] And because wireless services are inherently mobile, it is often "difficult for CMRS providers to determine, in real time … the customer's specific geographic location" for rate-making purposes.[90] Wireless and VoIP traffic make up a large percentage of all traffic today, and a disproportionately large percentage of intercarrier compensation disputes already arise from the

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[88] Specifically, the Court noted, with approval, the FCC's decision to preempt state laws "prohibiting subscribers from connecting their own phones unless used exclusively in interstate service." *See id.* at 376 n.4 (citing *North Carolina Utils. Comm'n v. FCC*, 537 F.2d 787 (4th Cir. 1976), and *North Carolina Utils. Comm'n v. FCC*, 552 F.2d 1036 (4th Cir. 1977)).

[89] *See Vonage Order*, 19 FCC Rcd at 22420-21 ¶ 25; *see also* Memorandum Opinion and Order, *Petition for Declaratory Ruling That Pulver.com's Free World Dialup Is Neither Telecommunications Nor a Telecommunications Service*, 19 FCC Rcd 3307, 3320-23 ¶¶ 21-24 (2004).

[90] *Local Competition Order*, 11 FCC Rcd at 16017-18 ¶ 1044.

exchange of such traffic, given the difficulty of pinpointing a wireless or VoIP call's geographic endpoints.[91] Wireless and VoIP services are now eclipsing traditional wireline telephony in commercial significance. As that process unfolds, it is increasingly difficult to determine, on a call-by-call basis, which calls are actually "intrastate" and which calls are actually "interstate." Section 2(b) does not require the Commission to withhold comprehensive intercarrier compensation reform, and distort the progress of the telecommunications industry, simply to accommodate that fool's errand.

4. The Commission's Implementation of Comprehensive Intercarrier Compensation Reform Would Be Fully Consistent with Section 252.

Section 252 poses no obstacle to the Commission's implementation of the intercarrier compensation reforms set out above. The Commission not only may prescribe bill-and-keep as the default final compensation rule for all PSTN traffic, but also has authority to impose a rational transition to that end state.[92]

The text of section 252(d)(2) permits bill and keep for all traffic, including unbalanced traffic.[93] As an initial matter, section 252(d)(2)(A) directs the Commission and the states (i) to "provide for the mutual and reciprocal recovery by each carrier of costs associated with the transport and termination on each carrier's network facilities of calls that originate on the network facilities of the other carrier," and (ii) to "determine such costs on the basis of a reasonable approximation of the additional costs of terminating such calls." 47 U.S.C.

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[91] Indeed, because the number of wireless connections now exceeds the number of wireline connections, telephone numbers are no longer a reliable method for determining the end points of a call.

[92] Again, bill and keep will be the default end state only for circuit-switched PSTN traffic. For VoIP traffic, interprovider compensation issues will be governed solely by market forces rather than prescriptive regulation, as they are on the Internet today.

[93] *WorldCom*, 288 F.3d at 434 (encouraging the Commission to consider invoking section 252(d)(2)(B)(i) as a basis for ordering bill and keep for ISP-bound traffic).

§ 252(d)(2)(A). This language is perfectly consistent with a regime, such as bill and keep, in which each carrier is afforded an opportunity for "recovery" of those costs from its own end users.[94]

If there were any question on this point, it would be answered by the "bill-and-keep" savings clause. Section 252(d)(2)(B)(i) expressly authorizes all regulatory "arrangements that afford the mutual recovery of costs through the offsetting of reciprocal obligations, including arrangements that waive mutual recovery (such as bill-and-keep arrangements)." 47 U.S.C. § 252(d)(2)(B)(i). As the legislative history of section 252 confirms, this clause permits "a range of compensation schemes, such as an in-kind exchange of traffic without cash payment (known as bill-and-keep arrangements)."[95] Importantly, the D.C. Circuit has already indicated its support for the same conclusion, noting the "non-trivial likelihood that the Commission has authority to elect" a bill-and-keep regime for section 251(b)(5) traffic under the terms of section 252(d)(2)(B)(i), which the court specifically cited.[96] Although section 252(d)(2), like the 1996 Act as a whole, "is in many important respects a model of ambiguity or indeed even self-contradiction," Congress "is well aware that the ambiguities it chooses to produce in a statute will be resolved by the implementing agency."[97] Here, the Commission can and should resolve any ambiguity in this statutory language in favor of an appropriately robust construction of the bill-and-keep savings clause.

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[94] *See Local Competition Order*, 11 FCC Rcd at 16055 ¶ 1112 ("bill-and-keep arrangements that lack *any* provisions for compensation do not provide for recovery of costs") (emphasis added).

[95] S. Rep. No. 104-230, at 120 (1996).

[96] *See WorldCom*, 288 F.3d at 434.

[97] *Iowa Utils. Bd.*, 525 U.S. at 397.

In prior proceedings, some parties have contended that a transition to bill-and-keep would violate the Act by requiring the Commission to cross a line, supposedly drawn by the Supreme Court in *Iowa Utilities Board*, separating the FCC's role in setting a cost *methodology* from the states' role in setting actual *rates*. This claim lacks merit.

First, the Commission would not inappropriately intrude on state jurisdiction in adopting bill and keep as the default end state for intercarrier compensation on the PSTN. The Court in *Iowa Utilities Board* made clear that the Commission has broad authority to specify a rate methodology from a "range of compensation schemes" to be used in implementing section 251.[98] Bill and keep is a methodology, not a "rate," just as CPNP is a methodology. The former requires carriers to recover their termination costs from their end users, whereas the CPNP methodology requires carriers to recover termination costs from another carrier. The end-user recovery approach does not amount to a rate prescription simply because the charge to a carrier under that scheme is zero.

Second, the Commission also has authority to set interim rates to establish a rational glide path from the existing regime to the default bill-and-keep end state. Specifically, the Commission could exercise its well-established authority to impose interim rules to ensure a smooth transition to a new regulatory regime. In a variety of contexts, and particularly in matters of intercarrier compensation, the courts have repeatedly granted the Commission expansive authority to mandate reasonable transitional measures needed to protect the industry from sudden disruptions.[99] The Commission has clear authority here to adopt similar measures to manage the

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[98] S. Rep. No. 104-230, at 120 (1996); *Iowa Utils. Bd.*, 525 U.S. at 385 (explaining that "the Commission has jurisdiction to design a pricing methodology").

[99] *See, e.g.*, *Competitive Telecomms. Ass'n v. FCC*, 309 F.3d 8, 14 (D.C. Cir. 2002) ("Avoidance of market disruption pending broader reforms is, of course, a standard and accepted justification for a temporary rule."); *Tex. Office of Pub. Util. Counsel v. FCC*, 183 F.3d 393, 437

transition from today's fragmented intercarrier compensation regime to a unified bill-and-keep regime.

In any event, nothing in *Iowa Utilities Board* limits the FCC to merely setting a cost methodology while the states set actual rates. The relevant passage in that decision holds only that section 252, which anticipates that state commissions will set rates in the course of arbitrating disputes, does not implicitly repeal the FCC's general rulemaking jurisdiction under section 201(b).[100] And the Court observed that the latter provision authorizes the Commission to "prescribe such rules and regulations as may be necessary in the public interest to carry out the provisions of" the Communications Act,[101] "which include §§ 251 and 252, added by the Telecommunications Act of 1996."[102] Administrative agencies like the FCC issue rules that run the gamut from very general to very specific. Here, the grant of rulemaking authority in section 201(b) does not remotely confine the Commission to the promulgation of abstract

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(5th Cir. 1999) ("*TOPUC*") ("Where the statutory language does not explicitly command otherwise, we defer to the agency's reasonable judgment about what will constitute 'sufficient' support during the transition period from one universal service system to another."); *id.* at 440 n.85 ("[W]e extend the FCC greater discretion in deciding what will [constitute] 'sufficient' [support] during the transition period."); *Competitive Telecomms. Ass'n v. FCC*, 117 F.3d 1068, 1073-75 (8th Cir. 1997) ("Although temporary agency rules are subject to judicial review notwithstanding their transitory nature, 'substantial deference by courts is accorded to an agency when the issue concerns interim relief.'") (quoting *MCI Telecomms. Corp. v. FCC*, 750 F.2d 135, 140 (D.C. Cir. 1984)).

[100] *See* 525 U.S. at 384-85.

[101] 47 U.S.C. § 201(b).

[102] 525 U.S. at 378. Notably, in *dissenting* from the majority's decision to uphold the FCC's pricing jurisdiction, Justice Breyer appeared to endorse what he called "[t]he FCC's strongest argument"—that "its rate rules do not actually supplant local ratesetting authority" but "simply set forth limits[.]" *Id.* at 423 (Breyer, J., dissenting in relevant part). Justice Breyer nonetheless dissented on the ground that "[t]he FCC's rules … are not general" but rather are "highly specific and highly detailed" (*id.*)—a fact that did not trouble the Court's majority, which upheld the rules anyway.

methodological rules instead of rules prescribing specific rate caps, as the Commission confirms each time it issues rules prescribing particular rates for particular services.[103]

Of particular relevance here, the Commission exercised that authority to set specific rates for terminating ISP-bound traffic, including the $0.0007 rate that applies today.[104] Although the D.C. Circuit invalidated the precise doctrinal basis of the Commission's ISP-bound traffic rules, the court declined to vacate the Commission's rate prescriptions because it found that the Commission might well succeed in imposing the same outcome "under §§ 251(b)(5) and 252(d)(B)(i)."[105] At no point did the D.C. Circuit suggest that the FCC might need to defer such rate-setting authority to the states, even though the rates at issue fall (as the Court found) within the purview of sections 251(b)(5) and 252(d)(2). Indeed, just two years later, the D.C. Circuit admonished the Commission to *avoid* undue delegations of federal rulemaking authority to the states.[106]

Finally, the Commission can and should forbear from section 252 to the extent that this provision could frustrate implementation of comprehensive intercarrier compensation reform. Section 10 of the Communications Act provides that the Commission "shall forbear from applying … *any* provision of this [Act]," including sections 252(c)(2) and 252(d)(2), if three conditions are met. 47 U.S.C. § 160(a) (emphasis added). They are met here. First, because

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[103] *See, e.g.*, Memorandum Opinion and Order, *Tariffs Implementing Access Charge Reform*, 13 FCC Rcd 14683, 14707 ¶ 53 (1998) (explaining that, "[u]nder Section 201(b), we are charged with ensuring the price cap LEC rates are just and reasonable, and in exercising that authority, we have the ability to set just and reasonable rates when we find rates to be unreasonable. The Communications Act empowers us 'to determine and prescribe what will be the just and reasonable charge, or the maximum or minimum, or maximum and minimum, charge or charges' these LECs are permitted to impose") (footnotes omitted).

[104] *ISP Remand Order*, 11 FCC Rcd at 9186-92 ¶¶ 77-85.

[105] *WorldCom*, 288 F.3d at 434.

[106] *See USTA II*, 359 F.3d at 565-66.

reform will ensure just, reasonable, and non-discriminatory intercarrier charges, enforcement of sections 252(c) and 252(d) "is not necessary to ensure that" intercarrier charges "are just and reasonable and are not unjustly or unreasonably discriminatory." *Id.* § 160(a)(1). Second, enforcement of these provisions "is not necessary for the protection of consumers." *Id.* § 160(a)(2). Indeed, creating greater national consistency in intercarrier compensation rates will *benefit* consumers. Third, forbearance is "consistent with the public interest." *Id.* § 160(a)(3). Forbearance will enable the Commission to fix a broken intercarrier compensation regime that is destabilizing the entire industry. Moreover, by reducing regulatory disparities and economic inefficiencies in the marketplace, reform will "promote competitive market conditions" and "enhance competition among providers of telecommunications services." *Id.* § 160(b) (defining "public interest" for purposes of 47 U.S.C. § 160(a)(3)).

5. The Commission Also Should Encourage Voluntary State Cooperation with Intercarrier Compensation Reform.

By employing the legal rationales discussed above, the Commission can preclude the states from obstructing comprehensive intercarrier compensation reform. Nonetheless, because there is some risk that a reviewing court might reject the Commission's assertion of jurisdiction over intrastate access charges, the Commission also should encourage *voluntary* state cooperation with its plan for intercarrier compensation reform. Specifically, the Commission should condition future universal service distributions in a state on that state's agreement to reduce intrastate access charges in accordance with the Commission's proposed reforms.[107]

Providing such incentives for access-charge reductions is perfectly consistent with the principle of dual jurisdiction. The federal government has broad authority to condition the

[107] We applaud those states that already have taken steps to reduce their intrastate access charges to the interstate access rate. And we encourage the states to continue making progress in harmonizing intra- and interstate intercarrier compensation rates.

extension of federal support on a state's adherence to the terms of a federal program. *See generally South Dakota v. Dole*, 483 U.S. 203 (1987). This principle applies to the Commission's relationship with the states under section 254. *See Qwest Corp. v. FCC*, 258 F.3d 1191, 1203-04 (10th Cir. 2001) ("*Qwest I*") (holding that the FCC has not just the authority, but the *obligation*, to give the states "carrot and stick" inducements to ensure their compliance with federal universal service goals); *TOPUC*, 183 F.3d at 393, 443-44 (holding that the Commission may place conditions on the states' receipt of federal universal service funding). Thus, the Commission has authority to adopt this belt-and-suspenders approach to protect its intercarrier compensation reforms against a subsequent court challenge.

II. THE COMMISSION AND THE STATES SHOULD ELIMINATE OUTDATED SERVICE OBLIGATIONS THAT UNNECESSARILY DELAY THE TRANSITION TO AN ALL-IP COMMUNICATIONS INFRASTRUCTURE.

The legacy POTS business model is declining at an astonishing rate. Incumbent carriers are hemorrhaging customers to competitors as consumers increasingly abandon legacy wireline services for wireless, VoIP, and other services. Competitive pressures and changes in consumer behavior—such as increased use of communications methods like e-mail, text messaging, and social-networking applications—are rapidly eroding the access charges and other implicit subsidies on which incumbent carriers have traditionally relied to provide service in high-cost areas. And the reforms that the Commission adopts in this proceeding will only hasten the demise of the legacy POTS business model by eliminating access charges and withdrawing explicit universal service support from legacy technologies.

In this context, it makes no sense to retain legacy service obligations that effectively require incumbent carriers to continue providing service throughout their territories using legacy, circuit-switched TDM technology. To the contrary, regulations that prop up the dying POTS regime only impede the transition to the next-generation networks of the future. As discussed

below, the states and the Commission should eliminate such legacy service obligations and adopt a procurement-model approach under which providers incur service obligations only when they consent to them in exchange for explicit universal service funding. In this way, regulators can hasten, rather than delay, the day when all Americans have access to broadband and IP-enabled services.

A. As the Industry Transitions to an All-IP Communications Infrastructure, Legacy Service Obligations Will Become Increasingly Obsolete.

State public utility commissions have traditionally imposed "carrier-of-last-resort," or "COLR," obligations on incumbent local exchange carriers. These obligations generally require carriers to provide telecommunications services to *all customers* in a given geographic area, often at regulated rates.[108] These obligations thus prevent carriers from refusing service to customers even when the costs of providing service far exceed the potential revenues.

Federal ETC obligations, though different in some respects, bear a striking similarity to state COLR obligations. Section 214(e)(1)(A) provides that ETCs "shall, throughout the service area for which the designation is received [ ] offer the services that are supported by Federal universal service support mechanisms under section 254(c)[.]" 47 U.S.C. § 214(e)(1)(A). The Commission has interpreted section 214(e)(1)(A) as requiring an ETC to provide supported services throughout its service area *regardless of whether the ETC is receiving any high-cost support for providing such service*.[109] Under this interpretation, an ETC's obligation to "offer and advertise the supported services 'throughout the service area for which the designation is

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[108] *See AT&T NBP #25 Comments* at 24-26; Comments of AT&T, Inc., *A National Broadband Plan for Our Future, NBP Public Notice #19*, GN Docket Nos. 09-51, 09-47, 09-137, at 11-12 (filed Dec. 7, 2009) ("*AT&T NBP #19 Comments*").

[109] *See, e.g.*, Report and Order, *Federal-State Joint Board on Universal Service*, 12 FCC Rcd 8776 ¶ 192 (1997) ("*First Universal Service Order*") (noting that an ETC's "service area" is the "overall area for which the carrier *may* receive support from federal universal service support mechanisms") (emphasis added).

received' … appl[ies] regardless of whether support is actually provided to ETCs operating within the designated area."[110] That interpretation thus imposes the equivalent of a federal COLR on every ETC in a given service area.

In addition, a variety of other legacy service obligations at both the state and federal levels specify the *types* of services that carriers must offer throughout their service areas. Many of those services can be provided only through circuit-switched, TDM technologies. For example, various states require providers to offer local dial tone service, rotary pulse dialing operability, dual-tone multi-frequency signaling, single-party service, SS7 signaling, and single-party revertive calling.[111] Similarly, the federal ETC rules require providers to offer several POTS-based features, such as access to interexchange service and access to operator and directory services, 47 C.F.R. § 54.101(a), as well as functionalities that assume service is provided over TDM, such as dual-tone multi-frequency signaling and single-party service, *id.* Together, therefore, carrier-of-last-resort and other legacy service obligations often have the effect of requiring carriers to serve every customer in their service areas using legacy POTS technologies.

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[110] *NPRM* ¶ 88. *See also* Order, *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service; Alltel Communications, Inc., et al. Petitions for Designation as Eligible Telecommunications Carriers; RCC Minnesota, Inc. and RCC Atlantic, Inc. New Hampshire ETC Designation Amendment*, 23 FCC Rcd 8834, 8847 ¶ 29 (2008) ("The Act does not … require that all ETCs must receive support, but rather only that carriers meeting certain requirements be *eligible* for support," and "designation as an ETC does not automatically entitle a carrier to receive universal service support.").

[111] *See, e.g.*, Ohio Revised Code § 4927.01(A)(1) (defining "basic local exchange service" to include local dial tone service); Wis. Admin. Code PSC § 160.03(2)(a)(3) (requiring rotary pulse dialing); Kan. Stat. Ann. § 66-1,187(p), (q) (requiring tone dialing and SS7 signaling); Mo. Code Regs. Ann. tit. 4 § 240-32.100(2)(B) (requiring dual tone multi-frequency signaling); *id*. § 240-32.100(2)(E) (requiring "SS7 … or an enhanced version thereof, down to the tandem level of the switching hierarchy"); Wis. Admin. Code PSC § 160.03(2)(a)(7) (requiring "[s]ingle party revertive calling, if 2 or more pieces of customer premises equipment can be simultaneously active on the line or channel being used by the customer").

These service obligations made sense in the era of local exchange monopolies, when the Commission's goal was ensuring that every consumer had access to POTS service. Indeed, they formed an integral part of the "regulatory compact" discussed above. Regulators granted incumbent carriers an exclusive franchise and guaranteed them a reasonable rate of return in exchange for a commitment by the carriers to offer high-quality, basic telecommunications services at affordable rates to all consumers in their service territories, including high-cost customers.[112] Carriers funded service in high-cost areas through a patchwork of implicit subsidies implemented through state-regulated rates for intrastate services and state and federal intercarrier compensation policies.

But as discussed above, that legacy POTS business model is in irreversible decline.[113] The introduction of competition has eroded the implicit subsidies on which carriers have traditionally relied to provide service in high-cost areas. And although Congress in the 1996 Act instructed the Commission and the states to develop alternative support mechanisms to ensure that consumers across the nation would have access to state-of-the-art telecommunications and information services,[114] federal and state regulators repeatedly have shied away from undertaking the sort of comprehensive universal service reforms required by the Act. While regulators have proceeded full-bore to implement the Act's market-opening provisions, they have continued to maintain COLR obligations—and their federal counterpart, ETC obligations—for incumbent carriers and forced them to continue relying on fast-eroding implicit subsidies to achieve universal service objectives. Although the Commission and some state regulators have replaced *some* of these implicit subsidies with explicit universal service support, for many carriers, that

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112 *AT&T NBP #25 Comments* at 24.

113 *See* Section I.A.1, *supra*.

114 47 U.S.C. § 254. *See Qwest I*, 258 F.3d at 1196.

support is woefully inadequate to offset the costs of providing service in high-cost areas. AT&T, for example, serves over one quarter of the rural lines in the country, yet it receives federal high-cost-model support in only three of its twenty-two ILEC states.[115] In short, ILECs must still serve customers in rural and other high-cost areas, often at rates significantly below their costs, but they have lost the implicit subsidies on which those low rates were based. The inevitable result is the collapse of the legacy POTS business model.

That collapse will be hastened by the reforms that the Commission adopts here. The purpose of this proceeding is accelerating the industry's transition from the legacy, circuit-switched network of yesterday to the all-IP architecture of the future. To that end, the Commission has proposed intercarrier compensation reforms that would eliminate access charges—one of the few remaining implicit subsidies funding carriers' provision of POTS service. And the Commission has proposed universal service reforms that would transition all explicit high-cost support for legacy POTS services to a Connect America Fund that supports broadband services. Under the new regime, many legacy high-cost support recipients will *not* receive high-cost universal service funding—instead, the CAF will support only one provider of broadband service in each high-cost area eligible for CAF funding.[116] In many cases, that provider will be a competitive provider instead of the ILEC. Thus, as a consequence of the Commission's reforms, many ILECs that are already struggling to maintain their existing POTS service will lose both their existing access revenues *and* their universal service support, making it infeasible for them to continue providing legacy telecommunications services in many high-cost areas.

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115 *See AT&T NBP #19 Comments* at 8.

116 *See* Section III.B.3, *infra*, for a discussion of which high-cost areas are "CAF-eligible."

This is not cause for lamentation. To the contrary, it makes abundant sense to sunset legacy networks, which do not provide the services that consumers increasingly demand, and to replace them with next-generation, all-IP communications networks. Further, it makes sense to manage scarce universal-service resources by limiting funding to a single provider of broadband service in each high-cost area. But in this radically new environment, it does *not* make sense to continue to saddle just one provider—the ILEC—with carrier-of-last-resort obligations that require it to provide service to all consumers. And it *certainly* does not make sense to impose legacy service obligations that effectively require the ILEC to continue providing *legacy POTS service* throughout its service territory.[117] Instead, *all* carriers should be permitted to make their own business decisions regarding the services they provide and the customers they serve. And universal service goals should be pursued not through public-utility-style service mandates, but through a procurement model in which providers agree to serve high-cost customers in return for explicit universal service support.[118]

Legacy service obligations are not merely unfair to providers; they are affirmatively harmful to consumers. As discussed in the next Section, these obligations impede the deployment of broadband and IP-enabled services in high-cost areas. And they inflict this harm without providing any countervailing benefit. Legacy service obligations are no longer necessary to ensure that customers have ready access to voice communications services. Rather, the POTS business model is collapsing precisely because consumers across the country are

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[117] For this reason, state requirements that compel ILECs to obtain approval from the state commission before ceasing to provide particular legacy services are not appropriate. Further, such requirements are discriminatory because providers of other communications services (such as wireless or interconnected VoIP) have no similar state service withdrawal obligations. *See, e.g.*, Nev. Rev. Stat. Ann. § 704.68885 (2007).

[118] The procurement-model approach to universal service is discussed in greater detail in Section III.A, *infra.*

abandoning traditional wireline providers for wireless, VoIP, and other services. Elimination of legacy obligations will not leave customers without communications service; to the contrary, it likely will increase their already abundant communications options by facilitating broadband deployment. In short, there no longer is any legitimate state or federal policy reason to compel any provider, or any class of providers, to be on call to serve any customer regardless of the cost. For all of these reasons, AT&T urges state policymakers to eliminate their outdated carrier-of-last-resort and other legacy service obligations. By doing so, policymakers can hasten the day when all of their constituents have access to broadband service.

The *NPRM* appears to recognize that fundamental changes must be made to the existing ETC regime to facilitate the transition to an all-IP communications network.[119] And many states have acknowledged that their obsolete service requirements must change as well. Indeed, some states have eliminated their carrier-of-last-resort and other legacy service obligations altogether.[120] Others have dramatically scaled them back.[121] And many more are actively considering eliminating their existing obligations.[122] AT&T commends these states for their efforts to adopt regulatory structures that are appropriate for 21st-century communications networks, and it urges other states to follow their lead. Indeed, AT&T expects that the vast

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119 *See NPRM* ¶¶ 89, 95-102.

120 Florida, for example, eliminated all COLR requirements effective January 1, 2009. Likewise, for certain companies, South Carolina has eliminated COLR obligations in most cases, except with respect to grandfathered, stand-alone residential basic POTS customers. *See AT&T NBP #19 Comments* at 22 & n.58.

121 Louisiana has eliminated COLR obligations for certain telephone exchanges based on the existence of competition, and has established a procedure by which carriers may obtain relief from COLR obligations in additional exchanges based on a showing of competition. *Id.*

122 *See, e.g.*, Mo. House Bill 339, at RSMo § 392.460(3), http://www.house.mo.gov/billtracking/bills111/billpdf/perf/HB0339P.PDF; *AT&T Louisiana's Petition for Modification of Rules and Regulations Necessary to Achieve Regulatory Parity & Modernization*, Docket No. R-31839 (La. Pub. Serv. Comm'n, filed Feb. 28, 2011); Tex. Sen. Bill 980, § 65.102, http://www.capitol.state.tx.us/BillLookup/History.aspx?LegSess=82R&Bill=SB980.

majority of states will take the steps necessary to promote the deployment of broadband within their borders.

The Commission has an important role to play in encouraging states to reform their existing obligations. As a positive inducement for reform, the Commission should give states that eliminate obsolete regulatory requirements a greater role in administering the CAF regime than those that do not. In addition, the Commission should condition all CAF funding on the state's agreement to eliminate COLR and other legacy service obligations that effectively require providers to continue offering POTS and long distance service and thereby inhibit the widespread availability and adoption of broadband services. As discussed above,[123] such an approach would fully comport with principles of dual jurisdiction—to the extent those principles continue to have meaning in an all-IP world. *See generally Dole*, 483 U.S. 203. Indeed, courts already have approved the use of such inducements to prompt state action with respect to universal service. *See, e.g.*, *Qwest I*, 258 F.3d at 1203-04 (holding that the FCC could "condition a state's receipt of federal funds upon" state actions that enable achievement of federal universal service goals); *TOPUC*, 183 F.3d at 443-44 (holding that the Commission may place conditions on a state's receipt of federal universal service funding).

This approach will prompt many states to eliminate obsolete legacy service obligations. In addition, by focusing state policymakers' attention on the transition from POTS to IP-enabled services, such inducements also could encourage states to adopt other policies—such as broadband funding mechanisms or tax credits for infrastructure deployment—that will accelerate that transition. In this way, the Commission could induce the states to become its full partners in ensuring that all Americans have access to broadband services.

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[123] *See* Section I.C.5, *supra*.

B. The Commission Should Ensure That State Commissions Eliminate Obsolete COLR and Legacy Service Obligations.

Despite the encouraging signs from many state policymakers, some states are likely to retain their legacy service obligations even if the Commission threatens to withhold CAF funding. In that event, the Commission will have little choice but to preempt those legacy obligations as inconsistent with federal universal service policy.[124]

Carrier-of-last-resort and other legacy service obligations impede the Commission's universal service policies in three different ways. *First*, in many cases they effectively preclude retirement of the PSTN, thereby requiring providers to maintain both legacy TDM and IP facilities—a costly and inefficient outcome that diverts capital from broadband deployment.[125] As discussed above, many state service obligations are defined by reference to a particular network architecture or include requirements that presume a carrier uses TDM technology.[126] In effect, these service obligations force incumbents to maintain their legacy, circuit-switched architecture. But maintaining both a circuit-switched *and* a packet-switched network is expensive—and each dollar that a carrier is forced to invest in the former is one less dollar that can be invested in deployment of next-generation broadband facilities and services. By one estimate, ILECs spent approximately $25 billion on capital expenditures in 2008, and over fifty

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[124] The Commission proposed to do just that in the draft order attached as Appendix C to its November 5, 2008 Further Notice of Proposed Rulemaking. *See 2008 IC/USF Order and FNPRM*, 24 FCC Rcd at 6697, Appx. C. Specifically, the Commission's order would have required winning bidders in the auction for broadband funding to assume "all of the [COLR] obligations of the incumbent LEC for [the ILEC's] study area, whether such obligations are imposed on the LEC pursuant to state or federal law." *Id.* at 6518 ¶ 39.

[125] These obligations also force industry vendors to dedicate resources to producing and maintaining antiquated equipment. Those resources would be far better spent on developing innovative IP equipment and services.

[126] *See* page 56, *supra*.

percent of that amount (52.2 percent) was spent on their legacy networks.[127] In other words, most of the capital resources of some of the largest telecommunications providers in the country are directed not towards improving broadband speeds or bringing broadband to more customers, but rather towards maintaining an increasingly obsolete network that is no longer capable of providing the services and features that American consumers and policymakers demand.[128]

Second, because in some states carrier-of-last-resort requirements force incumbent carriers to serve high-cost areas at below-cost rates, they make it more difficult for those carriers to devote the capital necessary to deploy broadband and advanced services in high-cost areas. Faced with service obligations that require them to operate at a loss in many high-cost areas, some ILECs—particularly the so-called "non rural" carriers that (despite the name) serve most of America's high-cost lines—expend significant resources to comply with their duty to provide POTS service throughout their service territories. And every dollar that a carrier is forced to spend to subsidize artificially low rates for POTS service is a dollar that cannot be spent on capital improvements necessary for the provision of next-generation communications services.[129]

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[127] Robert C. Atkinson & Ivy E. Schultz, Columbia Inst. For Tele-Info., *Broadband in America: Where It Is and Where It Is Going*, at 29-30 (Nov. 11, 2009), http://www.broadband.gov/docs/Broadband_in_America.pdf.

[128] As demonstrated by the precipitous line losses experienced by traditional wireline telecommunications carriers, consumers are increasingly demanding more than plain-old telephone service. *See* footnote 16, *supra* (discussing IBIS World report listing wired telecommunications carriers at the top of the list of "10 Key Dying Industries").

[129] The Commission appears to have recognized in the *NPRM* that it would be problematic to force a provider to shoulder the obligations of a broadband ETC designation without any assurance that the provider will obtain the universal service funding or other revenue necessary to provide that broadband service. *See, e.g.*, *NPRM* ¶ 319 n.484 (expressing concern that if the Commission does "not permit conditional ETC applications, but instead require[s] a carrier to be designated (or have applied for designation) as an ETC, at the time of an auction, in all areas for which it wishes to receive support, the carrier could find itself designated and obliged to provide services in areas where it does not receive any support"). The Commission should recognize in its order that it is no less problematic to impose ETC obligations on providers of legacy

Finally, state obligations that compel just one carrier—the ILEC—to offer service to all customers in a designated service territory are inconsistent with a procurement-model approach to universal service. As discussed above, the Commission should conclude that the time has come to abolish command-and-control, public-utility-style regulation and adopt a new regulatory compact that relies on consent rather than compulsion. Regulators should promote universal service in high-cost areas not through mandatory service obligations, but instead through explicit agreements with providers who agree to serve a specific area for a specific period of time in return for a specific amount of universal service funding. State carrier-of-last-resort obligations are fundamentally at odds with this approach to ensuring universal service.

In sum, legacy service obligations are inconsistent with federal universal service policy and frustrate the Commission's goal of ensuring that *all* Americans have access to broadband and IP-enabled services. Many state policymakers are likely to recognize this and conclude that they, too, have a compelling interest in eliminating outdated and discriminatory service obligations that impede broadband deployment in their states. However, if policymakers do not take steps to eliminate these obligations, the Commission will have no choice but to preempt them in favor of a procurement-model approach to universal service that better advances the Commission's broadband goals. In that case, the Commission can and should base such preemption authority on several independent grounds.

Traditional preemption analysis. If state regulators do not promptly eliminate carrier-of-last-resort and other legacy service obligations, the Commission should preempt those

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telecommunications services without ensuring that those providers have some means of recouping the costs of providing service.

obligations on the ground that they impermissibly regulate jurisdictionally mixed facilities in a manner that negates federal universal service policy.[130]

The Commission has recognized that "requiring an incumbent to maintain two networks—one copper and one fiber—would be costly [and] possibly inefficient, and reduce the incentive for incumbents to deploy fiber facilities." *National Broadband Plan* at 49. The Commission should now adopt a clear federal policy that outmoded, circuit-switched equipment and facilities should be retired and replaced with next-generation, IP networks.[131] If the Commission did so, it would have a strong basis for preempting state service obligations. As numerous courts have held, the legacy POTS architecture is jurisdictionally mixed because it carries both interstate and intrastate communications.[132] Further, many state service obligations are fundamentally inconsistent with a federal policy that legacy networks should be retired and replaced with IP networks, because they effectively preclude carriers from retiring their existing networks.[133] And it is hornbook law that where it is *physically impossible* to implement both federal policy (retirement of legacy facilities) and state policy (continued provision of legacy facilities) with respect to facilities used indivisibly for interstate and intrastate services, federal policy must prevail despite section 2(b) of the Communications Act.[134]

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[130] This analysis builds on the preemption discussion in Section I.C.3, *supra*. The same principles that give the Commission authority to regulate intrastate access charges also give it authority to preempt state legacy service obligations that impede the transition to an all-distance, all-IP end state.

[131] Indeed, AT&T has proposed that the Commission do exactly that in its prior comments. *See AT&T NBP #25 Comments* at 3-13; *AT&T NBP #19 Comments* at 22-23.

[132] *See, e.g.*, *Public Serv. Comm'n of Md. v. FCC*, 909 F.2d 1510, 1515 (D.C. Cir. 1990) ("[W]e have frequently held that services provided locally by the LECs which support access to the interstate communications network have interstate as well as intrastate aspects.").

[133] *See* pages 62-63, *supra*.

[134] *Louisiana PSC*, 476 U.S. at 376 n.4. *See also NARUC III*, 880 F.2d at 429-30 (where state regulation would "negate[] the exercise by the FCC of its own lawful authority over

Along similar lines, the Commission should conclude that state legacy service obligations negate the Commission's policy of ensuring that broadband is deployed throughout the nation. Granted, unlike with retirement of POTS facilities, it is not *physically* impossible to achieve the goal of broadband deployment in the face of state carrier-of-last-resort and other legacy service obligations. But, as discussed above, such obligations do make it *economically infeasible* for some carriers to roll out broadband service in high-cost areas. And that too is sufficient to justify federal preemption, despite section 2(b).[135]

For example, in *California v. FCC*, 39 F.3d 919, 931-33 (9th Cir. 1994), the Ninth Circuit upheld the Commission's preemption of state regulations requiring structural separation of the facilities and personnel used by BOCs to provide jurisdictionally mixed enhanced services. The FCC acknowledged that compliance with both state and federal requirements was technically possible. *Id.* at 933. But because "it would not be *economically feasible* for the BOCs to offer the interstate portion of such services on an integrated basis while maintaining separate facilities and personnel for the intrastate portion," the state regulation would necessarily result in structural separation of *both* interstate and intrastate services, thereby impeding the Commission's policy of abolishing such restrictions. *Id.* at 932-33 (emphasis added).[136] Accordingly, preemption was appropriate.

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interstate communication[s]" "state authority must yield to national imperatives"); *California v. FCC*, 39 F.3d 919, 933 (9th Cir. 1994) (concluding that preemption was clearly appropriate where "compliance with conflicting state and federal … rules would in effect be impossible").

[135] *See, e.g.*, *Public Serv. Comm'n*, 909 F.2d at 1515 (preemption is appropriate where "(1) the matter to be regulated has both interstate and intrastate aspects; (2) FCC preemption is necessary to protect a valid federal regulatory objective; and (3) state regulation would negat[e] the exercise by the FCC of its own lawful authority because regulation of the interstate aspects of the matter cannot be unbundled from regulation of intrastate aspects.") (internal quotation marks and citations omitted).

[136] *See also California*, 39 F.3d at 922 ("*[B]ecause of economic and operational factors*, enhanced service providers would separate their facilities for services that are offered both

Similarly, in a pair of cases, the Fourth Circuit upheld the Commission's preemption of state regulations prohibiting subscribers from connecting their own equipment to the telephone network unless that equipment was used *exclusively* for interstate service.[137] Even though it was physically possible for the state and federal regulations to coexist—because subscribers could use provider-supplied equipment for intrastate calls and their own equipment for interstate calls—the court concluded that preemption was permissible.[138] It noted that "[u]sually it is not feasible, as a matter of economics and practicality of operation, to limit the use of such equipment to either interstate or intrastate transmissions," and thus the "practical effect" of the state regulation would be to prohibit attachment of customer-provided equipment for *all* calls.[139] And because this would negate the federal policy permitting attachment of customer-provided equipment to the interstate network, the Commission had authority to preempt the contrary state regulation. *NCUC I*, 527 F.2d at 793; *NCUC II*, 552 F.2d at 1043.

So too here. It is impossible to limit the detrimental effect of state service obligations to the intrastate jurisdiction alone; rather, they have the "practical effect" of making it infeasible to deploy jurisdictionally interstate broadband facilities in many high-cost areas. Thus, if a state fails to eliminate those obligations, the Commission can and should preempt them as inconsistent

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interstate and intrastate, thereby *essentially negating the FCC's goal* of allowing integrated provision of enhanced and basic services.") (emphasis added).

[137] *North Carolina Utils. Comm'n v. FCC*, 537 F.2d 787 (4th Cir. 1976) ("*NCUC I*"); *North Carolina Utils. Comm'n v. FCC*, 552 F.2d 1036 (4th Cir. 1977) ("*NCUC II*"). The Supreme Court cited both of these cases with approval in *Louisiana PSC*. *See* 476 U.S. at 376 n.4.

[138] *See NCUC I*, 537 F.2d at 791; *NCUC II*, 552 F.2d at 1043; *see also California*, 39 F.3d at 933 ("The Fourth Circuit acknowledged that it was possible to comply with both the states' and the FCC's regulations: customers could have one telephone for interstate use and one for intrastate use.").

[139] *NCUC I*, 537 F.2d at 791, 793; *see also NCUC II*, 552 F.2d at 1043 (noting the "practical and economic impossibility" of providing separate equipment for the interstate and intrastate jurisdictions); *California*, 39 F.3d at 933 ("[I]t was highly unlikely, due to practical and economic considerations, that customers would maintain two separate phones.").

with federal universal service goals. Indeed, this was the very conclusion reached by the Commission in its *Western Wireless Order*.[140] There, the Commission preempted state regulations that amounted to an unfunded COLR obligation for competitive ETCs, noting: "To the extent that a state's [ETC requirements] … also involve[] matters properly within the state's intrastate jurisdiction under section 2(b) of the Act, such matters that are inseparable from the federal interest in promoting universal service in section 254 remain subject to federal preemption." *Western Wireless Order*, 15 FCC Rcd at 15179-80 ¶ 27.[141]

Finally, if the Commission were to adopt a procurement-model approach to universal service, it could preempt any remaining state carrier-of-last-resort and other service obligations on the basis that they directly negate that federal policy. As discussed above, legacy service obligations that *compel* incumbent providers to offer service are inconsistent with a new regulatory paradigm under which providers incur service obligations only to the extent that they consent to them in explicit agreements with regulators.[142] Given this, the Ninth Circuit's decision in *California* is directly on point. As with elimination of structural separation requirements, the Commission cannot achieve its deregulatory goals by eliminating legacy service obligations on the federal level alone. *See California*, 39 F.3d at 931-33. Rather, state command-and-control policies *must* be eliminated for the Commission to transition from the

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[140] Declaratory Ruling, *Federal-State Joint Board On Universal Service, Western Wireless Corporation Petition for Preemption of an Order of the South Dakota Public Utilities Commission*, 15 FCC Rcd 15168, 15181 ¶ 31 (2000) ("*Western Wireless Order*").

[141] The state regulation in question required competitive telecommunications carriers to provide service throughout an ILEC's service area before being designated as an ETC in that service area. *Western Wireless Order*, 15 FCC Rcd at 15181 ¶¶ 30-31.

[142] For this reason, the Commission should preempt service obligations even in those states that allow providers to satisfy their obligations using IP technology. Absent the consent of the provider in exchange for explicit funding, these obligations are inconsistent with the procurement-model approach to universal service.

existing public-utility-style regime to a new procurement-model approach. Accordingly, the Commission could readily demonstrate that "its regulatory goals … would be negated" if it does not preempt state service obligations. *Id.* at 933.

Section 254(f). Quite apart from the traditional preemption analysis, the Commission should preempt any remaining state service obligations on the additional and independent ground that they contravene section 254(f) of the Communications Act. Granted, that provision allows states to adopt "regulations … to preserve and advance universal service," 47 U.S.C. § 254(f), and COLR obligations were designed to promote universal service. But Congress also provided that such state measures are permissible only if: (i) they are "not inconsistent with the Commission's rules to preserve and advance universal service," (ii) they "do not rely on or burden Federal universal service support mechanisms," *and* (iii) they require "every telecommunications carrier that provides intrastate telecommunications services [to] contribute, on an equitable and nondiscriminatory basis … to the preservation and advancement of universal service in that State." *Id.*

State service obligations satisfy none of these requirements. *First*, as discussed above, those legacy burdens are "inconsistent with" the Commission's efforts to achieve ubiquitous deployment of broadband services. *Id.* They also are inconsistent with the procurement-model approach to universal service. *Second*, those obligations "burden Federal universal service support mechanisms" because they require carriers to offer POTS service in areas where it is uneconomic to do so, thereby increasing the need for legacy universal service support and growing the size of the federal fund. They also are likely to increase the size of the CAF, because POTS-oriented service obligations force providers to spend capital on legacy services

instead of investing that capital in broadband deployment. *Id.*[143] *Third*, because most states impose service obligations only on ILECs, those obligations are not an "equitable and nondiscriminatory" form of promoting universal service. *Id.* Given this, the Commission would be well within its authority under section 254(f) to preempt state service obligations in the event that states do not eliminate those obligations themselves.[144] And because the statute itself supplies the source of the Commission's preemption power, section 2(b) of the Act poses no obstacle to the Commission's assertion of jurisdiction.[145]

This analysis is supported by court decisions and Commission orders interpreting section 254(f). As the Tenth Circuit has explained, "[f]or regulation aimed at promoting universal service, Section 254(f) provides a hierarchy in which states cannot conflict with the federal universal services program[.]" *WWC Holding*, 488 F.3d at 1272. And the Commission has repeatedly interpreted the statute as foreclosing state requirements that undermine federal universal service goals, explaining as recently as last month that "section 254(f) … bars states from adopting regulations that are inconsistent with the rules established by the Commission to

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[143] *See also WWC Holding Co., Inc. v. Sopkin*, 488 F.3d 1262, 1277 (10th Cir. 2007) ("Section 254(f) authorizes a state to create its own universal service standards *only to the extent that a state is providing state funding to meet those standards*. To hold otherwise would ignore the last and longest sentence of section 254(f).") (emphasis added).

[144] Even if the statute were ambiguous, a reviewing court would be required to defer to the Commission's interpretation of section 254(f). *See, e.g.*, *Qwest Commc'ns Intl, Inc. v. FCC*, 398 F.3d 1222, 1229-30, 1233 (10th Cir. 2005) ("*Qwest II*").

[145] The Supreme Court held in *Iowa Utilities Board* that, after the 1996 Act, the states retain jurisdiction over intrastate matters only "[i]nsofar as Congress has remained silent." 525 U.S. at 381 n.8. Here, because section 254(f) expressly precludes states from adopting universal service rules that are "inconsistent with" federal regulation, the Commission has authority to preempt even regulations that apply only to intrastate communications.

preserve and advance universal service."[146] Indeed, in its *Western Wireless Order*, the Commission relied on section 254(f) in preempting a state requirement that a competitive carrier "provide service throughout [an ILEC's] service area prior to designation as an ETC" there.[147] The Commission noted that such a requirement—which is essentially an unfunded COLR obligation for competitive carriers—"discourages 'emerging technologies' from entering high-cost areas" and, accordingly, would be "inconsistent with the Commission's universal service policies and rules" in violation of section 254(f).[148] As discussed above, state legacy service obligations have the same effect on ILECs, deterring them from deploying broadband capability in high-cost areas. Accordingly, section 254(f) provides a firm basis for preemption of those obligations in the event that state policymakers do not eliminate them.

Jurisdictional Separations. As a belt-and-suspenders approach, the Commission also should foreclose state legacy service obligations by allocating 100% of the local loop to the interstate jurisdiction through the jurisdictional separations process. Although the local loop traditionally has been viewed as jurisdictionally mixed, last-mile infrastructure increasingly is being used to provide broadband and VoIP, both of which the Commission has concluded should be regulated at the federal level.[149] And that trend from POTS service to VoIP and other

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146 Notice of Proposed Rulemaking, *Lifeline and Link Up Reform and Modernization; Federal-State Joint Board on Universal Service; Lifeline and Link Up*, 26 FCC Rcd 2770, 2850 ¶ 258 & n.458 (2011) ("*Lifeline NPRM*").

147 *Western Wireless Order*, 15 FCC Rcd at 15181 ¶ 31.

148 *Id. See id.* at 15179-80 ¶ 27 (discussing deployment-deterring effect of COLR-like obligations). *See also* pages 77-79, *infra* (discussing Commission and Joint Board decisions discussing section 254(f) in the context of state ETC designations).

149 *See* Report and Order, *Preserving the Open Internet; Broadband Industry Practices*, 25 FCC Rcd 17905, 17970 ¶ 121 n.374 (2010) ("*Net Neutrality Order*") ("The Commission historically has recognized that services carrying Internet traffic are jurisdictionally mixed, but generally subject to federal regulation.") (citing authority); *Vonage Order*, 19 FCC Rcd 22404; *see also Quinn VoIP Ex Parte* at 3 (explaining that the *Vonage Order* applies equally to

broadband-enabled services will inexorably continue until providers have transitioned entirely to IP architecture. Given these market-transforming developments, the Commission can and should reasonably conclude that the local loops over which these innovative services are increasingly being provided should be allocated fully to the interstate jurisdiction.

There is ample precedent for this approach. In the special access context, for example, the Commission allocates 100% of a special access link to the interstate jurisdiction even when 90% of the traffic on that link is "intrastate" when evaluated under a traditional end-to-end jurisdictional analysis. *Qwest Corp. v. Scott*, 380 F.3d 367, 371 (8th Cir. 2004) (discussing the Commission's "ten percent rule"). Similarly, the Commission has deemed DSL service to be a special access service subject to the ten-percent rule,[150] and consequently that service too is allocated fully to the federal jurisdiction even though some DSL communications might be considered "intrastate" under an end-to-end analysis.[151]

And the Commission has always had a flexible view of jurisdictional separations with respect to the local loop in particular. For decades, the Commission has allocated one quarter of the loop to the interstate jurisdiction even though the vast majority of the calls made over that

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facilities-based VoIP services). Similarly, the Commission will have plenary authority to regulate the terms and conditions of wireless VoIP services provided over the LTE platform. *See Wireless Broadband Order*, 22 FCC Rcd at 5901 ¶ 1.

[150] *See* Memorandum Opinion and Order, *GTE Telephone Operating Cos., GTOC Tariff No. 1, GTOC Transmittal No. 1148*, 13 FCC Rcd 22466, 22480 ¶ 25 (1998) ("We agree that GTE's ADSL service is a special access service, thus warranting federal regulation under the 'ten percent' rule.").

[151] *Id.* at 22479 ¶ 22 ("[S]ome of the ISP traffic carried by GTE's ADSL service may be destined for intrastate or even local Internet websites or databases."). A number of parties have called for a more formal approach to allocation of the costs of DSL service. *See, e.g.*, Peter Bluhm, Lorraine Kenyon, & Dr. Robert Loube, *Separations: A White Paper to the State Members of the Federal-State Joint Board on Universal Service*, at 13-14, Appx. A (Feb. 7, 2011), http://www.naruc.org/special/Separations%20White%20Paper%202011%2002%2007.pdf (proposing to allocate cable and wire facilities that carry exclusively data and/or video as 100% interstate).

loop were *intra*state calls.[152] And both the Commission and the courts have consistently rejected the argument that such an allocation is inappropriate because it does not track consumers' actual calling patterns.[153] These cases make clear that the fact that *some* loops will continue to be used for legacy POTS service rather than broadband and VoIP is immaterial. Irrespective of the *actual* breakdown of traffic on any given line, the Commission may allocate 100% of the local loop to the interstate jurisdiction.

Were the Commission to take this step, it could preempt state regulation of last-mile infrastructure, including state legacy service obligations. The purpose of the separations process is "to determine the portions of a single asset that are used for interstate and intrastate service," and "[b]ecause the separations process literally separates costs … between interstate and intrastate service, it facilitates *the creation or recognition of distinct spheres of regulation*." *Louisiana PSC*, 476 U.S. at 369, 375 (emphasis added). Consistent with this holding, courts have allowed the Commission to preempt all state regulation of facilities that are allocated to the interstate jurisdiction. For example, the Eighth Circuit has concluded that the Commission has plenary authority to preempt any state regulation of interstate special-access links even when the

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[152] *Compare Nat'l Ass'n of Regulatory Comm'rs v. FCC*, 737 F.2d 1095, 1105 (D.C. Cir. 1984) ("*NARUC I*") (noting that the Commission had allocated "roughly 26% of the costs of local exchange plant to the interstate jurisdiction"), *with NCUC II*, 552 F.2d at 1044 n.7 ("Approximately 97% of telephone calls are intrastate."). Currently, the interstate portion of the local loop is set at 25%. Report and Order, *Jurisdictional Separations and Referral to the Federal-State Joint Board*, 25 FCC Rcd 6046, 6047-49 (2010).

[153] *See, e.g.*, *NCUC II*, 552 F.2d at 1046 ("Petitioners confuse the fact that almost all terminal equipment is and has been used predominantly for local communication, *with the statutory division of decisionmaking power*. We find it difficult to credit an argument which amounts to an assertion that Congress created a regulatory scheme that depends on the calling habits of telephone subscribers to determine the jurisdictional competence of the FCC versus state utility commissions."); *NARUC I*, 737 F.2d at 1115 (rejecting the notion that "jurisdictional significance attends an individual subscriber's decision to use its line entirely for intrastate calls," noting that "[i]t would be prohibitively complex and inefficient to have the separations formula vary from subscriber to subscriber. Any equivalent adjustment would have to be based on the totality of subscriber plant investment and expenses.").

vast majority of traffic on those links is intrastate in nature. *See Scott*, 380 F.3d at 374 (finding that, with respect to special access services, the Commission "certainly has the wherewithal to preempt state regulation in this area if it so desires," even where only 10% of the traffic on a given link is interstate).[154] The same would be true here if the Commission allocated 100% of the loop to the interstate jurisdiction.

Interim Rulemaking Authority. Finally, in addition to using the other preemption theories discussed above, the Commission should conclude that, because it will have plenary authority to regulate broadband and VoIP after the transition to an all-IP infrastructure, it should have significant discretion *during* that transition to preempt state rules that hinder deployment of the broadband facilities necessary to effect that transition.

As discussed above, the Commission has exclusive jurisdiction to regulate both broadband services and VoIP in its various forms. As these services increasingly replace POTS, the traditional role of state authorities will grow ever smaller, until the FCC is solely responsible for any regulation, within its authority, of voice services that are provided as just one of many applications over an all-IP infrastructure. To facilitate an orderly transition to this end state, the Commission is necessarily authorized to enact interim rules, including those preempting state legacy regulations that hinder the transition. Indeed, it is well-established that the Commission has expansive authority to impose reasonable transition measures to ensure a smooth transition to a new regulatory regime. *See Competitive Telecommunications Ass'n*, 309 F.3d at 14

[154] *See also id.* at 372 ("[T]he FCC has the *power* to preempt states from establishing standards and requiring reports relating to special access services.").

("Avoidance of market disruption pending broader reforms is, of course, a standard and accepted justification for a temporary rule.").[155]

Hopefully, the Commission will have no need to use any of these tools, because state policymakers will act quickly to eliminate antiquated and discriminatory service obligations. If they fail to do so, however, the Commission should preempt those obligations using the authority outlined here.

C. Legacy ETC Obligations Should Be Modified So That They Encourage, Rather Than Thwart, Broadband Deployment.

Federal ETC obligations thwart the Commission's broadband goals in essentially the same ways as state legacy service obligations.[156] And they too are inconsistent with a procurement-model approach to universal service. By modifying these ETC obligations, the Commission can immediately improve the environment for broadband investment without expending any additional universal service resources. Thus, instead of implementing a Phase 1 CAF and retaining legacy ETC obligations, as the *NPRM* proposes, the Commission should make a more dramatic and timely impact on broadband investment by adopting the relatively simple ETC changes suggested below.

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[155] *See, e.g.*, *Alenco Commc'ns, Inc. v. FCC*, 201 F.3d 608, 616 (5th Cir. 2000) ("Because the provisions under review are merely transitional, our review is especially deferential."); *TOPUC*, 183 F.3d at 440 n.85 ("[W]e extend the FCC greater discretion in deciding what will be 'sufficient' during the transition period."); *Competitive Telecomms Ass'n*, 117 F.3d at 1073-74 ("[S]ubstantial deference by courts is accorded to an agency when the issue concerns interim relief.") (quoting *MCI Telecomms.*, 750 F.2d at 140).

[156] In this Section, we discuss only legacy ETC obligations. As discussed in Section III.B.6, *infra*, the Commission should establish a separate ETC program for CAF recipients.

1. ETC Service Obligations Should Be Limited to Only Those Areas Where a Carrier Is Receiving Universal Service Support.

The Commission should modify legacy ETC obligations in two ways to keep them from impeding broadband deployment. Both of these options are within the Commission's authority to implement.

First, the Commission should reinterpret section 214(e)(1)(A) of the Act so that an ETC has an obligation to serve a given geographic area *only* when the ETC receives high-cost support for that area. Section 214(e)(1)(A) states that ETCs "shall, throughout the service area for which the designation is received [ ] offer the services *that are supported by* Federal universal service support mechanisms under section 254(c) …." 47 U.S.C. § 214(e)(1)(A) (emphasis added). The Commission has previously interpreted this provision as requiring an ETC to provide supported services *throughout its service area*, regardless of whether the ETC is receiving any high-cost support in that area. But this is not the only permissible interpretation of the statutory language. The Commission should reinterpret it to mean that a carrier's obligation to offer service applies only in those geographic areas where the carrier is receiving support—*i.e.*, where the services "are supported."[157] Under this interpretation, even if an ILEC technically is an ETC for a large "service area," its actual service obligations would be far less expansive.[158]

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[157] By contrast, where the ETC *is* receiving high-cost support, it would be required to provide the services and functionalities set forth in 47 C.F.R. § 54.101(a). Similarly, where a carrier is receiving E-rate or Rural Health Care funding, it would be required to provide the services supported by those programs to eligible customers in a manner consistent with the Commission's rules. And until the Commission creates a new Lifeline Provider service category that is separate from the ETC designation, *see* Section II.C.2, *infra*, existing ETCs would be required to continue participating in the Commission's low-income program.

[158] Such an interpretation is not only consistent with the plain language of the statute, but also with Congress's expectation and intent that, in markets opened to competition, regulators would replace implicit subsidies with explicit universal service funding. Where service providers have a positive business case to provide service without support, they will do so. Thus, limiting service obligations to only those areas where explicit support is necessary to create such a

Second, the Commission should direct the states to redefine the "service areas" of existing ETCs so that they include only those locations where the ETCs are receiving legacy support. Section 214(e)(5) states that an ETC's "'service area' means a geographic area established by a State commission … for the purpose of determining universal service obligations and support mechanisms." 47 U.S.C. § 214(e)(5). While this subsection establishes a presumption that the "service area" for a *rural* carrier is its "study area,"[159] Congress established no such presumption for a *non*-rural carrier's service area—and thus plainly envisioned that it would be *smaller* than its study area. *Id.* Consistent with this notion, the Commission in its *First Universal Service Order* encouraged states to define small service areas when designating non-rural carriers as ETCs.[160] But, despite the urging of the Commission (and the Joint Board),[161] many states have designated non-rural carriers as ETCs for their entire study areas.[162]

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positive business case not only would ensure that support is sufficient to meet universal service objectives, but also finally comply with Congress's direction that implicit subsidies be replaced by explicit universal service funding.

[159] 47 U.S.C. § 214(e)(5) ("In the case of an area served by a rural telephone company, 'service area' means such company's 'study area' unless and until the Commission and the States, after taking into account recommendations of a Federal-State Joint Board … establish a different definition of service area for such company.").

[160] 12 FCC Rcd at ¶ 116.

[161] *See* Recommended Decision, *Federal-State Joint Board on Universal Service*, 12 FCC Rcd 87, 181 ¶¶ 176-77 (1996) ("*Joint Board Recommended Decision*").

[162] In a handful of the twenty-two states where AT&T serves as an ILEC, the state commission designated AT&T as an ETC on a wire-center or exchange basis. But because AT&T is designated as an ETC in *all* of its wire centers in those states, this is a distinction without a difference—in effect, AT&T is required to serve as an ETC throughout its entire study area.

At the time, the Commission warned that this action might be unlawful because it would interfere with federal universal service goals.[163] Specifically, the Commission noted that, "if a state commission adopts as a service area for its state the existing study area of a large ILEC, this action would erect significant barriers to entry" for competitive providers, undermining universal service and potentially violating section 254(f).[164] Here too, excessively large service-area designations hinder federal policy—in this case, the deployment of broadband services by non-rural carriers. Accordingly, the Commission should deem those designations "inconsistent with the Commission's rules to preserve and advance universal service,"[165] and direct the states to redefine ETC service areas to encompass only those places where ETCs receive legacy universal service support.[166]

Section 214 does give the states discretion over various aspects of the ETC designation process. But the Commission has authority to interpret the text of section 214, and to the extent that the statutory language is ambiguous, the courts must defer.[167] That deference should be especially strong in this context, because section 254 of the Act grants the Commission broad authority to implement the entire federal universal service program, of which ETC designations

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163 *First Universal Service Order*, 12 FCC Rcd at ¶¶ 184-85.

164 *Id. See also Joint Board Recommended Decision*, 12 FCC Rcd at 181 ¶¶ 176-77 (noting that excessively large ETC service areas "could potentially violate section 254(f)" by undermining the Commission's efforts to preserve and advance universal service).

165 47 U.S.C. § 254(f).

166 Of course, after all legacy high-cost universal service funding is phased down to zero, no provider should continue to have any legacy ETC obligations. *See* Section III.B.8, *infra*, discussing the five-year phase-down in legacy high-cost support.

167 With respect to section 214 in particular, the Tenth Circuit has noted that "[t]he FCC's interpretation of the Telecommunications Act's provisions addressing state ETC designations is, of course, subject to deference." *WWC Holding*, 488 F.3d at 1273.

form only a small part.[168] The Commission recognized as much in the *Western Wireless Order*, noting that state commissions do not "have unlimited discretion" under 214(e) to adopt policies that thwart federal universal service goals, and that to conclude otherwise would "effectively undermine[] congressional intent in adopting the universal service provisions of section 254."[169]

In any event, the Commission has authority to preempt the states' ETC-designation decisions under the theories discussed above in Section II.B insofar as they violate federal policy goals. ETC obligations can have the same effect on broadband deployment as state legacy service obligations, and when imposed in the absence of explicit universal service funding, they are inconsistent with the procurement-model approach to universal service. Thus, the justifications for preempting the latter also apply to the former. Finally, the Commission also should provide inducements for the states to modify their ETC designations voluntarily. By conditioning CAF funding, the Commission can greatly increase the likelihood that states will adopt ETC policies that are consistent with the Commission's universal service goals.

2. The Commission Should Establish a Category of "Lifeline Providers" That Are Not Section 214 ETCs.

Ensuring that low-income Americans have access to essential communications services is one of the Commission's most important objectives. But the existing Lifeline/Link-Up program suffers under antiquated rules and requirements, including overly burdensome ETC obligations

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[168] As discussed above, numerous courts have held that the Commission's interpretation of section 254 is reviewable under *Chevron* step two.

[169] *Western Wireless Order*, 15 FCC Rcd at 15180 ¶ 29 ("While Congress has given the state commissions the primary responsibility under section 214(e) to designate carriers as ETCs for universal service support, we do not believe that Congress intended for the state commissions to have unlimited discretion in formulating eligibility requirements…. [W]e do not believe that Congress intended to grant to the states the authority to adopt eligibility requirements that have the effect of prohibiting the provision of service in high-cost areas by non-incumbent carriers. To do so effectively undermines congressional intent in adopting the universal service provisions of section 254.").

that discourage providers from participating. To remedy this, the Commission should establish a "Lifeline Provider" service category. A Lifeline Provider could be *any* provider of the Lifeline-supported service (currently voice and, eventually, broadband). Such providers would not be ETCs and, thus, would not be subject to the requirements of the traditional ETC designation established under section 214.

The Commission's rules couple participation in the low-income program with a service provider's designation as an ETC. *See, e.g.*, 47 C.F.R. §§ 54.401, 54.405, 54.411. But because some providers elect not to participate in the Commission's other universal service programs, these rules prevent eligible low-income consumers from purchasing what would otherwise be Lifeline-eligible services from those non-ETC providers.[170] Accordingly, AT&T has advocated in prior proceedings that the Commission establish a Lifeline Provider service category, which would enable a qualifying consumer to select any provider as his or her provider of Lifeline-supported services.[171] Permitting service providers to participate only in the Lifeline/Link-Up program, without regard to their participation in other universal service programs, could expand the base of providers to include entities that have, to date, been either unwilling to offer Lifeline service (because of the many non-Lifeline-related obligations applicable to ETCs) or unable to

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[170] *See AT&T NBP #19 Comments* at 29-30.

[171] *See, e.g.*, Comments of AT&T Inc., *High-Cost Universal Service Support; Federal-State Joint Board on Universal Services*, WC Docket 05-337, CC Docket No. 96-45, at 25-27 (filed Apr. 17, 2008) ("*AT&T April 2008 USF Comments*"); Comments of AT&T Inc., *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service; Lifeline and Link Up; Universal Service Contribution Methodology; Numbering Resource Optimization; Implementation of the Local Competition Provisions in the Telecommunications Act of 1996; Developing a Unified Intercarrier Compensation Regime; Intercarrier Compensation for ISP-Bound Traffic; IP-Enabled Services*, WC Docket No. 05-337, 03-109, 06-122, CC Docket No. 96-45, 99-200, 96-98, 01-92, 99-68, 04-36, at 53-54 (filed Nov. 26, 2008) ("*AT&T November 2008 IC/USF Comments*"); *AT&T NBP #19 Comments* at 29.

qualify under the current rules.[172] Importantly, Lifeline Providers could be non-telecommunications carriers. This would allow consumers to obtain voice service from interconnected VoIP providers and, eventually, broadband service from providers that clearly are not "telecommunications carriers."[173]

The Commission has ample authority to establish a Lifeline Provider service category under Title I of the Communications Act. Indeed, the Commission relied on its Title I authority in 1985 to establish the Lifeline program.[174] Moreover, the Commission already has approved ETC applications for the sole purpose of providing Lifeline service.[175] In doing so, the Commission has tacitly (if not explicitly) recognized: (1) that it may, through forbearance from certain requirements, authorize ETCs to participate in the low-income program without subjecting them to the full panoply of obligations associated with the high-cost program; and (2) that significant consumer benefits can be derived from expanding the Lifeline program to include non-traditional ETCs.

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172 *AT&T April 2008 USF Comments* at 26.

173 AT&T recommends that the Commission issue final Lifeline Provider rules no later than the time that it issues its final CAF rules. It is important that the Commission adhere to this schedule so that qualifying low-income consumers who reside in areas where no provider receives high-cost support (and, thus, where no provider will have an obligation to provide supported services under the new rules proposed above) will nonetheless still be able to obtain Lifeline/Link-Up service from any provider of the supported services, which may ultimately include broadband service.

174 *See 2008 IC/USF Order and FNPRM*, 24 FCC Rcd at Appx. C, 6725 ¶ 61; *AT&T April 2008 USF Comments* at 26-27. *See also First Universal Service Order*, 12 FCC Rcd at ¶¶ 329-40 (explaining that the Commission was relying on its preexisting authority under Titles I and II of the Act to modify its existing Lifeline program).

175 *See, e.g.*, Order, *Federal-State Joint Board on Universal Service, Tracfone Wireless, Inc.*, 23 FCC Rcd 6206 (2008); Order, *Virgin Mobile USA, L.P. Petition for Forbearance from 47 U.S.C. § 214(e)(1)(A); Petition for Designation as an Eligible Telecommunications Carrier*, 24 FCC Rcd 3381 (2009); Order, *i-wireless, LLC Petition for Forbearance from 47 U.S.C. § 214(e)(1)(A)*, 25 FCC Rcd 8784 (2010).

Section 254(e) poses no obstacle to establishment of Lifeline Providers. Congress made clear in section 254(j) that "[n]othing in this section," *i.e.*, section 254, "shall affect the collection, distribution, or administration of the Lifeline Assistance Program provided for by the Commission." 47 U.S.C. § 254(j). This provision clearly preserves the Commission's preexisting authority to regulate Lifeline service as it sees fit, independent of any obligations imposed on other universal service programs under the 1996 Act. In its *First Universal Service Order*, the Commission agreed, finding that "we have the authority under sections 1, 4(i), 201, 205, and 254 to extend Lifeline to include carriers other than eligible telecommunications carriers."[176] Simply put, there is no statutory impediment to the Commission establishing a category of Lifeline Providers that are not designated as ETCs under section 214. And by taking this step, the Commission can immediately enhance the effectiveness of the low-income program.

III. THE COMMISSION SHOULD ADOPT A PROCUREMENT MODEL FOR UNIVERSAL SERVICE TO ENSURE UBIQUITOUS ACCESS TO BROADBAND SERVICES.

The Commission's existing universal service regime is fundamentally broken. Although the Commission and the states provide some explicit funding to support legacy services, many providers are forced to rely primarily on rapidly eroding implicit subsidies to fund their provision of service in high-cost areas. This system is incapable of promoting universal service even with respect to POTS, and it certainly is not up to the task of ensuring that all Americans have access to broadband and IP-enabled services. The Commission should jettison this antiquated system and adopt a universal service regime that is better suited to furthering the Commission's broadband goals.

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[176] *First Universal Service Order*, 12 FCC Rcd at ¶ 369.

To that end, the Commission should not implement its proposed "Phase 1" program but should instead immediately create its final Connect America Fund, or "CAF," to provide support for the deployment and maintenance of broadband service in high-cost areas throughout the country. There is no legitimate policy reason to further delay comprehensive universal service reform, which is essentially what the Phase 1 program would do. While that program ostensibly would be narrowly targeted and streamlined, implementing it would divert significant Commission and stakeholder resources from the more important task of engineering a complete transition to the final CAF mechanism. That transition need not be complicated or lengthy. It can, and should, be achieved simply and quickly.

In the pages below, we detail AT&T's vision of what comprehensive universal service reform should look like. First, we discuss the foundational principles that the new regime should be based on. We then sketch out a Plan for how the CAF should be designed and administered. Finally, we discuss the legal issues relevant to universal service reform. In particular, we detail how the Commission has ample authority to use universal service funding to support broadband services and providers, but we also caution that the Commission does not have authority to *compel* providers to offer broadband in the absence of such support.

A. The Commission Should Base Its Universal Service Reforms on a Set of Foundational Principles.

In Section III.B below, AT&T outlines its Plan for comprehensive universal service reform. That Plan is based on several basic principles that should form the foundation for *any* universal service reforms the Commission adopts in this proceeding.

Support Should Be Distributed Through a Procurement-Model Approach. The Commission should design the CAF program around a procurement model, under which providers incur service obligations *only* to the extent they agree to them in explicit agreements

with the Commission. Under this regime, providers could not be compelled to offer broadband in high-cost areas, but would instead agree to serve those areas in exchange for a specific amount of universal service funding. Providers' service obligations would be clear from the outset and would be geographically and temporally defined. Importantly, regulators could not unilaterally abrogate the terms of the parties' agreement and force providers to bear additional obligations without their consent.

Such reforms would create certainty about the costs and benefits of participating in the Commission's broadband universal service program—and thereby encourage more providers to take part. By contrast, a heavy-handed approach that imposes unfunded mandates or evolving service obligations that become more burdensome over time would undermine the Commission's broadband goals. Providers would be far less likely to participate in the CAF program on such terms. And if fewer providers compete for funding, the winning bids for CAF support will be higher, increasing the amount of support needed to ensure that all Americans have access to broadband services. And this, in turn, will increase the burden on contributors to the CAF fund, making broadband service less affordable and undermining the Commission's *adoption* goals. In any event, even if there were policy benefits to diverging from the procurement model, imposing an unfunded mandate to provide broadband service would be unlawful, as discussed in Section III.D below.

The Commission Should Not Reform Universal Service in Stages, But Should Instead Immediately Adopt Final CAF Rules. The Commission proposes to adopt its CAF rules in two different stages: "a set of immediate reforms including … establishment of the CAF, followed by the final selection of the long-term CAF funding mechanism." *NPRM* ¶ 18; *see also, e.g.*, *id.* ¶¶ 18-33. The Commission also proposes to begin distributing funding from the Phase 1 CAF to

support broadband deployment in unserved areas. *Id.* ¶ 267. The Commission should reject these proposals. Instead, it should issue final, comprehensive CAF rules *now* that detail how the CAF will operate, then move quickly to implement those rules. If the Commission is not clear from the outset about its final rules, it will create great uncertainty about the CAF program. This uncertainty would be exacerbated by conducting a Phase 1 program under one set of rules while anticipating a future "long term" CAF program under a different set of rules. Such uncertainty will deter many providers from participating, giving rise to all of the problems discussed above. Indeed, uncertainty might *preclude* the participation of most smaller providers, which often must borrow money to finance facilities deployment. A lack of clarity about how CAF support will be distributed would make it difficult for these providers to obtain the financing they need to roll out broadband. As one party has explained, "Lenders don't lend against hypothetical costs and they don't get repaid in hypothetical dollars."[177]

The CAF Should Be Sized Appropriately to Achieve the Commission's Broadband Goals. The CAF should be large enough to enable providers to deploy broadband service to *all* Americans. Indeed, adequate funding is required by sections 254(b)(5) and 254(e), which provide that support must be "sufficient" to preserve and advance universal service. 47 U.S.C. §§ 254(b), (e). At the same time, a fund that is too large would undermine the Commission's broadband goals. We anticipate that the CAF eventually will be financed by contributions from consumers of broadband and other communications services. And an excessively large fund

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[177] Comments of CoBank, ACB, *Connect America Fund; A National Broadband Plan for Our Future; High-Cost Universal Service Support*, WC Docket Nos. 10-90 & 05-337, GN Docket No. 09-51, at 5 (filed July 12, 2010). Joint Reply of NECA, NTCA, OPASTCO, WTA and the Rural Alliance, *Connect America Fund; A National Broadband Plan for Our Future; High-Cost Universal Service Support*, WC Docket Nos. 10-90 & 05-337, GN Docket No. 09-51, at i (filed Aug. 11, 2010) ("Already, uncertainty caused by the NOI and NPRM has begun to cause RLEC financing for broadband investment to dry up.").

would unnecessarily burden those contributors, making broadband service less affordable and undermining the Commission's adoption goals.

To promote both *access to* and *adoption of* broadband services, the Commission should take steps to ensure that the CAF is only as large as necessary to effect ubiquitous broadband deployment. For example, the Commission should permit CAF recipients to fulfill their service requirements in some particularly high-cost areas using satellite broadband service. Because, as discussed below, the 250,000 highest-cost households in the U.S. account for more than half of the $24 billion price tag for ubiquitous broadband deployment,[178] serving such customers with satellite is the best way to ensure that all Americans have access to broadband without ballooning the size of the fund so much that consumers cannot afford it.

The Commission Should Ensure That All Americans Have Access to Mobile Wireless Broadband Service. As AT&T has detailed elsewhere (and as the *NPRM* recognizes), mobile communications services offer many unique benefits to consumers.[179] Citing such benefits, the Joint Board has determined that "mobility" is "a fundamental necessity for an overwhelming

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[178] FCC, *The Broadband Availability Gap*: OBI Technical Paper No. 1, at 5 (Apr. 2010), http://download.broadband.gov/plan/the-broadband-availability-gap-obi-technical-paper-no-1.pdf ("*Broadband Availability Gap Paper*"); *National Broadband Plan* at 136.

[179] *See NPRM* ¶ 4 (noting that the "benefits of mobility may be particularly important to rural consumers and schoolchildren who typically travel farther distances to reach work and school, and are vital for public safety"); *see also, e.g.*, *AT&T National Broadband Plan Comments* at 128-29 (noting that "mobile broadband services complement the way Americans increasingly live and communicate"); *AT&T Net Neutrality Comments* at 180-81 (describing applications such as wireless e-book access, "wireless automobile diagnostic repair and roadside assistance service that AT&T offers together with an automobile company, [] 3G-enabled GPS products that AT&T [] offer[s] to small businesses in partnership with a GPS device maker, [and] various wireless healthcare, Smart Grid, and other machine-to-machine devices and applications"); Reply Comments of AT&T Inc., *Preserving the Open Internet; Broadband Industry Practices*, GN Docket No. 09-191, WC Docket No. 07-52, at 98 (filed Apr. 26, 2010) ("No area of the broadband ecosystem holds more promise for transformational innovation than mobile.") (quoting Prepared Remarks of Chairman Julius Genachowski, FCC, New America Foundation, *Mobile Broadband: A 21st Century Plan for U.S. Competitiveness, Innovation and Job Creation*, Washington, D.C., at 3 (Feb. 24, 2010)).

majority of consumers for public health, safety, and economic development."[180] Indeed, the Joint Board has concluded that "mobility" should be a universal service priority in its own right: "mobility satisfies the statutory requirements for inclusion as a separately supported service and should no longer be eligible for support because it happens to satisfy requirements designed for wireline voice communications." *Id*. at ¶ 63. The Commission should adopt and extend that same analysis to mobile wireless broadband service and conclude that universal service funds should be used to support deployment of mobile wireless broadband services.

The Commission Should Firmly Ground Its Universal Service Reforms in Section 254(b) of the Act. For years, the Commission has unsuccessfully defended its high-cost universal service mechanism for so-called "non-rural" carriers.[181] That mechanism was generated through a results-driven process that focused solely on minimizing the size of the fund; the Commission ignored its statutory obligation to promote the other principles articulated in section 254(b). *See, e.g.*, *Qwest I*, 258 F.3d at 1200-03 (holding that the "language [of 254(b)] indicates a mandatory duty on the FCC" and faulting the Commission for failing to explain how its universal service regime was consistent with those statutory principles). To avoid a repeat of history, the Commission should ensure that its CAF mechanism furthers *all* of the relevant principles in section 254(b). Moreover, in its final order adopting the CAF rules, the Commission should clearly *explain* how its new broadband-focused mechanism furthers those principles.

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[180] Recommended Decision, *Federal-State Joint Board on Universal Service*, CC Docket No. 96-45, FCC 07J-4, at ¶ 64 (rel. Nov. 20, 2007).

[181] *See Qwest I*, 258 F.3d at 1200-03; *Qwest II*, 398 F.3d 1222.

B. The Commission Should Provide Explicit Universal Service Support to Promote Broadband Deployment.

AT&T proposes that the Commission adopt the following Plan for the design and administration of the CAF. This Plan is consistent with all of the foundational principles discussed above.

1. Brief Overview of Key Plan Components.

The first step in designing a broadband universal service mechanism is deciding what minimum characteristics the service supported by that mechanism should have. In defining the meaning of "broadband" for purposes of the CAF,[182] the Commission should not fixate on throughput and ignore other important broadband characteristics such as latency, jitter, packet loss, security, and reliability. Instead, the Commission should adopt a consumer- and application-focused definition that encompasses all of the service characteristics necessary to support the applications that consumers *actually use* today and are likely to use in the near future.[183] In addition, the Commission should acknowledge that there is a fundamental trade-off between the *speed* of broadband services and the number of *people* to whom those services can be cost-effectively deployed. In short, rather than focusing on the definition of "broadband" in a vacuum, the Commission should adopt a service definition that is consistent with what consumers need.

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[182] As the Commission has acknowledged in many contexts, a wide variety of services should be considered "broadband" services. Indeed, "[a]t present, the Commission categorizes connections reported through its FCC Form 477 at 72 speed tiers defined by eight ranges of downstream speed and nine ranges of upstream speed." *NPRM* ¶ 108 n.182. In this proceeding, the Commission need not, and should not, adopt a "universal" definition of broadband. To the contrary, the Commission should continue using context-specific definitions that view the term expansively in some contexts and narrowly in others. For ease of reading, however, in these comments we frequently refer to the service supported by the CAF mechanism as "broadband" service.

[183] The definition of the "broadband" service supported by the CAF may be different from the definition used for purposes of the Advanced Mobility Fund.

The next step is identifying the geographic areas where funding is needed to ensure that consumers have access to the level of "broadband" service supported by the CAF. AT&T proposes that the CAF mechanism support both the *deployment* of broadband infrastructure and the *maintenance* of broadband service in certain high-cost areas. The Commission should identify high-cost areas on a census-block basis using a Commission model that calculates the costs of providing service throughout the country and, for each census block, determines whether the costs of providing broadband service exceed a high-cost benchmark. High-cost census blocks should be eligible for CAF funding (*i.e.*, "CAF-eligible") if no non-ETC provider offers fixed "broadband" service there. The Commission's preliminary identification of such areas should not be final; instead, providers should be entitled to challenge the designation of each census block as "CAF-eligible."

After concluding that a given census block is eligible for support, the Commission should select a *single* fixed broadband provider to receive funding there. As a first step, the Commission should examine every wire center containing CAF-eligible census blocks and identify those wire centers where a current ETC already is offering fixed broadband service to more than a certain percentage (such as 50%) of the housing units there.[184] In those wire centers, the qualifying broadband provider should be offered a "right of first refusal" that entitles it to designation as the CAF ETC in the wire-center's CAF-eligible census blocks in exchange for the amount of support that the Commission's model calculates is necessary to provide service in those census blocks.

[184] Importantly, for purposes of this calculation, the Commission should apply an expansive definition of broadband rather than the formal "broadband" definition that it uses to describe the service supported by the CAF mechanism.

Only after the existing provider has rejected this offer should the CAF-eligible census blocks in that wire center be subject to the second phase, a competitive, application-based process. This process should be open to any provider offering a fixed "broadband" service, including one that declined a right of first refusal. Broadband providers should submit applications to serve the census blocks of their choice, and the Commission, in concert with the states, should prioritize those applications based on the price bid per housing unit served.

Each provider that prevails in this competitive funding-allocation process (or that exercises a right of first refusal) should be required to apply for designation as a CAF ETC in all of the census blocks where it has been selected as the CAF funding recipient. If the provider's application satisfies the relevant requirements, the Commission should designate that provider as a CAF ETC in *all* of the census blocks for which it is receiving CAF support, and *only* in those census blocks.

As soon as the Commission issues its final CAF rules, it should begin phasing down all legacy high-cost support and transitioning that funding to the CAF. This transition should be completed in five years—though the phase-down period may be shorter for some legacy ETCs, depending on the amount of CAF support they qualify for.

Finally, the Commission also should create a separate Advanced Mobility Fund within the CAF to support mobile wireless broadband services. As legacy high-cost support for CETCs is phased down, that funding should be transitioned to the Advanced Mobility Fund. Any support that remains after funding is distributed to mobile providers could be repurposed to the broader CAF. Indeed, this fund could be quite small, because wireless providers are already deploying broadband service in nearly every part of the country, largely without any universal

service support. Support from this fund should be allocated in much the same way as funding from the CAF.

In the sections that follow, we discuss in greater detail each of the Plan elements outlined above.

2. Defining the Services Supported by the CAF Program.

The objective of the Connect America Fund is making "broadband" service available throughout the nation. To design a funding mechanism that achieves this objective, the Commission must first identify the characteristics of the service that it will define as "broadband" for purposes of the CAF.[185]

The *NPRM* proposes a definition based exclusively on throughput. Specifically, it would define "broadband" as an Internet access service that provides throughput of 4 Mbps downstream and 1 Mbps upstream. *NPRM* ¶ 109. As AT&T has explained in other contexts, such a throughput-based definition places excessive weight on the speed of a broadband connection, to the exclusion of other important considerations.[186] Instead, the Commission should adopt a more holistic, application-based definition of broadband that views throughput as just one of many different service characteristics, among them jitter, latency, packet loss, security, and reliability.[187] To strike the appropriate balance among these many factors, the Commission should analyze the *actual uses* to which consumers put their Internet connections—and then

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[185] As discussed above, "broadband" is an expansive concept, and the Commission should continue to apply a context-specific definition in other proceedings. In this Section, we discuss *only* the definition of the specific service to be supported by the CAF mechanism.

[186] *See* Comments of AT&T, Inc., *A National Broadband Plan for Our Future, NBP Public Notice #1*, GN Docket Nos. 09-51, 09-47, 09-137 (filed Aug. 31, 2009) ("*AT&T NBP #1 Comments*"); *AT&T National Broadband Plan Comments* at 12-21.

[187] *AT&T National Broadband Plan Comments* at 15-17; *AT&T NBP #1 Comments* at 5.

define broadband to encompass *all* of the service characteristics needed to support the applications that consumers frequently use today and are likely to use in the near future.

Indeed, even with respect to throughput, the Commission should not set an arbitrary threshold in the abstract. Rather, it should analyze consumers' broadband consumption patterns and use that data to inform its view of the minimum throughput needed to meet consumers' current and future broadband needs. An excessively aspirational speed goal would deny federal support to broadband services that are perfectly sufficient for the *actual* needs of consumers. And embracing a broadband funding strategy that has no relation to actual user needs or marketplace demand would not only violate section 254,[188] but also undermine the Commission's broadband *adoption* goals by requiring providers to deploy fast connections that consumers do not require—and cannot afford.[189]

Finally, because CAF support will be limited, the Commission should consider that there is a basic trade-off between services with the highest *speeds* and services capable of reaching the most *people*. Consumer groups have urged the Commission to recognize this, arguing that "maximum coverage should be the goal, rather than chas[ing] a gold-plated network that will restrict the number of households that can be reached in the near future. We need to get people connected for basic communications that open[] the door to economic and civic participation in cyberspace."[190] For Americans who lack access to broadband, their pressing concern is not obtaining the ability to engage in real-time, two-way gaming, but rather gaining meaningful

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[188] As discussed below, Congress instructed the Commission to direct universal service funding to those services that are subscribed to by "a substantial majority of residential customers." 47 U.S.C. § 254(c)(1)(B)

[189] *See AT&T National Broadband Plan Comments* at 17-18; *AT&T NBP #1 Comments* at 3.

[190] Comments of the Consumer Federation of America and Consumers Union, *Report on Rural Broadband Strategy*, GN Docket No. 09-29, at 3 (filed March 25, 2009).

access to the Internet's resources and to reliable email communications and other basic tools that consumers in other parts of the country take for granted. Fulfilling *that* need is the appropriate national priority at this time. Granted, the Commission should also look for ways to promote deployment of more sophisticated, higher-speed and lower-latency services. But for purposes of the CAF program, the Commission should adopt a definition of "broadband" that embraces services that can be deployed cost-effectively in areas that, to date, have been unable to support deployment of *any* type of broadband service.

With these principles in mind, we turn to the Commission's proposed 4/1 Mbps threshold. Not only does it ignore all but one of the broadband characteristics discussed above, it is overly ambitious with respect to throughput. Congress directed the Commission to consider, in defining universal service, the extent to which a service has, "through the operation of market choices by customers, been subscribed to by a substantial majority of residential customers." 47 U.S.C. § 254(c)(1)(B). Today, a "substantial majority of residential customers" subscribes to slower Internet connections. As the Commission noted in its most recent status report on Internet access services, nearly 70% of reportable connections would not meet the 4/1 Mbps threshold.[191]

Furthermore, adoption of a 4/1 Mbps threshold would unnecessarily increase the size of the CAF. The Commission has sought comment on whether "adopting a slightly lower threshold … [would] lessen the financial impact on USF." *NPRM* ¶ 110. The answer is clearly yes. Even if the Commission were to retain its 4 Mbps downstream threshold, modestly reducing the upstream threshold would dramatically reduce the amount of funding necessary to ensure

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[191] *FCC Local Telephone Competition Report* at 6, 2 n.4 ("69% of reportable Internet access service connections (or 106.2 million connections) in June 2010 were too slow in both the downstream and upstream directions, or too slow in a single direction, to meet the broadband availability benchmark" of 4/1 Mbps).

ubiquitous "broadband" deployment. Although AT&T is still analyzing the relationship between fund size and throughput, a preliminary analysis using a modified version of the Commission's existing cost proxy model to reflect broadband characteristics[192] reveals that ILECs would require about *50 percent more* support to provide service at 4/1 Mbps than at 4 Mbps downstream and 768 kbps upstream.[193] And adopting a threshold of 3 Mbps downstream and 768 kbps upstream would reduce costs even more, ensuring faster and more efficient deployment of service to households in high-cost areas. The Commission should carefully consider these trade-offs before adopting its proposed throughput standard, as a more modest threshold would reduce the size of the CAF, and thus the burden on the broadband customers who, we anticipate, will contribute to the fund.

Regardless of what throughput standard the Commission adopts, it should not require "that the speed be 'actual' speed rather than the 'advertised' or 'up to' speed." *NPRM* ¶ 113. Today, providers do not sell broadband service at an "actual" speed to consumers. Indeed, no definition of "actual" speed exists, as the *NPRM* recognizes when it seeks comment on "how to define 'actual' speed." *Id.* There is a good reason for this:

> Because actual speeds depend on factors beyond the broadband provider's knowledge or control, and thus are likely to vary from website to website and from hour to hour, predictions of actual throughput run the risk of being unreliable and confusing. By contrast, the standard industry practice of describing maximum performance capabilities … enables consumers to make apples-to-apples assessments regarding relative performance of a provider's service, irrespective of the fact that real-world conditions may make it difficult to achieve those maximum capabilities in certain circumstances[.][194]

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192 *See* FCC, *Universal Service - Hybrid Cost Proxy Model*, http://www.fcc.gov/wcb/tapd/hcpm/welcome.html.

193 This calculation assumes that costs above a benchmark of $40 would be supported.

194 Reply Comments of Time Warner Cable, Inc., *Consumer Information and Disclosure; Truth-in-Billing and Billing Format; IP-Enabled Services*, CG Docket No. 09-158, CC Docket No. 98-170, WC Docket No. 04-36, at 3 (filed Oct. 28, 2009).

Many factors on the customer's side of a broadband connection can make "actual" speed an unreliable measure, including customer-owned inside wiring.[195] Other such factors include "the presence of viruses, automatic updating, low memory capacity, processor capabilities, the type and capabilities of the operating system, the version and configuration of the web browser software used," as well as "factors specific to a subscriber's household network," including "the presence and capabilities of a router, whether several computers or other devices are accessing the Internet simultaneously, … whether other devices, such as cordless phones … are in use which may cause interference with WiFi devices, the distance from the consumer's computer to the WiFi access point, [and] whether and what type of WiFi encryption is used."[196] Given these issues, the Commission should accept the prevailing industry practice and allow broadband providers to use "up to" or "advertised" speeds when offering broadband service to consumers.

The Commission also seeks comment on how a provider's compliance with a speed threshold should be tested or audited. *NPRM* ¶¶ 115-18. The Commission should use the same testing methodology that it ultimately adopts in other proceedings where this issue has been teed up for some time.[197] Specifically, the Commission should continue to work with its third-party

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[195] *NPRM* ¶ 118 (discussing customer-side "choke points"); *id.* at ¶ 117, Figs. 4, 5 (illustrating how the "[c]onsumer device [is] connected to [a] modem through internal wire").

[196] Comments of the National Cable & Telecommunications Association on NBP Public Notice #24, *Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996, as amended by the Broadband Data Improvement Act; A National Broadband Plan For Our Future; International Comparison and Survey Requirements in the Broadband Data Improvement Act*, GN Docket Nos. 09-137, 09-47, 09-51, at 8 (filed Dec. 14, 2009).

[197] To expedite broadband deployment, a provider's technology could be tested and certified as meeting this minimum standard, and all subsequent deployments made using that technology could be presumed to comply with the minimum standard. This presumption could be rebutted using the hardware-based testing methodology discussed in the text. Requiring broadband providers to test (and report on) every single broadband connection would consume considerable resources that could be much better spent on broadband deployment.

measurement company, SamKnows, to develop a hardware-based testing methodology, and use that methodology to evaluate the sufficiency of broadband services provided by CAF recipients.[198] Such an approach would have the benefit of consistency. The Commission also might consider giving the states a role in auditing broadband providers' compliance in offering "broadband" services.[199]

Finally, the Commission seeks comment on how often it should revisit any speed threshold included in its definition of "broadband." *NPRM* ¶ 119. Although the Commission should periodically reassess its minimum standards for CAF-supported services, frequent changes to the "broadband" definition could undermine the stability of the CAF program. In any event, the Commission's revised broadband definitions should apply only prospectively, to new distributions of CAF funding. As discussed above, requiring existing providers to meet new, higher standards without additional funding would contravene the procurement-model approach to universal service. Instead, the terms of service for existing CAF recipients should change *only* if recipients agree to increased support in return for meeting a higher broadband standard.[200]

3. Identification of Geographic Areas Eligible for CAF Support.

After defining the services that qualify as "broadband" for purposes of the CAF mechanism, the Commission should identify those areas of the country where Americans will not

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198 *See, e.g.*, Public Notice, *Comment Sought on Residential Fixed Broadband Services Testing and Measurement Solution*, 25 FCC Rcd 3836 (2010).

199 Although state commissions could play an important role in investigating providers' compliance with federally mandated obligations, they should have no role in imposing penalties on a CAF recipient that fails to comply with those obligations. *See NPRM* ¶¶ 153, 155.

200 Thus, the Commission should not require CAF recipients "to meet an evolving speed requirement, post-award, to account for changes in technology and consumer demand over time." *NPRM* ¶ 312.

have access to "broadband" service absent government support. It is to those areas that the Commission should direct CAF funding.

The Commission should adopt a cost model to identify, on a census-block basis, the areas of the country that are most expensive to serve. Specifically, the Commission should analyze the characteristics of each census block to determine the cost per housing unit of serving the census block.[201] If that cost exceeds a certain benchmark, the census block should be deemed "high cost." High-cost census blocks should be eligible for CAF funding (*i.e.*, "CAF-eligible") unless a non-ETC provider already offers fixed "broadband" service there.[202]

To identify those census blocks where a non-ETC provides "fixed" broadband service, the Commission could look to publicly available data sources, such as the Commission's own Form 477 data, NTIA's coverage maps, Centris data, and third-party data sources. *See NPRM* ¶ 269. To further refine this analysis, the Commission should permit providers to challenge the preliminary designation of an area as CAF-eligible, or vice versa. This "challenge" procedure should enable providers to demonstrate that a given census block is, or is not, already served by a non-ETC broadband provider. In addition, because it makes no sense to award support to a new provider in an area where an existing provider will soon deploy broadband service without CAF

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[201] Cost per housing unit should be derived using the lowest-cost technology for providing fixed "broadband" as that term is defined by the Commission.

[202] To ensure that CAF funding is targeted to those areas where it will generate the greatest benefits, the Commission might consider distinguishing between two types of areas where "broadband" service is not provided: unserved areas and underserved areas. Unserved areas are those where no provider currently offers *any* form of broadband service. Underserved areas are those where a provider offers service that would be considered broadband under the ordinary meaning of that term, but that service fails to meet the technical definition of "broadband" that the Commission adopts for purposes of the CAF program. (For example, the service might supply lower throughput or higher latency than the Commission specifies in its formal broadband definition.) If the Commission's model reveals that there will be insufficient CAF funding to support deployment of the Commission's definition of "broadband" throughout both types of areas, the Commission should consider prioritizing truly "unserved" areas over "underserved" areas in its funding-allocation process.

funding, the challenge procedure should allow providers to certify that they plan to deploy service in a given census block. The Commission should ask state public utility commissions—which are familiar with the providers and the services offered within their states—to evaluate these challenge claims within a specific period of time and report their findings to the Commission. After this process is complete, those high-cost census blocks that survive the challenge procedure should be designated as "CAF-eligible areas."[203]

4. Right of First Refusal for Existing Fixed Broadband Providers.

After determining which *areas* are eligible for CAF support, the Commission will need to determine which broadband *providers* should receive support. That analysis should be conducted in two phases. In the first, the Commission should give certain existing broadband providers an opportunity to be the CAF ETC in specific areas in exchange for a specific amount of funding (*i.e.*, the provider should be granted a "right of first refusal").[204] Only after the existing provider has rejected this offer should those areas be subject to the second phase, a competitive award procedure.

Specifically, the right of first refusal should be granted to any current ETC in a particular wire center that is already offering fixed broadband service to more than a certain percentage (such as 50%) of the housing units in that wire center.[205] That provider should be given the opportunity to be the CAF ETC for the CAF-eligible census blocks in that wire center in

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[203] The Commission has proposed limiting eligibility for the CAF program to states that have undertaken access-charge reform. *NPRM* ¶¶ 297, 321. If the Commission takes this step, it should publish the list of eligible states *before* commencing the CAF process so that providers do not waste time preparing applications for areas that ultimately will be ineligible for funding.

[204] *See NPRM* ¶ 31.

[205] For purposes of this threshold calculation alone, the Commission should apply an inclusive definition of broadband service rather than the more specific "broadband" definition that it uses to determine whether a service meets the requirements for CAF funding.

exchange for the amount of support that the Commission's model calculates is necessary for serving those census blocks. The provider should be required to deploy service in accordance with the same timelines and rules applicable to all other providers receiving CAF funding. *See* Section III.B.6, *infra.*

This two-phase approach makes sense because an existing broadband provider's costs of upgrading and extending service to nearby areas will generally be far lower than the costs that a new broadband provider would incur to deploy comparable service there. Established providers can leverage their existing facilities, including, in many cases, last-mile facilities where the provider serves as a local exchange carrier. And as discussed, the Commission should ensure that broadband service is deployed as efficiently as possible to reduce the size of the CAF and thereby increase broadband adoption.

If the existing broadband provider declines to exercise its right of first refusal, the CAF-eligible census blocks in that wire center should become available for the second, competitive phase of the funding-allocation process, as discussed in the next Section.

5. Competitive, Application-Based Funding-Allocation Process.

For all CAF-eligible census blocks where no broadband provider exercises a right of first refusal, CAF funding should be allocated through a competitive, application-based process. That process should be open to any fixed broadband provider.

Each participant in the competitive process should submit an application to provide service in a specific area composed of the census blocks of its choice. The Commission, in concert with the states, should evaluate these applications and select *one* fixed provider in each area to receive CAF funding. All applicants should be subject to the same build-out, service, and other CAF ETC obligations discussed below in Section III.B.6.

The Commission should require each provider to specify in its application the amount of CAF funding that it deems necessary to serve all of the CAF-eligible census blocks encompassed by its application. The Commission should then divide that sum by the number of housing units that would be served if the provider's application were granted. Finally, the Commission should prioritize the applications based on the price proposed per housing unit.[206]

AT&T strongly believes that such an application-based process is the best method of allocating CAF support. If, however, the Commission nevertheless decides to employ a reverse-auction-based process, *see NPRM* ¶¶ 324-71, AT&T offers the following refinements to the Commission's proposed auction mechanism. First, as described in more detail below, submission of an ETC application should not be a prerequisite to participation in the auction, and the eventual ETC designation should be granted by the Commission, not a state PUC.[207] Second, the Commission should not establish auction reserve prices or maximum opening bids. *See NPRM* ¶ 342. By its very nature, an auction presumes that the auctioneer (the Commission) does not know the minimum cost of providing service in a given area. Setting either of these amounts, therefore, could send inappropriate signals to bidders and undermine the efficiency of the auction.[208] Third, the Commission should not require auction winners to detail how they spend their CAF support. *See NPRM* ¶ 369. Such a requirement would impose significant administrative burdens on CAF recipients with no offsetting benefit, because the only relevant

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[206] If no provider applies to serve a given census block, the Commission could place that census block on a slower track for funding and could consider offering more than the model-generated support amount (*e.g.*, 10% more, then 20% more, then 30% more) until a broadband provider applies for CAF support there.

[207] *Compare NPRM* ¶ 352 *with* Section III.B.6, *infra*.

[208] *See* Comments of AT&T, Inc., *Universal Service Reform, Mobility Fund*, WT Docket No. 10-208, at 18-19 (filed Dec. 16, 2010) ("*AT&T Mobility Fund Comments*").

metric is whether the recipient actually satisfies its service obligations.[209] Finally, the Commission should require bidders not only to designate on their pre-auction "short forms" the areas they propose to serve, but also to certify that their service will meet the Commission's minimum throughput and quality thresholds. *See NPRM* ¶¶ 326-30. The Commission will need such information to adequately evaluate the submitted bids.

6. Commission Evaluation of CAF ETC Applications.

Each provider that prevails in the competitive funding-allocation process discussed above, or that exercises a right of first refusal, should be required to apply for designation as a CAF ETC. The Commission should designate that provider as a CAF ETC in *all* of the census blocks for which it is awarded CAF support, and *only* in those census blocks.[210]

Timing and Mechanics of the ETC Designation Process. Any provider that is selected as the CAF recipient in a given area should have a certain number of days (*e.g.*, 60) to submit an application for designation as the CAF ETC there. If the provider fails to file an ETC application within that time period, or if the Commission denies the provider's application, that provider should not receive CAF funding. Instead, the Commission should select another provider, and that provider should be required to submit a CAF ETC application within 60 days (or whatever time period the Commission deems appropriate).

Requiring broadband providers to apply for ETC status only *after* their bids are accepted would ensure that providers do not "find[] themselves designated [as ETCs], and subject to the

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[209] *AT&T Mobility Fund Comments* at 20-21. As a safeguard, the Commission could require CAF recipients to file a letter each year certifying that they are using their support for the intended purpose, consistent with section 254(e). The Commission requires IAS recipients to make these same certifications directly to the Commission on an annual basis. *See* 47 C.F.R. § 54.809.

[210] Providers should be relieved of their CAF ETC designations (and thus their broadband service obligations) upon expiration of the term of their agreement with the Commission to provide broadband service.

obligations that go along with being designated, in areas where they do not win support." *NPRM* ¶ 319. Alternatively, the Commission could require providers to file ETC applications when they apply for CAF funding, but deny the applications to the extent they encompass areas where the provider is not selected as the funding recipient. This would enable the Commission to evaluate funding and ETC applications at the same time. If there are deficiencies in the ETC application, the Commission could require corrections within 10 days (or some other brief period of time) or, if the deficiencies cannot be corrected, select another funding applicant.

Regardless of the procedure used, broadband providers should be designated as CAF ETCs *only* in those census blocks for which they actually receive CAF funding. Any other result would be inconsistent with the procurement-model approach to universal service. And, as discussed above, diverging from that approach would undermine the Commission's broadband goals. *See* Sections II.B and III.A, *supra.*

Required Service Offerings. To receive CAF funding, providers should be required to offer "broadband" service that conforms to the Commission's definition. Each provider should certify in its ETC application that it will comply with this requirement.

The Commission should, however, recognize a limited exception for the highest-cost census blocks in the United States. As the Commission noted in connection with the *National Broadband Plan*, a mere "250,000 housing units account for $13.4 billion of the total $23.5 billion" in investment that will be necessary to bring wireline broadband service to all Americans.[211] In other words, it would cost an average of $53,600 to deploy broadband service to *each* of these customers. Such astronomical deployment costs cannot be justified given the limited amount of CAF funding available. Accordingly, for the highest-cost census blocks in the

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[211] *Broadband Availability Gap Paper* at 5.

country, the Commission should permit CAF participants to satisfy their broadband service commitments via satellite. The Commission should identify these satellite-eligible census blocks using its cost model and make this information available to providers before the CAF application deadline.[212]

CAF ETCs also should be required to supply access to voice services. Most broadband providers will choose to offer VoIP service to their customers, but this should not be a condition for receipt of CAF funding. Instead, the Commission should conclude that this criterion is satisfied so long as broadband customers have access to over-the-top VoIP services.[213] Moreover, the Commission should not require CAF ETCs to offer voice services on a stand-alone basis. *Cf. NPRM* ¶ 99. Competition will ensure that all customers have multiple options for voice service. In its recent report on local competition, the Commission determined that, as of June 2010, 88% of U.S. households were located in zip codes where *ten or more* CLEC or non-ILEC VoIP providers are offering service.[214] Importantly, these data do not even count

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[212] It is premature to establish any threshold for the housing units that should be served by satellite. Instead, this threshold should be set after the Commission and the industry review the results of the cost model and the projections for the overall size of the CAF.

[213] A broadband connection that provides a downlink/uplink throughput of 3 Mbps / 768 kbps would be more than sufficient to permit customers to access voice services through an over-the-top VoIP provider. *See, e.g.*, Vonage, *Vonage Support – Is Your Internet Speed Fast Enough?*, http://support.vonage.com/doc/en_us/497.xml ("Vonage recommends minimum upload speed of 90 kilobytes per second or greater per phone line to attain the highest audio quality," but customers can adjust their "Vonage sound quality to the very efficient 30 kbps (kilobits per second) normal level, [and] still maintain excellent sound quality while saving bandwidth"); Skype, *Help for Skype: How much bandwidth does Skype need?*, https://support.skype.com/en_US/faq/FA1417/How-much-bandwidth-does-Skype-need;jsessionid=38552A96629632BD4140F9FDA8A69443 (requiring a minimum upload/download of 30/30 kbps and recommending 100/100 kbps for voice calling).

[214] *FCC Local Telephone Competition Report* at 29 (Table 19). Similarly, in its recent *Lifeline NPRM*, the Commission noted: "Today, most low-income households have a choice of voice service from one or more wireline providers and potentially multiple mobile wireless providers." *Lifeline NPRM*, 26 FCC Rcd at 2788 ¶ 50 & n.86.

mobile providers; in that same report, the Commission noted that 279 million Americans subscribe to mobile telephony. *Id.* at 28 (Table 17). And in its *Fourteenth CMRS Competition Report*, the Commission found that "[a]pproximately 281 million people, or 98.6 percent of the population, are served by at least two mobile voice providers" and "[a]pproximately 273 million people, or 95.8 percent of the population, are served by at least three mobile voice providers."[215] In any event, requiring broadband providers to offer standalone voice service is more likely to harm consumers than help them, as it would deter broadband providers from participating in the CAF program. And a standalone voice requirement is nonsensical in a world where, as the Commission recognizes, voice is just one "application" among many provided over a broadband connection.

Most importantly, when a CAF ETC *does* offer voice service, it should not be subject to the antiquated regulatory obligations that apply to legacy voice services. In the *NPRM*, the Commission proposes retaining the federal "voice telephony service" obligations that apply to existing ETCs. *NPRM* ¶¶ 95-98; *see* 47 C.F.R. § 54.101(a) (listing service obligations for voice ETCs). Even worse, the Commission has proposed retaining legacy *state* obligations for voice ETCs. *NPRM* ¶ 100.[216] But as discussed above, many of these obligations presume that voice service is provided using circuit-switched, TDM technology, and thus it makes no sense to apply

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215 *Fourteenth CMRS Competition Report*, 25 FCC Rcd at 11413 ¶ 4.

216 These obligations vary widely from state to state and often are inconsistent across states. Examples include specific outage reporting requirements, expenditure plans, back-up power requirements, and mandates to offer "basic" service plans that provide a specified amount of included usage. *See, e.g.*, Order, *Eligible Telecommunications Carrier Designation for Federal Universal Service Support*, Docket No. 05-AD-662, Ex. A, ETC Checklist §§ I.A.1.(d), II.A.1 (Miss. Pub. Serv. Comm'n Apr. 6, 2007) (establishing one-year expenditure plan); 3 Alaska Admin. Code § 53.410(a)(14)(A) (requiring calling plan with at least 500 free minutes of local usage per month). This lack of uniformity increases the costs of compliance and discourages providers from seeking designation as an ETC.

them to VoIP calls that never transit the PSTN.[217] In addition, the Commission seeks comment on other legacy "service requirements" that might be imposed on CAF recipients. *See NPRM* ¶¶ 125-28. These requirements, which govern such topics as line extensions and exit conditions, constitute common-carrier regulation. And for the reasons discussed above, such common-carrier regulation of VoIP services is not only unnecessary, but would be affirmatively harmful to consumers.[218] Moreover, such obligations would deter providers from participating in the CAF program, with all of the negative consequences detailed above.

Coverage Commitments. Each CAF participant should be required to certify that it will provide broadband service to *all* housing units in the census blocks where it has been awarded funding. Further, each participant should commit to fully deploying service within the time period established by the Commission for such deployment, and to continue providing service in those census blocks for a defined period of years thereafter.[219]

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[217] *See* Section II.A, *supra*. As discussed above, state-level obligations require providers to offer such services as local dial tone service, rotary pulse dialing operability, dual-tone multi-frequency signaling, single-party service, SS7 signaling, and single-party revertive calling. And federal-level obligations impose many of the same requirements. In addition, these obligations would require broadband providers to offer a voice service that includes "access to interexchange voice," which the FCC has previously interpreted as possibly meaning equal access, *i.e.*, "the ability to access the presubscribed long distance carrier of the customer's choice by dialing 1+ the phone number." Report and Order, *Federal-State Joint Board on Universal Service*, 20 FCC Rcd 6371, 6386 ¶ 35 n.90 (2005).

[218] *See* Section I.B.3, *supra* (discussing the need for a minimally regulatory end state for VoIP services).

[219] The Commission should not adopt a waiver process that allows some providers "more time to come into compliance with the[ir] obligations." *NPRM* ¶ 154. Such a process would be fundamentally unfair to losing bidders whose CAF funding demands were based on the support necessary to deploy service within the time period designated by the Commission. And a waiver procedure could create significant problems and inefficiencies, as the Commission's experience with the Rural Health Care Pilot Program demonstrates. There, many program participants are requesting more funding years after applying for and being selected to receive an applicant-defined amount of support; seeking more time to complete certain milestones; and requesting that the Commission extend the life of the pilot program. *See, e.g.*, Public Notice, *Wireline Competition Bureau Seeks Comment on Requests by the California Telehealth Network and the*

Today, a legacy ETC can satisfy its service obligations "either using its own facilities or a combination of its own facilities and resale of another carrier's services[.]" 47 U.S.C. § 214(e)(1)(A). The same should be true of CAF ETCs. Further, the Commission should not impose any limits on the percentage of households that broadband providers may serve through resale. *See NPRM* ¶ 282. In its *First Universal Service Order*, the Commission found (at ¶ 169) that such limits on resale were unnecessary, and there is no reason to revisit that conclusion now.

"Public-Interest" Commitments. The Commission seeks comment on a variety of so-called "public interest" conditions that some parties have suggested should apply to CAF recipients. *See, e.g.*, *NPRM* ¶¶ 148-52. The Commission should reject all of these conditions. All are unnecessary to protect consumers, and some are so onerous that they would deter the majority of broadband providers from participating in the CAF program. And, for the reasons discussed above, this in itself would severely undermine the "public interest."

Additional open-Internet obligations for CAF ETCs, for example, *see NPRM* ¶ 150 n.250, would certainly fall into this category. They are unnecessary because CAF ETCs, like all other broadband providers, will be subject to the Commission's recently-adopted net neutrality rules. *See Net Neutrality Order*, 25 FCC Rcd at 17932 ¶ 44. And they would be harmful because the new rules carefully balance net neutrality with other important goals, such as encouraging innovation and investment by broadband providers. The Commission would upset that equilibrium if it imposed additional neutrality obligations on CAF participants. A similar

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Palmetto State Providers Network for Additional Funding Under the Rural Health Care Pilot Program, DA 11-529 (WCB, rel. Mar. 21, 2011) (regarding a request for a combined $94.3 million funding increase); Public Notice, *Requests for Extension of the June 30, 2011 Deadline for Funding Commitments Under The Universal Service Rural Health Care Pilot Program*, DA 11-172 (WCB, rel. Jan. 28, 2011) (regarding extending the deadline for all participants to select a vendor and request funding-commitment letters, based on requests from 17 pilot program participants).

analysis applies to facilities-sharing requirements. *See NPRM* ¶ 148 & n.242. Such requirements are unnecessary to protect consumers because, as discussed above, the vast majority of Americans will have access to several different voice-service providers, and all will have access to mobile broadband service. In any event, imposing facilities-sharing obligations on broadband providers would deter investment and innovation, distort the marketplace, and create many other inefficiencies.[220]

Commission Oversight of the CAF ETC Application Process. The Commission should assert exclusive jurisdiction over the designation of CAF ETCs. *See NPRM* ¶ 429 (asking whether the Commission has "exclusive jurisdiction to rule on" broadband ETC applications). There is no reason to perform CAF ETC designations under the cumbersome process outlined in section 214 of the Act. Rather, section 214(e)(2) grants state commissions authority only to "designate a *common carrier* … as an eligible *telecommunications* carrier." 47 U.S.C. § 214(e)(2) (emphasis added). Because broadband is an information service regulated by the Commission under Title I of the Act, the Commission has ample authority to create a separate process for evaluating CAF ETC applications.[221]

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[220] For example, the Commission and the courts have repeatedly recognized that unbundling regulations impose substantial "administrative and social costs" and "a sharing requirement may diminish the original owner's incentive to keep up or to improve [their] property." *Iowa Utils. Bd.*, 525 U.S. at 428-29 (Breyer, J., concurring in part and dissenting in part); *see also* Report and Order and Order on Remand and Further Notice of Proposed Rulemaking, *Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, 18 FCC Rcd 16978, 16983, 17006-07, 17022-23, 17141-41 ¶¶ 3, 33, 64, 272 (2003) (finding that "network unbundling requirements tend to undermine the incentives of both incumbent LECs and new entrants to invest in new facilities and deploy new technology"), *vacated in part and remanded*, *United States Telecomm Ass'n v. FCC*, 359 F.3d 554 (D.C. Cir. 2004).

[221] *See, e.g.*, *Cable Modem Order*, 17 FCC Rcd at 4822-23 ¶¶ 38-40; *Wireline Broadband Order*, 20 FCC Rcd at 14855-56 ¶¶ 1-3; *Wireless Broadband Order*, 22 FCC Rcd at 5902 ¶ 2; *see also* Report to Congress, *Federal-State Joint Board on Universal Service*, 13 FCC Rcd 11830, 11537-39 ¶ 76-80 (1998) ("*Stevens Report*").

State commissions nonetheless might assert a right to designate CAF ETCs. In that event, the Commission should expressly preempt additional state eligibility criteria under section 254(f) or the traditional *Louisiana PSC* preemption analysis.[222] In addition, the Commission should explain that it will prioritize applications for CAF funding from those states that choose *not* to adopt additional eligibility criteria. *NPRM* ¶ 89. It would be appropriate for the Commission to limit federal support in this manner because additional state-imposed eligibility criteria are likely to reduce CAF participation, thereby increasing the bids of the few providers willing to be subjected to those state requirements.

7. Advanced Mobility Fund.

As discussed above, "mobility" should be a supported service in its own right.[223] Accordingly, the Commission should create an Advanced Mobility Fund within the CAF to support mobile wireless broadband services.[224]

This Advanced Mobility Fund should be kept separate from the CAF until no areas in the United States remain unserved by mobile broadband providers. Funding should be used to support deployment of mobile broadband infrastructure in high-cost areas where such service currently is not available. This support should be allocated to providers in much the same way as CAF funding. In particular, support should be allocated to a *single* provider in each high-cost area through a competitive application process.

Funding for this mechanism should be repurposed from the legacy high-cost support that CETCs currently receive. Because that support is likely to be far greater than necessary to

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222 47 U.S.C. § 254(f); *Louisiana PSC*, 476 U.S. at 376 n.4. We discuss these bases for preemption in detail in Section II.B, *supra.*

223 *See* Section III.A, *supra.*

224 Throughout this Section, we use the term "mobile broadband" to refer to mobile wireless broadband services (*i.e.*, not satellite services).

ensure ubiquitous mobile broadband service, any Advanced Mobility Fund support that remains after funding is distributed to mobile providers should be distributed to fixed broadband providers through the CAF. Indeed, the Advanced Mobility Fund is likely to be quite small. Mobile providers already have deployed broadband service in many rural and high-cost areas. AT&T itself recently committed to deploy LTE service to 95% of the U.S. population after consummation of its transaction with T-Mobile.[225] Thus, by the time the Advanced Mobility Fund is operational, mobile broadband service already will be available in almost all of the country. This means that fewer census blocks will require support from that fund than from the CAF.

8. Transition from Legacy High-Cost Support to CAF Support.

As soon as the Commission issues its final CAF rules, it should begin phasing down all legacy high-cost support and transitioning that funding to the CAF. This transition should be identical for *all* legacy high-cost support, regardless of the mechanism and regardless of the type of carrier (*e.g.*, ILEC, wireless). The reductions in legacy support should be implemented at the *holding company* level, and not, for example, in each individual wire center where a provider receives support. Finally, legacy funding should be fully transitioned to the CAF over the course of five years—although the phase-down period may technically be shorter for some legacy ETCs depending on whether and how much CAF support they receive. Below, we describe the four basic transition scenarios.

For ETCs that receive legacy high-cost funding but that do not receive CAF funding, the five-year phase-out of high-cost support should be implemented in five equal increments at the

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[225] AT&T, Press Release, *AT&T to Acquire T-Mobile USA from Deutsche Telekom*, Mar. 20, 2011, http://www.att.com/gen/press-room?pid=19358&cdvn=news&=&mapcode= corporate|financial.

holding-company level. Thus, if an ETC currently receives $100,000 of high-cost support in aggregate across its various subsidiaries and service areas, that support should be phased out in $20,000 increments each year, until the provider no longer receives any legacy support. Again, this support would be reduced systematically at the holding-company level, without regard to where legacy universal service funding had been distributed or from what legacy mechanism.

The converse situation is equally straightforward. A CAF recipient that does not currently receive legacy high-cost support will simply begin receiving the amount of CAF support that it agreed to in its procurement agreement with the FCC, based on the support schedule developed by the Commission. These providers, obviously, will not be affected by the phase-down of legacy support.

For CAF recipients that also receive legacy high-cost support, the calculation appears more complicated but is actually very simple as well. Like other legacy funding recipients, the provider's high-cost support will be subject to the same five-year phase-out at the holding company level. Each year, the provider's aggregate amount of legacy high-cost support for that year would be compared against (again, at the holding-company level) the aggregate agreed-upon amount of CAF support due to the provider for that year. The provider would receive whichever amount is greater, but it would never receive both amounts. Assume, for example, that a holding company currently receives, in the aggregate, $100,000 of legacy high-cost support per year. Also assume that this same holding company agrees to accept $70,000 of CAF support for a number of census blocks to be served by its various subsidiaries. In Year 1 of the phase-down, this holding company would be entitled to $80,000 of legacy high-cost support (a 20% reduction). Since $80,000 is more than the $70,000 of CAF support it has agreed to accept, it will receive the $80,000 in Year 1. But in Year 2 of the phase-down, the holding company

would be entitled to only $60,000 of legacy support. Since this amount is less than its agreed-upon amount of CAF support, its phase-down would be complete and it would now begin to receive the larger of the two amounts—that is, $70,000 of CAF support—each year for the length of the CAF agreement.

If a legacy high-cost recipient becomes a CAF recipient and is entitled to *more* universal service support at the holding-company level under the new system (say, $130,000 of CAF funding in the example provided above), the provider would not experience any phase-down in funding. Rather, the Commission could either make a flash-cut in support from the legacy high-cost fund to the CAF and disburse $130,000 to the provider in Year 1 or, to minimize funding constraints, it could increase the support in equal increments over a set number of years.

This transition mechanism is simple and workable because it is indifferent to the origins of legacy support, either geographically or by funding mechanism, and it operates at the holding-company level. By acknowledging that all money is fungible, including money received from different universal service funds, this approach frees the transition to the CAF mechanism from the tentacles of the dysfunctional legacy mechanism. Adopting this transition plan is the Commission's best hope for implementing a powerful and fully funded CAF in a timeframe that is consistent with the Commission's broadband goals.

C. The Commission Has Ample Authority to Support Broadband Services with Universal Service Funding.

The Commission has at least three sources of authority to transition the universal service program from subsidizing legacy telecommunications services to supporting broadband infrastructure and services in unserved, high-cost areas. First, section 254 of the Communications Act (47 U.S.C. § 254)—interpreted in light of section 1 of the Act (*id.* § 151) and section 706 of the Telecommunications Act of 1996 (*id.* § 1302)—gives the Commission

direct authority to support broadband with universal service funding. Second, section 706(b) independently empowers the Commission to adopt a broadband universal service funding mechanism. Finally, the Commission has ancillary authority to effect that transition as well.[226]

1. Section 254.

Section 254(b) directs the Commission to use federal universal service programs to promote access to information services. It mandates that "the Commission *shall* base policies for the preservation and advancement of universal service on" six principles, two of which concern access to information services. 47 U.S.C. § 254(b) (emphasis added). Specifically, section 254(b)(2) states that "[a]ccess to *advanced* telecommunications and *information services* should be provided in all regions of the Nation." 47 U.S.C. § 254(b)(2) (emphasis added). And section 254(b)(3) provides that "[c]onsumers in all regions of the Nation, … should have access to telecommunications and *information services*, including interexchange services and *advanced* telecommunications and *information services*, that are reasonably comparable to those services provided in urban areas[.]" *Id.* § 254(b)(3) (emphasis added).[227]

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[226] AT&T has made each of these arguments in prior comments and ex partes, which we incorporate by reference here. *See, e.g.*, Comments of AT&T Inc., *Framework for Broadband Internet Service*, GN Docket No. 10-127, at 11, 22-27 (filed July 15, 2010) ("*AT&T Title II Comments*"); Reply Comments of AT&T Inc., *Framework for Broadband Internet Service*, GN Docket No. 10-127, at 15-18 (filed Aug. 12, 2010) ("*AT&T Title II Reply Comments*"); Reply Comments of AT&T Inc., *High-Cost Universal Service Support; Federal-State Joint Board on Universal Service*, WC Docket No. 05-337 & CC Docket No. 96-45, at 4-7 (filed June 2, 2008); Letter from Gary L. Phillips, AT&T, to Marlene H. Dortch, FCC, GN Docket Nos. 09-51, 09-47, & 09-137 and WC Docket Nos. 05-337 & 03-109 (filed Jan. 29, 2010) ("*Phillips 1/29/10 Letter*"); Letter from Gary L. Phillips, AT&T, to Marlene H. Dortch, FCC, GN Docket Nos. 09-51 & 09-137 and WC Docket Nos. 05-337 & 03-109 (filed Apr. 12, 2010) ("*Phillips 4/12/10 Letter*").

[227] These principles are more than sufficient to empower the Commission to use universal service to support broadband, and thus there is no need for the Commission to adopt an "additional section 254(b) principle" for that purpose. *NPRM* ¶¶ 58-59 (capitalization altered).

As the *NPRM* notes (at ¶¶ 61-62), there is some tension between these principles and section 254(e), which states that "only an eligible telecommunications carrier designated under section 214(e) of this title shall be eligible to receive specific Federal universal service support." 47 U.S.C. § 254(e). Similarly, section 254(c)(1) provides that "[u]niversal service is an evolving level of *telecommunications* services[.]" 47 U.S.C. § 254(c)(1) (emphasis added). But these provisions are not sensibly read to bar the Commission from using universal service to support broadband.

To the contrary, section 254(c)(1) itself rejects a static focus on legacy technologies, defining "universal service" as an "*evolving* level of telecommunications services that the Commission shall establish periodically under this section, *taking into account advances* in telecommunications *and information technologies and services*." *Id.* (emphasis added). The remainder of section 254(c) further confirms that universal service can encompass broadband. Section 254(c)(2) authorizes the Commission to "modif[y] … the definition of the *services* that are supported by Federal universal service support mechanisms." *Id.* § 254(c)(2) (emphasis added). This direction to "modif[y] … the definition" of universal service refers not to the "telecommunications services" that are to be supported, but more broadly to the "services" that are to be supported. And as the Commission explained in connection with section 254(h), which sets out the universal service framework for schools and libraries, "the varying use of the terms 'telecommunications services' and 'services' … suggests that the terms were used consciously to signify different meanings."[228] There, even though section 254(h) is entitled "*Telecommunications services for certain providers*," 47 U.S.C. § 254(h) (emphasis added), the Commission nonetheless concluded that the use of the broader term "services" in sections

[228] *First Universal Service Order*, 12 FCC Rcd at ¶ 439.

254(h)(1)(B)[229] and 254(c)(3)[230] authorizes the Commission to support *non*-telecommunications services for schools and libraries. *First Universal Service Order*, 12 FCC Rcd at ¶¶ 436-39. Similarly, here, Congress's use of the same broad term "services" in section 254(c)(2) authorizes the Commission to "modif[y] … the definition" of universal service to include non-telecommunications services, even though section 254(c)(1) refers to "telecommunications services." 47 U.S.C. §§ 254(c)(1), (2). At the very least, this language creates ambiguity about the scope of section 254, and thus a reviewing court would be required to defer to the Commission's interpretation.[231]

The Fifth Circuit reached a similar conclusion in *TOPUC*, which affirmed the Commission's decision to support Internet access and other non-telecommunications services in the schools and libraries program. Although the court recognized that the statutory language points both ways, 183 F.3d at 440-42, it found that section 254(c)(1) "invites the FCC periodically to re-define 'universal service' to 'tak[e] into account advances in telecommunications and information technologies and services.'" *Id.* at 442 (quoting 47 U.S.C. § 254(c)(1)). The court also acknowledged that other language in section 254(h) "instructs the FCC to establish competitively neutral rules to 'enhance … access to advanced

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[229] 47 U.S.C. § 254(h)(1)(B) provides, in relevant part: "All *telecommunications carriers* serving a geographic area shall, upon a bona fide request for any of *its services* that are within the definition of universal service under subsection (c)(3) of this section, provide *such services* to elementary schools, secondary schools, and libraries for educational purposes at rates less than the amounts charged for *similar services* to other parties." (Emphasis added.)

[230] 47 U.S.C. § 254(c)(3) provides: "In addition to *the services* included in the definition of universal service under paragraph (1), the Commission may designate *additional services* for such support mechanisms for schools, libraries, and health care providers for the purposes of subsection (h) of this section." (Emphasis added.)

[231] Several courts have held that the Commission's interpretation of section 254 is reviewable under *Chevron* step two. *See, e.g.*, *Rural Cellular Ass'n v. FCC*, 588 F.3d 1095, 1101-02 (D.C. Cir. 2009); *Qwest I*, 258 F.3d at 1200-02.

telecommunications and information services.'" *Id.* (quoting 47 U.S.C. § 254(h)(2)(A)). The court held that this language made the statute "ambiguous enough to require deference under *Chevron* step-two," and it affirmed the Commission's decision to extend universal service support to information services in the schools and libraries program. *Id.* at 440, 442-43. Likewise, here, the additional language in sections 254(b) and 254(c)(1)-(2) creates more than enough ambiguity to permit the Commission to direct universal service funding to broadband despite any contrary suggestion in sections 254(c)(1) or 254(e).[232]

A cramped reading of section 254 that fixates on the "telecommunications" language and ignores the "information services" language would also contradict provisions elsewhere in the Act that elucidate Congress's intent for the Commission to promote broadband and other advanced services. As the D.C. Circuit explained in *Comcast*, "statements of congressional policy can help delineate the contours of statutory authority,"[233] and here, three such statements make clear that the Commission has authority to support information services with universal service funding.

First, the Commission's core statutory mission—as expressed in the first sentence of the Act—is "to make available, so far as possible, to all the people of the United States … a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges." 47 U.S.C. § 151. In today's world, a universal service system that does not support broadband Internet access services would have no chance of meeting this objective. Thus, section 1 supports reading section 254 broadly to permit funding for broadband.

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[232] Because section 254 permits the Commission to direct universal service funding to *both* telecommunications and information services, the Commission need not classify interconnected VoIP as a telecommunications service in order to support it. *Cf. NPRM* ¶ 73 (noting that "[i]f the Commission were to classify interconnected VoIP as a telecommunications service, this would enable the Commission to support networks used to provide interconnected VoIP").

[233] *Comcast Corp. v. FCC*, 600 F.3d 642, 654 (D.C. Cir. 2010).

Similarly, section 706(a) of the 1996 Act provides that the Commission "shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans." 47 U.S.C. § 1302(a). Section 706(b) further states that if the Commission finds that advanced telecommunications capability is not being deployed to all Americans, it "shall take immediate action to accelerate deployment of such capability." *Id.* § 1302(b). Given the Commission's findings regarding the obstacles to deployment of broadband in high-cost areas, sections 706(a) and (b) clearly support a broad view of the FCC's authority under section 254.

Finally, the American Recovery and Reinvestment Act of 2009 makes ubiquitous broadband deployment a key Commission goal and mandates that the Commission "shall seek to ensure that all people of the [U]nited [S]tates have access to broadband capability." 47 U.S.C. § 1305(k)(2). It also directs the Commission to develop "a detailed strategy for achieving affordability of such service." *Id.* § 1305(k)(2)(B). These clear statutory directives should also inform the Commission's interpretation of section 254.

The foregoing analysis reveals that the Commission has ample authority under section 254 to support broadband. Nonetheless, to further buttress its authority under that section, the Commission could forbear from sections 254(c)(1) and 254(e), or from any other statutory provision that could conceivably limit universal service to "telecommunications" carriers or services. *See NPRM* ¶ 72. Indeed, Section 706 of the 1996 Act expressly identifies forbearance as a key means of fulfilling the Commission's obligation to ensure ubiquitous access to broadband services.[234] Further, the D.C. Circuit already has upheld the Commission's use of

[234] 47 U.S.C. § 1302(a) ("The Commission … shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans … by utilizing, in a manner consistent with the public interest, convenience, and necessity, price cap regulation, regulatory forbearance, measures that promote competition in the local

forbearance for this purpose. *See, e.g.*, *Ad Hoc Telecomms. Users Comm. v. FCC*, 572 F.3d 903, 907 (D.C. Cir. 2009) ("As contemplated by § 706, the FCC has utilized forbearance from certain Title II regulations as one tool in its broadband strategy.").

2. Section 706(b).

Quite apart from section 254, the Commission also may rely on section 706(b) as a *direct* source of authority for adoption of a broadband support mechanism. *See NPRM* ¶¶ 66-67. Section 706(b) directs the Commission, if it concludes that "advanced telecommunications capability" is not "being deployed to all Americans in a reasonable and timely fashion," to "*take immediate action* to accelerate deployment of such capability by *removing barriers to infrastructure investment*[.]" 47 U.S.C. § 1302(b) (emphasis added). Section 706(d) defines "advanced telecommunications capability" as "high-speed, switched, broadband telecommunications capability that enables users to originate and receive high-quality voice, data, graphics, and video telecommunications using any technology." *Id.* § 1302(d)(1). Section 706(b) thus provides a clear, discrete grant of authority for the Commission to address "barriers to infrastructure investment" in order to "accelerate [broadband] deployment."[235] As AT&T has previously explained, using universal service to fund providers in areas unserved by broadband services certainly meets this criterion.[236]

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telecommunications market, or other regulating methods that remove barriers to infrastructure investment.").

[235] The D.C. Circuit has noted that "[t]he general and generous phrasing of § 706 means that the FCC possesses significant albeit not unfettered, authority and discretion to settle on the best regulatory or deregulatory approach to broadband—a statutory reality that assumes great importance when parties implore courts to overrule FCC decisions on this topic." *Ad Hoc*, 572 F.3d at 906-07.

[236] *AT&T Title II Comments* at 25-27; *AT&T Title II Reply Comments* at 17-18. Lifeline and Linkup support also remove barriers to infrastructure investment. They ensure that more residents in a given area ultimately subscribe to broadband Internet access (in industry terms, a

3. Ancillary Jurisdiction.

The Commission's authority under Title I of the Communications Act complements its authority under sections 254 and 706 and removes any question regarding the Commission's authority to support broadband with universal service funds. *See NPRM* ¶¶ 68-69.[237] Section 4(i) empowers the Commission to "perform any and all acts, make such rules and regulations, and issue such orders … as may be necessary in the execution of its functions." 47 U.S.C. § 154(i). For the Commission to exercise its "ancillary jurisdiction" under section 4(i), two conditions must be met: (1) "the subject of the regulation must be covered by the Commission's general grant of jurisdiction under Title I of the Communications Act, which … encompasses 'all interstate and foreign communication by wire or radio,'"[238] and (2) the subject of the regulation must be "reasonably ancillary to the Commission's effective performance of its statutorily mandated responsibilities."[239] Both conditions are met here.

First, broadband Internet access service constitutes interstate "communications by wire or radio." *See* 47 U.S.C. § 153(59) (defining "communication by wire" as "the transmission of writing, signs, signals, pictures, and sounds of all kinds by aid of wire, cable, or other like connection between the points of origin and reception of such transmission …"). Second, establishing a broadband universal service program is "reasonably ancillary" to the statutory directives in sections 254 and 706, as informed by Congress's policy statements in section 1 and

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higher "take rate"), which is a critical factor that providers consider in assessing whether broadband investment in an area can be justified by its projected returns.

[237] AT&T's prior ex parte submissions provide a detailed analysis of this issue. *See Phillips 1/29/10 Letter*; *Phillips 4/12/10 Letter*.

[238] *Am. Library Ass'n v. FCC*, 406 F.3d 689, 691-93 (D.C. Cir. 2005) (quoting *United States v. Southwestern Cable Co.*, 392 U.S. 157, 167 (1968) and 47 U.S.C. § 152(a)).

[239] *Id.* at 692; *see also Southwestern Cable*, 392 U.S. at 178 (same).

the Recovery Act.[240] In order to "effective[ly] perform[] its statutorily mandated responsibilities" to promote universal service and access to "information services" under section 254, and to "take immediate action to accelerate deployment of" advanced services under section 706(b), the Commission *must* direct universal service funding to broadband services. Thus, regardless of whether section 254 or section 706 gives the Commission *direct* authority to support broadband, such support falls well within the Commission's ancillary authority under Title I.

Indeed, the Commission *already* has successfully relied on its Title I authority to support broadband in circumstances very similar to those present here. In implementing the 1996 Act's universal service requirements (*i.e.*, section 254), the Commission exercised its Title I authority to provide funding to information service providers participating in the schools and libraries program. As discussed above, the Commission relied solely on its *direct statutory authority* under section 254 to extend funding to non-telecommunications *services*. But to justify funding information-service *providers* who were not also telecommunications carriers, the Commission additionally relied on its ancillary authority. The relevant statutory text referred only to "telecommunications carriers," and thus it was unclear whether information-service providers were entitled to funding. *See* 47 U.S.C. § 254(h)(1)(B) (providing reimbursement guidelines for "telecommunications carrier[s] providing service under" the program). The Commission nevertheless decided "to provide discounts for Internet access and internal connections provided

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[240] While *Comcast* held that statutory "statements of policy"—such as section 1 of the Act—are, standing alone, an insufficient basis for the invocation of ancillary jurisdiction, the court also recognized that when statutory policy statements are combined with other "express delegations of regulatory authority," the Commission *may* exercise ancillary jurisdiction over matters reasonably related to those policies. *Comcast*, 600 F.3d at 652-55. This holding clearly encompasses promotion of universal service, which (unlike net neutrality) is entrusted to the Commission by both broad policy statements *and* the specific statutory directives in sections 254 and 706.

by *non*-telecommunications carriers," claiming both direct authority under section 254 and ancillary authority under section 4(i). *First Universal Service Order*, 12 FCC Rcd at ¶ 589 (emphasis added).

On appeal, the Fifth Circuit affirmed the Commission's use of Title I to complement its authority under section 254. *TOPUC*, 183 F.3d at 444. Noting that "Congress intended to allow the FCC broad authority to implement" section 254, the court concluded that, even though the statute did not explicitly allow information service providers to be included in the program, the Commission's rules were justified by a combination of section 254 and "the FCC's 'necessary and proper' authority under section 154(i)." *Id.* at 443-44.[241] By funding information service providers, the Commission was "not asserting additional jurisdictional authority, but, rather [was] issuing a regulation '*necessary to fulfill its primary directives*'" of promoting universal service. *Id.* at 444 (emphasis added). The same logic applies here.[242]

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[241] Similarly, here, the Commission can rely on its ancillary authority to provide CAF funding to non-telecommunications providers. *Compare First Universal Service Order*, 12 FCC Rcd at ¶¶ 589-600.

[242] The Commission seeks comment on whether disbursing support to information service providers would "comport with federal appropriations laws." *NPRM* ¶ 62 (discussing the Constitution's Appropriations Clause, a provision governing appropriations, the Antideficiency Act, and the Miscellaneous Receipts Act); *see also id.* ¶¶ 62 n.77, 67 & n.89. As discussed above, the same statutory provisions that authorize the Commission's existing universal service programs also give the Commission authority to support broadband services. Thus, expanding universal service to fund broadband would no more violate the Appropriations Clause and the statutes cited in the *NPRM* than the Commission's existing programs. Moreover, Congress has granted the Commission an express exemption from the Antideficiency Act, 31 U.S.C. §1341(a)(1) for "any amount collected or received as Federal universal service contributions required by Section 254 of the [Act]," and "the expenditure or obligation of amounts attributable to such contributions for universal service support programs established pursuant to that section." Pub. L. No. 108-494, 118 Stat. 3986, § 302(a) (2004); *see also* Pub. L. No. 111-322, 124 Stat 3518, Title I § 155 (2010) (extending exemption through Dec. 31, 2011). Thus, just as this exemption has permitted the Commission to use universal service funds to reimburse non-telecommunications providers in other contexts, it would also permit the funding of broadband.

D. The Commission Should Not, and May Not, Compel Providers to Deploy Broadband Service.

The Commission seeks comment on whether it should add broadband to the list of supported services in 47 C.F.R. § 54.101(a) and thereby compel *all ETCs* to provide it. *See NPRM* ¶ 63. The Commission also asks whether it should condition receipt of *legacy* high-cost support on a carrier's deployment of broadband services. *See id.* ¶¶ 70-71. The Commission should reject these proposals. Both would balloon the size of the federal fund, requiring larger USF contributions and increasing the price of communications services. This, in turn, would harm consumers and hinder universal service in violation of the principles in section 254. In addition, compelling providers to deploy broadband would exceed the Commission's jurisdiction under Title I of the Communications Act and violate the Takings Clause of the U.S. Constitution.

First, under the Commission's existing interpretation of section 214(e)(1), *every* Eligible Telecommunications Carrier would be required to offer broadband service throughout *all* of the service areas where it is designated as an ETC if the Commission were to add broadband to the list of supported services.[243] Likewise, conditioning legacy funding on deployment of broadband would often require multiple providers in a given high-cost area to deploy broadband services.[244]

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[243] 47 U.S.C. § 214(e)(1). *See* discussion at pages 55-56, *supra*, explaining how the Commission has interpreted section 214(e)(1) as requiring ETCs to provide supported services throughout their designated service areas regardless of whether they receive high-cost funding to support their provision of those services. Notice of Proposed Rulemaking, *Universal Service Reform, Mobility Fund*, 25 FCC Rcd 14716, 14732 ¶ 48 n.54 (2010) ("Pursuant to 47 U.S.C. § 214(e)(1) and 47 C.F.R. § 54.101(b), an ETC is obligated to provide all of the supported services defined in 47 C.F.R. § 54.101(a) throughout the area for which it has been designated an ETC.").

[244] 47 U.S.C. § 214(e)(2) (requiring state commissions to designate multiple ETCs in many areas); Order and Notice of Proposed Rulemaking, *High-Cost Universal Service Support, Federal-State Joint Board on Universal Service, Lifeline and Link-Up*, 25 FCC Rcd 4136, 4143 ¶ 17 n.50 (2010) (explaining that there are multiple providers eligible to receive legacy support in a particular high-cost area).

The costs of such duplicative broadband deployment would be extraordinarily high.[245] Indeed, the existing universal service fund is several orders of magnitude too small to adequately support deployment of broadband by *every* ETC and *every* legacy support recipient in *every* area that they serve throughout the country.

Adopting either proposal would thus present a legal quandary for the Commission. Were it to require providers to deploy broadband *without* vastly expanding the size of the fund, it would contravene section 254(b)(5), which requires "*sufficient* Federal and State mechanisms to preserve and advance universal service," and section 254(e), which provides that "any [universal service] support should be … *sufficient* to achieve the purposes of this section." 47 U.S.C. §§ 254(b)(5), (e) (emphasis added). Both the Tenth Circuit and the Fifth Circuit have explained that ensuring the sufficiency of universal service support is a direct statutory command.[246] In short, the Commission cannot add broadband to the list of supported services or otherwise require a provider to deploy broadband without also ensuring that there is sufficient funding to support such a mandate. And, given the costs of the duplicative deployments that would result from adoption of either proposal, the Commission could comply with this "sufficiency" mandate only if it drastically expanded the size of the federal fund.

At the same time, however, expanding the size of the fund would require vastly expanded *contributions* to universal service as well. Doubling the size of the high-cost fund—which

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[245] As discussed above, AT&T's solution is far preferable to either of the proposals discussed in the text. Although it would ensure ubiquitous deployment of broadband, it would do so at a fraction of the cost by (i) using a competitive process to select a *single* provider to offer broadband in each high-cost area, and (ii) ensuring that providers receive no more funding than necessary to supply broadband service.

[246] *Qwest I*, 258 F.3d at 1197, 1200 (explaining that "the FCC must base its policies on the [enumerated] principles" in section 254(b) and holding that the principles' "language indicates a mandatory duty on the FCC"); *TOPUC*, 183 F.3d at 412 (holding that "the plain language of § 254(e) makes sufficiency of universal service support a direct statutory command").

would probably still not enable *all* ETCs to provide broadband service throughout *all* of their designated service areas—would cause the contribution factor to jump to *24.8 percent*, which would result in considerably higher prices for consumers. This, in turn, would price some consumers out of the market for communications services, thereby undermining universal service.

Courts have expressed concern that a high-cost fund that is too large may be in tension with section 254(b)(1), which requires that "[q]uality services should be available at just, reasonable, and affordable rates." 47 U.S.C. § 254(b)(1). The Tenth Circuit, for example, has noted that section 254(b)(1) could be read to "encompass[] the principle that … universal services[] should be kept affordable, and thus excessive subsidization of universal services … may violate the principle found in § 254(b)(1)."[247] Similarly, the D.C. Circuit recognized in upholding the Commission's cap on support for competitive ETCs that focusing too much on ensuring that "the USF is 'sufficient' for purposes of § 254(b)(5)" could make the fund "so large it actually makes telecommunications services less 'affordable,' in contravention of § 254(b)(1)."[248] In short, expanding the list of supported services to include broadband or conditioning legacy support on the provision of broadband would put the Commission in the untenable position of contravening section 254 regardless of whether it refused to, or agreed to, expand the size of the USF fund.

Moreover, either option would be a highly ineffective means of promoting broadband deployment. Non-rural carriers, which serve the bulk of high-cost customers, often receive no

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[247] *Qwest I*, 258 F.3d at 1200.

[248] *Rural Cellular Ass'n*, 588 F.3d at 1103. *See also Alenco*, 201 F.3d at 620 ("Because universal service is funded by a general pool subsidized by all telecommunications providers—and thus indirectly by the customers—excess subsidization in some cases may detract from universal service by causing rates unnecessarily to rise, thereby pricing some consumers out of the market.").

high-cost support in rural areas. AT&T, for example, receives high-cost-model support in only three of its twenty-two ILEC service areas. *AT&T NBP #19 Comments* at 8. Thus, simply increasing the size of the fund to support broadband or conditioning legacy support without fundamentally changing the structure of the non-rural, high-cost mechanism, would do nothing to give currently unsupported carriers the incentive or ability to expand their deployment of broadband in rural and other areas where such deployment is not economic today.

Second, even if requiring providers to deploy broadband service could somehow be reconciled with the plain language of section 254, the Commission would lack authority to do so for an entirely independent reason: it lacks authority to impose this type of common-carrier obligation under Title I of the Act.

The Commission has repeatedly affirmed that broadband is an information service to be regulated under Title I of the Communications Act.[249] And section 3(51) of the Act expressly precludes the Commission from imposing common-carrier regulations on information services. 47 U.S.C. § 153(51). Specifically, it provides that a "telecommunications carrier shall be treated as a common carrier under this chapter only to the extent that it is engaged in providing telecommunications services." *Id.* This statutory provision thus precludes the Commission from imposing any common-carrier-type rules on the provision of broadband Internet access.[250] Mandatory build-out obligations unquestionably constitute the type of common-carrier

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[249] *See, e.g.*, *Cable Modem Order*, 17 FCC Rcd at 4822-23 ¶¶ 38-40; *Wireline Broadband Order*, 20 FCC Rcd at 14855-56 ¶¶ 1-3; *Wireless Broadband Order*, 22 FCC Rcd at 5902 ¶ 2; *see also Stevens Report*, 13 FCC Rcd at 11537-39 ¶¶ 76-80.

[250] *See AT&T Title II Reply Comments* at 22, 29-33; Reply Comments of AT&T Inc., *Preserving the Open Internet; Broadband Industry Practices*, GN Docket No. 09-191, WC Docket No. 07-52, at 165-66 (filed Apr. 26, 2010).

regulation precluded by section 3(51)—indeed, such obligations are one of the *hallmarks* of traditional Title II, common-carrier regulation.[251]

Finally, compelling providers to offer broadband services in areas where doing so is uneconomic would also violate the Fifth Amendment's prohibition that "private property" shall not "be taken for public use, without just compensation." U.S. Const. amend. V.

Requiring providers to deploy broadband services in high-cost areas would constitute a *physical taking*—the most serious type of government intrusion on private property—by forcing carriers to attach broadband facilities to their networks without just compensation. *See Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 426 (1982) ("a permanent physical occupation" effects a taking). In *Loretto*, the Supreme Court found a taking where a property owner was required to allow a cable operator to install a small box on an apartment building. *Id.* at 438. Similarly, in the telecommunications context, the D.C. Circuit has held that requiring service providers to permit the attachment of third-party equipment to their physical facilities without just compensation implicates the Takings Clause.[252] Here, an uncompensated build-out

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[251] *See, e.g.*, 47 U.S.C. § 214(e)(3) ("[I]f no *common carrier* will provide the services that are supported by Federal universal service support mechanisms under section 254(c) to an unserved community or any portion thereof that requests such service" the Commission and the states, for inter- and intrastate services, respectively, "shall determine which *common carrier* or carriers are best able to provide such service to the requesting unserved community … and shall order such carrier or carriers to provide such service.") (emphasis added); Memorandum Opinion and Order, *Federal-State Joint Board on Universal Service*: *Western Wireless Corporation Petition for Designation as an Eligible Telecommunications Carrier for the Pine Ridge Reservation in South Dakota*, 16 FCC Rcd 18133, 18140 ¶ 18 n.47 (2001) ("Pursuant to section 214(e)(3), the Commission, with respect to interstate services, and the state, with respect to intrastate services, may order a *common carrier* to provide the supported services to an unserved community.") (emphasis added).

[252] *Bell Atlantic Tel. Cos. v. FCC*, 24 F.3d 1441, 1445 (D.C. Cir. 1994) (quoting *Loretto*, 458 U.S. at 426) ("The Commission's decision to grant [competitive providers] the right to exclusive use of a portion of the petitioners' central offices directly implicates the Just Compensation Clause of the Fifth Amendment, under which a 'permanent physical occupation authorized by government is a taking without regard to the public interests that it may serve.'").

requirement would be far more intrusive than merely *allowing* a third party to attach a box or co-locate its facilities at a carrier's switching station. To enable broadband connectivity over facilities that do not support it now, a carrier would have to make significant modifications and additions to its network infrastructure, *and pay for them*, itself.

In addition, requiring providers to deploy broadband services in high-cost areas without just compensation also would effect a *regulatory taking*. Whether administrative action constitutes such a taking turns on the three factors set out in the Supreme Court's decision in *Penn Central Transportation Co. v. City of New York*, namely: (i) the economic impact of the regulation; (ii) the extent to which the regulation interferes with legitimate investment-backed expectations; and (iii) the character of the governmental action. 438 U.S. 104, 124 (1978).

An unfunded broadband-deployment mandate would have a severe economic impact on providers like AT&T. The expense of modifying existing facilities and building new facilities to provide broadband service in previously unserved areas would be substantial. Indeed, the FCC itself determined that rolling out terrestrial broadband to currently unserved customers would require over $24 billion in additional funding. *National Broadband Plan* at 136.

Mandating deployment of broadband also would severely undermine carriers' investment-backed expectations. Carriers never anticipated that their designation as eligible telecommunications carriers for legacy POTS service would result in them being subject to mandatory, uncompensated build-out requirements for broadband service. While a universal service recipient might reasonably expect that the amount of its benefits could vary over time, it

would not expect that, as a condition of continuing to receive *the same benefit*, it might need to provide an entirely different type of product.[253]

Moreover, as discussed above, the Commission's proposal would constitute a physical invasion of carriers' networks. *Penn Central*, 438 U.S. at 124. Although a physical occupation constitutes a *per se* violation of the Takings Clause, *Loretto*, 458 U.S. at 426, such an intrusion is relevant to the regulatory takings analysis as well. As the Supreme Court has explained, a regulatory takings claim is stronger when the challenged regulation "amounts to a physical invasion" and does not "merely affect[] property interests through 'some public program adjusting the benefits and burdens of economic life to promote the common good.'" *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 528, 539-40 (2005) (quoting *Penn Central*, 438 U.S. at 124). Here, requiring providers to upgrade their networks *would* constitute a physical invasion, and thus all three elements of the *Penn Central* test are met. Accordingly, adoption of the Commission's rules would constitute a regulatory taking.

Finally, requiring POTS providers to enter an entirely new line of business without enabling them to recover their costs would also constitute a *confiscatory* regulatory taking. *See Duquesne Light Co. v. Barasch*, 488 U.S. 299, 307 (1989). For purposes of this analysis, it does not matter whether the provider is making a profit in its other lines of business—instead, an agency action constitutes a confiscatory taking if it renders even one of a company's business

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[253] In discussing a proposed reduction in IAS support, the *NPRM* cites cases holding that "alter[ation]" of a Congressional "benefit program" does not constitute a taking and that carriers are not entitled to "government-subsidized profits" or a certain return on investment. *See NPRM* ¶ 240 & n.384. Those cases are inapposite here. None addresses the situation where an agency *compels* a company to provide service, but then prevents that company from recovering the costs of providing the service. And those cases certainly do not address the situation where an agency requires a company to enter an entirely new line of business to retain a benefit designed to compensate the company for providing another service at a government-mandated, below-cost rate.

segments unprofitable. *See Brooks-Scanlon Co. v. R.R. Comm'n*, 251 U.S. 396, 399 (1920) ("The plaintiff may be making money from its sawmill and lumber business but it no more can be compelled to spend that [profit] than it can be compelled to spend any other money to maintain a railroad for the benefit of others who do not care to pay for it.").

CONCLUSION

The Commission should smooth the transition from the circuit-switched PSTN to the all-IP network of tomorrow through the universal service and intercarrier compensation policies outlined above.

Respectfully submitted,

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