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**Public Meeting on High-Cost Universal Service Support (Panel I, II) November  
17,2004**

**Heritage Reporting Corporation**

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**CONDENSED TRANSCRIPT AND CONCORDANCE  
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## Page 1

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 ( 3) FEDERAL COMMUNICATIONS COMMISSION  
 ( 4) PUBLIC MEETING  
 ( 5) ON HIGH-COST UNIVERSAL SERVICE SUPPORT  
 ( 6) FOR AREAS SERVED BY RURAL CARRIERS AND RELATED  
 ( 7) ISSUES  
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 (12) PANEL I  
 (13) SUPPORT IN AREAS SERVED BY RURAL CARRIERS AND  
 (14) THE DEFINITION OF "RURAL TELEPHONE COMPANY"  
 (15) PANEL 2  
 (16) BASIS OF SUPPORT FOR CETCs AND TRANSFERRED  
 (17) EXCHANGES  
 (18) November 17, 2004  
 (19)  
 (20) Gaylord Opryland Resort, Nashville, TN  
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- ( 1) APPEARANCES (CONT'D)  
 ( 2) PANELISTS II  
 ( 3) SCOTT BERGS, MIDWEST WIRELESS  
 ( 4) DAVID COLE, CENTURYTEL  
 ( 5) GENE JOHNSON, FAIRPOINT COMMUNICATIONS  
 ( 6) DENISE PARRISH, WYOMING OFFICE OF CONSUMER  
 ( 7) ADVOCATE  
 ( 8) DALE LEHMAN, ALASKA PACIFIC UNIVERSITY  
 ( 9) LEE SELWYN, ETI  
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## Page 2

- ( 1) APPEARANCES  
 ( 2)  
 ( 3) JOINT BOARD  
 ( 4) COMMISSIONER KATHLEEN Q. ABERNATHY  
 ( 5) COMMISSIONER KEVIN J. MARTIN  
 ( 6) COMMISSIONER THOMAS DUNLEAVY  
 ( 7) COMMISSIONER ROBERT NELSON  
 ( 8) COMMISSIONER LILA JABER  
 ( 9) CONSUMER ADVOCATE BILLY JACK GREGG  
 (10)  
 (11) PANELISTS I  
 (12) RICH COIT, SOUTH DAKOTA INDEPENDENT TELEPHONE  
 (13) COALITION  
 (14) PAUL GARNETT, CELLULAR TeIcOMMUNICATIONS  
 (15) INDUSTRY ASSOCIATION  
 (16) JEFF REYNOLDS, PARRISH, BLESSING & ASSOCIATES  
 (17) INC.  
 (18) JOEL LUBIN, AT&T  
 (19) DENNIS WELLER, VERIZON  
 (20) DALE LEHMAN, ALASKA PACIFIC UNIVERSITY  
 (21) LEE SELWYN, ETI  
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- ( 1) \* \* \*  
 ( 2) COMMISSIONER ABERNATHY: My name is  
 ( 3) Kathleen Abernathy. I'm the FCC Commissioner.  
 ( 4) I want to welcome everybody to today's en banc  
 ( 5) where we are going to focus on possible  
 ( 6) reforms to the universal service support  
 ( 7) mechanism for high-cost rural areas.  
 ( 8) As all of us recognize, universal  
 ( 9) service is one of the cornerstones of the  
 (10) Federal Communications policy, and Congress  
 (11) did make it a top priority in the 1996 Act.  
 (12) So, it's vital for us to ensure that the  
 (13) program remains sustainable over the long  
 (14) haul, that it operates fairly and efficiently,  
 (15) and that we are addressing problems before  
 (16) they become critical. So, what we're looking  
 (17) at today is how do you calculate and receive  
 (18) high-cost universal service support.  
 (19) And the first panel will address the  
 (20) question of whether high-cost support for  
 (21) rural carriers should continue to be based on  
 (22) embedded costs, should be transitioned to  
 (23) forward-looking costs as under the non-rural  
 (24) support mechanism, or are there other  
 (25) alternatives available.

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( 1) I think the Commission concluded  
 ( 2) several times in the past that a  
 ( 3) forward-looking cost methodology was an  
 ( 4) optimal choice. but refrained from  
 ( 5) implementing such an approach based on  
 ( 6) concerns about the reliability of the cost  
 ( 7) models that you would have for rural areas.  
 ( 8) And I know many of those questions remain. At  
 ( 9) the Joint Board now. we are revisiting this  
 (10) fundamental question. and I'm sure that our  
 (11) panelists will give us a lot of insight into  
 (12) the strengths and weaknesses of the competing  
 (13) proposals. What we've found is that these en  
 (14) banc hearings provide a unique opportunity for  
 (15) us to hear from all parties side by side and  
 (16) kind of address many of the questions that  
 (17) come up.

(18) The first panel also is going to  
 (19) address the definition of rural carrier. Some  
 (20) have argued that holding companies that own  
 (21) and operate rural telephone companies in  
 (22) different parts of the United States should be  
 (23) required to aggregate those operations into a  
 (24) single study area for purposes of calculating  
 (25) universal service support. And essentially

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(1) what we would be doing is treating these  
 (2) holding companies the same as non-rural  
 (3) carriers. So, our panelists are going to  
 (4) discuss the merits of the current approach,  
 (5) where we do not engage in that kind of  
 (6) analysis versus some of the potential  
 (7) alternatives.  
 (8) Then we will have a short break. We  
 (9) will need a break. And then we'll move to our  
 (10) second panel where we're going focus primarily  
 (11) on the basis of support for competitive ETCs.  
 (12) Incumbent carriers have long argued that  
 (13) wireless carriers and other competitive ETCs,  
 (14) which is eligible telcom carriers, should  
 (15) receive their support based on their own  
 (16) embedded cost rather than on the incumbent's  
 (17) cost.  
 (18) Competitors, by contrast, generally  
 (19) argue that incumbents and competitors must  
 (20) receive identical support, whether it's based  
 (21) on forward-looking costs, the lowest cost,  
 (22) provider's costs or any other measure. So,  
 (23) we're going to explore all of those arguments  
 (24) in detail.  
 (25) And I think, in addition, the second

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(1) panel will address the FCC rule that limits  
 (2) support for acquired exchanges to the amount  
 (3) that the seller received, whether or not that  
 (4) should be revisited.  
 (5) Now, before we get on to the  
 (6) substance of our first panel, I want to begin  
 (7) my offering a heartfelt thank you for all of  
 (8) our esteemed panelists for traveling to  
 (9) Nashville at their own expense to help the  
 (10) Joint Board grapple with these very, very  
 (11) important issues. You've given us advance  
 (12) presentation materials that are informative.  
 (13) We're going to be able to hear from you. We  
 (14) really do appreciate this; it's essential. We  
 (15) need your help as we struggle with these very  
 (16) complicated, complex issues. And so, thank  
 (17) you.  
 (18) And I also want to take a moment to  
 (19) recognize two colleagues who are departing  
 (20) from public service and, as a result, from  
 (21) their participation on the Joint Board. It's  
 (22) Bob Rowe from Montana and Lila Jaber from  
 (23) Florida.  
 (24) Bob and Lila have been part of  
 (25) the Joint Board since I joined a little over

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(1) three years ago. They have been instrumental in  
 (2) helping this Joint Board, I think, cover a  
 (3) tremendous amount of material, controversial,  
 (4) complex issues that folks said we'd never be  
 (5) able to reach consensus on and we did.  
 (6) Bob was instrumental in urging us  
 (7) to adopt this en banc approach, which we did.  
 (8) It's been very, very successful and helpful. I  
 (9) want to thank Bob for that, for his good humor,  
 (10) for his wit, his knowledge of the details. And  
 (11) it's going to be a loss that you will no longer  
 (12) be a part of the Joint Board and a loss, I  
 (13) think, for the public. But I wish you all the  
 (14) best in whatever you do next. I'm assuming we  
 (15) will continue to hear from you about your  
 (16) thoughts on many of these issues, so thank you  
 (17) for all your help.  
 (18) And Lila also has just been a  
 (19) tremendous asset on this Joint Board, very good  
 (20) at reconciling some of the issues between the  
 (21) larger states, the rural states and the non-rural  
 (22) states, and how you balance those concerns; a  
 (23) friend who has helped as we've struggled through  
 (24) some of these issues, and who has helped me  
 (25) understand the workings of NARUC.

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- (1) And I wish them both the best.
- (2) I'm sorry they're leaving because we have a nice
- (3) little family. I got very comfortable. The
- (4) good news is that NARUC has nominated some
- (5) excellent replacements in time for them to
- (6) attend today's event. We've got Elliott Smith
- (7) of Iowa. I want to thank Elliott for being
- (8) willing to step into some issues and to deal
- (9) with some very controversial and complex issues.
- (10) They didn't tell you that, I'm sure. And Ray
- (11) Baum of Oregon - Ray, thank you, also.
- (12) They've both been nominated by
- (13) NARUC. There will be a formal process through
- (14) the FCC and then they will formally join the
- (15) Board very soon.
- (16) And, finally, I want to give an
- (17) opportunity to my colleagues to be able to talk
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- (18) a little bit about what we're doing here and why
- (19) we're exploring these issues. And then we'll
- (20) move right to the first panel.
- (21) My first colleague that I want to
- (22) introduce here is via phone, and that's Jonathan
- (23) Adelstein. He's a little bit busy meeting with
- (24) some important folks today.
- (25) Jonathan, are you on the phone?

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- (1) COMMISSIONER ADLESTEIN: I sure am.
- (2) Can you hear me?
- (3) COMMISSIONER ABERNATHY: Yes. We can
- (4) hear you just fine. So, if you want to make a
- (5) few opening remarks, I appreciate you taking
- (6) the time to get on the phone. And I'm sorry
- (7) you couldn't be with us today.
- (8) COMMISSIONER ADLESTEIN: Thank you,
- (9) Commissioner Abernathy. You've done a great
- (10) job of organizing this, together with the
- (11) Joint Board's staff, folks from the Wireline
- (12) Competition Bureau here, and, of course, our
- (13) excellent state staff.
- (14) I think this is a great en banc
- (15) hearing you've got organized. I'm really
- (16) disappointed I can't be there. I really wish
- (17) I could be in Nashville today, not just
- (18) because I love the Grand Ole Opry. I had my
- (19) tickets; I was ready to go. But there's some
- (20) pressing business here in Washington that you
- (21) may have heard about that keeps me from being
- (22) there. But I'm listening to as much of this
- (23) by audio as I possibly can but, as you
- (24) indicated, I might get called away. There's
- (25) quite a few things going on here today.

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- (1) I do want to join you, Chairman
- (2) Abernathy, in thanking Bob Rowe and Lila Jaber
- (3) for their contributions to the Joint Board. I
- (4) really enjoyed working with both of them so
- (5) much, and I really appreciated the expertise
- (6) and the contributions that they brought to
- (7) this Joint Board. They've been tremendous and
- (8) we're going to miss them dearly. But I'm also
- (9) very excited about working with Commissioners
- (10) Smith and Baum going forward. I think they're
- (11) going to make a great addition, but we'll miss
- (12) our departing colleagues dearly.
- (13) I'd also like to extend a particular
- (14) thanks to the remarkable group of panelists
- (15) who made the time to participate today. I'm
- (16) glad to see that Rich Coit will be there from
- (17) South Dakota so that South Dakota will be
- (18) represented even if I can't make it. All the
- (19) panelists, including Rich and the others,
- (20) bring a rich wealth of experience that will
- (21) really enrich us on these issues. And I think
- (22) together they reflect a diversity of issues
- (23) that we've got to consider in this proceeding.
- (24) While the details at issue in this
- (25) proceeding are really complicated, I can't

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(1) overemphasize the importance of the task at  
 (2) hand. I've spoken a lot about these issues,  
 (3) and clearly Congress has recognized the  
 (4) importance of ensuring that we maintain a  
 (5) specific, sufficient, and predictable  
 (6) universal support mechanism. Putting that  
 (7) directive into concrete terms is a lot of work  
 (8) for us and will have an impact going forward  
 (9) for generations to come on the ability of  
 (10) providers in rural America to deliver high  
 (11) quality, innovative services. And it's going  
 (12) to affect the overall economy in development  
 (13) of the marketplace in those areas.  
 (14) I'm really looking forward to the  
 (15) discussions here. What I can't hear today  
 (16) I'll look at the record. And, once again, I  
 (17) really want to send my thanks to all of you  
 (18) involved in the effort to put this together  
 (19) and tackle these important issues today.  
 (20) COMMISSIONER ABERNATHY: Thank you  
 (21) very much. And we completely understand and,  
 (22) needless to say, this is just the beginning of  
 (23) what these issues – it's just the opening  
 (24) round of comments. So, stay tuned, Jonathan,  
 (25) and good luck.

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(1) And, I think we'll start with you,  
 (2) Commissioner Martin.  
 (3) COMMISSIONER MARTIN: Thank you.  
 (4) Thank you for organizing the panel and thank  
 (5) all the panelists for making the trip all of  
 (6) the way out here and for extending their stay  
 (7) here at NARUC.  
 (8) I also do want to thank and begin by  
 (9) recognizing the efforts of Bob Rowe and Lila  
 (10) Jaber over the last few years. They've  
 (11) certainly been instrumental in a lot of the  
 (12) decisions we've done. I personally have  
 (13) benefitted greatly from their insight and  
 (14) their wisdom as we try to address several of  
 (15) these contentious issues. And I think they've  
 (16) done a pretty good job of public service, not  
 (17) only on this Joint Board but in serving the  
 (18) citizens of their states and serving all of  
 (19) the citizens in the country by their efforts  
 (20) here. So, I do want to wish them the best of  
 (21) luck, and we'll continue to miss both of you  
 (22) as we go forward.  
 (23) As Jonathan mentioned, Congress has  
 (24) required the Commission to ensure that we have  
 (25) a sufficient universal service support

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(1) mechanism to make sure that all of rural  
 (2) America and all of rural Americans have the  
 (3) ability to obtain service at rates that are  
 (4) relatively comparable to those of citizens  
 (5) living in urban areas. And I think that one  
 (6) of the core goals during my time at the  
 (7) Commission has been to ensure that we have the  
 (8) connectivity to the 21st century networks for  
 (9) all Americans, including those who live in  
 (10) rural areas.  
 (11) Today's en banc is certainly going to  
 (12) address some of the contentious and critical  
 (13) issues for how we go about achieving that goal  
 (14) and the future of universal service and the  
 (15) support for those networks.  
 (16) As I have said before and in private  
 (17) meetings with many of you and in some of my  
 (18) previous statements, I do have concerns and am  
 (19) troubled by some of the Commission's potential  
 (20) to request that the Joint Board consider  
 (21) whether a forward-looking economic cost model  
 (22) is more appropriate than for high cost and for  
 (23) non-rural telephone companies. When the  
 (24) Commission explicitly adopted that mechanism  
 (25) for the non-rural companies, they explicitly

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(1) stated that might not be an appropriate  
 (2) mechanism for rural companies.  
 (3) And, indeed, the Rural Task Force has  
 (4) made clear that – one of their cornerstone  
 (5) concepts of their recommendation was the  
 (6) decision to recommend the continued use of the  
 (7) embedded cost mechanism rather than the  
 (8) Commission's forward-looking cost model for  
 (9) sizing universal support for rural carriers.  
 (10) And I continue to be concerned about the  
 (11) implications for them.  
 (12) So, I'm anxious to have the dialogue  
 (13) with the panel today to further understand  
 (14) their views and the options of the Commission.  
 (15) And I equally think that the second panel with  
 (16) regard to ETCs will be an important discussion  
 (17) for the Joint Board. Again, I think that many  
 (18) of the issues related to the ETCs have been  
 (19) widely discussed among the Joint Board, and I  
 (20) think there's many concerns about the level of  
 (21) scrutiny that the Commission should be  
 (22) applying to the ETCs and also how we should be  
 (23) distributing resources there as well. So, I  
 (24) think we will have a spirited, I'm sure,  
 (25) debate on the first and second panel.

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- (1) With that, I'll turn it over to my
- (2) other colleagues.
- (3) COMMISSIONER ABERNATHY: Thank you,
- (4) Commissioner Martin.
- (5) Now, we'll hear from Commissioner
- (6) Dunleavy.
- (7) COMMISSIONER DUNLEAVY: Thank you
- (8) very much, Madam Chairman.
- (9) And I'd like to echo, of course,
- (10) Commissioner Abernathy's comments and
- (11) Commissioner Adelstein's comments and
- (12) Commissioner Martin's comments relative to the
- (13) contributions that were made by both Bob Rowe
- (14) and Lila Jaber. I'll tell you that I for one
- (15) will sorely miss the good counsel and help
- (16) that was provided so freely and generously on
- (17) every question. They were never too busy to
- (18) help out wherever they were asked. They will
- (19) be sorely missed.
- (20) And I think we are, likewise, very
- (21) fortunate to have the opportunity to be joined
- (22) here by Elliott Smith from Iowa, who is doing
- (23) a bang-up job on the ICC task force for the
- (24) telecom committee and NARUC; and, of course,
- (25) Ray Baum, who will bring – who does bring a

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- (1) tremendous amount to the table.
- (2) Lila and Bob are big shoes to fill,
- (3) but I'm sure that over time that that will –
- (4) COMMISSIONER JABER: His are bigger.
- (5) COMMISSIONER DUNLEAVY: – that will
- (6) take place.
- (7) In any event, I think that it
- (8) probably goes without saying that none of us
- (9) here today questions the importance of
- (10) universal service and the issues before us.
- (11) I'm sure, too, that we would all agree that
- (12) our goal is, as the Act directs us, to ensure
- (13) that comparable telecommunications services
- (14) are available in all regions of the country at
- (15) reasonably comparable rates.
- (16) Now, we might even all agree that we
- (17) want new telecommunications capabilities, new
- (18) technology to become available in all areas in
- (19) a very timely fashion. Those are all in
- (20) agreement. And there is, as we have heard
- (21) repeatedly at a variety of meetings and panels
- (22) at the NARUC convention during the week, that
- (23) there is a growing concern over the
- (24) sustainability of the current universal
- (25) service regime in general and its high-cost

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- (1) mechanism in particular. And this suggests to
- (2) me that perhaps more of the same is simply not
- (3) an acceptable answer. Therefore, we're going
- (4) to need to find and agree on a new approach to
- (5) achieving our common goal.
- (6) Now, unfortunately, after reviewing
- (7) the positions offered and the comments in this
- (8) proceeding and the statements of – some
- (9) statements of some of our panelists, I sense
- (10) that we haven't yet made great progress
- (11) towards finding and agreeing on any new
- (12) approaches. Indeed, I have the sense that we
- (13) don't even agree on the role high-cost support
- (14) should play in achieving universal service.
- (15) And so, I sincerely hope that today's
- (16) en banc will give us the opportunity to find
- (17) and explore some new ideas. And I hope that
- (18) instead of what so often happens here in our
- (19) world that instead of finger pointing and name
- (20) calling, that we could use our limited time
- (21) together to discover areas of agreement that
- (22) will help all of us along our path to
- (23) universal service reform and achievement of
- (24) all of our common goals.
- (25) And now, in the interest of

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- (1) preserving time and knowing that I've already
- (2) said too much, I will thank you, Madam
- (3) Chairman, and turn it over.
- (4) COMMISSIONER ABERNATHY: And now I
- (5) want to welcome Commissioner Bob Nelson to his
- (6) first en banc. Thanks for joining us. He's
- (7) been, already, an important part of the team
- (8) as we prepared for this proceeding.
- (9) COMMISSIONER NELSON: Thank you. And
- (10) I do also want to extend my remarks regarding
- (11) Lila Jaber and Bob Rowe. I echo the
- (12) sentiments of Commissioners Abernathy, Martin,
- (13) Adelstein, and Dunleavy. They led the way for
- (14) me and others to join this Joint Board,
- (15) including Elliott Smith and Ray Baum, and have
- (16) set very fine examples for us to follow.
- (17) In terms of what we're going to be
- (18) hearing today, I agree with Tom that, you
- (19) know, perhaps the written comments so far have
- (20) not coalesced behind a unified approach to the
- (21) issues that have been teed up in this proceeding.
- (22) But I am certainly eager to hear the thoughts
- (23) of the panelists today regarding the
- (24) sustainability of the high-cost fund and how
- (25) that can be best addressed through the goals

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- (1) that we're offering today.
- (2) So, with that, I'll close my remarks.
- (3) COMMISSIONER ABERNATHY: And now
- (4) we'll hear from Billy Jack Gregg, Consumer
- (5) Advocate from West Virginia.
- (6) CONSUMER ADVOCATE GREGG: Ditto to
- (7) Bob and Lila. Good luck, God speed in your
- (8) transition to civilian life.
- (9) In my entire time on the Joint Board
- (10) the issues that we faced remain the same.
- (11) It's whether we're going to support access or
- (12) excess. Unlike my fellow commissioners, when
- (13) I read the comments, I did see a broad
- (14) agreement among the parties. It was that
- (15) there is abuse in the system, and it's the
- (16) support that the other guy is getting.
- (17) I hope that as we talk about trying
- (18) to harmonize the currently existing rural and
- (19) non-rural support mechanisms, that we don't
- (20) lose sight of the more distant future and what
- (21) an appropriate universal service support
- (22) system will be in a broadband age that is
- (23) rapidly coming down upon us. And I'm going to
- (24) take any opportunities I have today to elicit
- (25) suggestions from the panelists on steps we can

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- (1) start to take now to transition the universal
- (2) service fund to one that will be appropriate
- (3) in the broadband age. Thank you.
- (4) COMMISSIONER ABERNATHY: Thank you
- (5) very much, Billy Jack.
- (6) And then finally we'll hear from
- (7) Commissioner Lila Jaber from Florida.
- (8) COMMISSIONER JABER: Thank you,
- (9) Commissioner.
- (10) I think that I can take the liberty
- (11) and speak on Bob's behalf as well -
- (12) Commissioner Rowe's behalf that this is an
- (13) awesome body that has been led by a fantastic
- (14) manager/leader in Kathleen Abernathy. I think
- (15) Bob and I can attest to the fact that
- (16) certainly the criticism that the Joint Board
- (17) moves slow has been put to bed under your
- (18) leadership, Kathleen. And I just want to stop
- (19) and recognize you for your incredible ability
- (20) to have the body reach consensus when we could
- (21) reach consensus and be concise about the areas
- (22) that we just simply disagree on in a manner
- (23) that is timely and that has afforded an
- (24) opportunity for folks to respond to different
- (25) options that we put on the table. And I give

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- (1) you complete credit for that.
- (2) And I also want to recognize
- (3) Commissioners Martin and Adelstein for their
- (4) incredible ability to have us think through
- (5) very tough issues. And, frankly, this topic
- (6) in particular, both Kevin and Jonathan have
- (7) been voices and, before you, Commissioner
- (8) Copps, who started out on the board when I got
- (9) on the board and Bob was on the board - just
- (10) for your thoughtful, deliberative manner and
- (11) requesting that we think through all issues
- (12) and being the voices of reason when we
- (13) desperately needed that.
- (14) This is an incredible opportunity,
- (15) commissioners and folks in the audience, to
- (16) think ahead while times that - there are
- (17) state commissioners leaving. And, certainly,
- (18) Bob and I will miss our state colleagues on
- (19) the Joint Board and we recognize you for your
- (20) effort. I see it as a fantastic opportunity
- (21) to move forward. And I think Elliott and Ray
- (22) are two people that can help in that regard
- (23) and my compliments to the selection.
- (24) But I also think it's an opportunity
- (25) to move the universal service program forward.

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- (1) Like all things in all programs, certainly
- (2) government-type programs, there are
- (3) inefficiencies that have to be addressed.
- (4) That's not to take away from the success of
- (5) the program. Billy Jack referenced that a
- (6) little bit earlier, that we have heard that
- (7) there are reforms, and certainly we see
- (8) directly that there are reforms that need to
- (9) take place. And we are excited today to hear
- (10) what those reforms should be.
- (11) But I hope we also remember that this
- (12) is a well-founded, successful program that
- (13) needs to be improved upon and become even more
- (14) sustainable. And the questions I have today
- (15) really go toward trying to figure out what
- (16) these improvements are. In my questions,
- (17) you'll see a theme. I'm really focused on the
- (18) definition of a rural telephone company and
- (19) how that plays a part in this debate going
- (20) forward.
- (21) My compliments, again, to the entire
- (22) group. I wish you the best of luck and I hope
- (23) our paths cross again in some form or fashion.
- (24) We'll see you soon.
- (25) COMMISSIONER ABERNATHY: Thank you

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- (1) very much, Commissioner Jaber.
- (2) And now we'll move toward to the
- (3) panel. I want to emphasize what we would
- (4) love, because we do have your written
- (5) materials, which we have reviewed. If you
- (6) could keep it down to three minutes, which I
- (7) know is really tough – but that's because we
- (8) do want to hear them all, but we want to
- (9) direct specific questions at you.
- (10) If you could also go ahead – we'll
- (11) start with Rich Coit and work our way down the
- (12) line. If you go ahead and introduce yourself
- (13) very briefly, make your presentation. And
- (14) then as questions are asked, if you could
- (15) identify yourself, because we have a record
- (16) that's going to go into the docket. And we
- (17) want to be able to identify which parties are
- (18) supporting various proposals.
- (19) So, we'll start with Rich Coit of
- (20) South Dakota Telecommunications Association.
- (21) MR. COIT: Thank you, Madam Chairman,
- (22) members of the committee – or the board. I
- (23) would just like to thank you for inviting me
- (24) today. I look at this as an honor. And I
- (25) think, looking at other members of the panel,

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- (1) we will have a great discussion today. And
- (2) hopefully we'll get closer to where we need to
- (3) be to get to where we need to be in the
- (4) future.
- (5) I would just like to spend just a few
- (6) minutes here just giving you a little
- (7) background. I am here today representing the
- (8) South Dakota Telecommunications Association
- (9) and also the National Telephone Cooperative
- (10) Association.
- (11) With respect to SDTA, as an
- (12) organization, currently we have 29 member
- (13) companies, all of which are rural telephone
- (14) companies. Twelve of those companies are
- (15) member-owned cooperatives, and 13 of those
- (16) companies we would consider private companies,
- (17) companies that are either owned by family
- (18) businesses – some of those companies are also
- (19) owned by some of the cooperatives, are
- (20) subsidiaries of some of the cooperatives.
- (21) We have three municipal telephone
- (22) companies that are members, and we also have a
- (23) tribally owned telephone company, Cheyenne
- (24) River Sioux Tribe Telephone Authority.
- (25) In terms of the service that those

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- (1) companies provide in South Dakota, they serve
- (2) approximately 152,000 access lines spread
- (3) across 61,000 square miles of South Dakota.
- (4) That accounts for approximately 75 to 80
- (5) percent of the state's geography. And our
- (6) companies serve all or part of eight of nine
- (7) Native American reservations in South Dakota.
- (8) To give you an idea of the true rural
- (9) nature of the companies, the three largest
- (10) communities served by the SDTA member
- (11) companies are Brookings, South Dakota, which
- (12) is a town in the eastern part of the state
- (13) with a population of about 18,504; Hot Springs
- (14) with a population of 4,129. And the third
- (15) largest is Winter, South Dakota, with a
- (16) population of 3,137. So, that will give you
- (17) an idea of the types of communities we serve.
- (18) Obviously, our companies serve
- (19) incorporated and unincorporated communities.
- (20) Some of the unincorporated communities, they
- (21) probably don't even have populations of 20.
- (22) So, we are very sparse in terms of the area
- (23) that we serve. Looking at the population
- (24) density of the counties that are served by
- (25) SDTA member companies, the average density is

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- (1) four persons per square mile. Eleven of those
- (2) counties have less than two persons per square
- (3) mile.
- (4) As a group of companies, as someone
- (5) who's been involved in the telecommunications
- (6) industry and the rural industry in South
- (7) Dakota for a fair number of years, I can say
- (8) that we're proud as an industry of the
- (9) investments that the rural carriers have made
- (10) in South Dakota.
- (11) As a group, they've deployed almost
- (12) 6,000 miles of fiber across the state, which
- (13) includes a backbone network today utilizing
- (14) SONET and EWEM technology. These facilities
- (15) have allowed us to extend frame relay and ATM
- (16) services to any requesting school in our
- (17) service areas. That was done in large part in
- (18) partnership with the Digital Dakota Network,
- (19) which is an entity, a network, of leased
- (20) facilities established by the State of South
- (21) Dakota for use by schools throughout the
- (22) state.
- (23) We have – looking at the local
- (24) facilities' deployment, local exchange
- (25) facilities' deployment, any upgrades of the

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- (1) loop facilities over the past five or six
- (2) years or so, we have been able to reach 250
- (3) communities with DSL services. VDSL is also
- (4) now available in more than 50 of those
- (5) communities.
- (6) There are a number of issues that are
- (7) before the board today. I suspect that
- (8) probably much of the discussion will be on
- (9) forward-looking cost models versus embedded
- (10) cost models. As you can tell from our written
- (11) comments, we have indicated support for the
- (12) embedded cost models. We've – you will hear
- (13) challenges today to – and criticisms of both
- (14) of those methods, and I would just ask the
- (15) Joint Board as you evaluate those criticisms,
- (16) evaluate alternatives to address the issues
- (17) that are presented – first and foremost, we
- (18) believe that the Joint Board needs to,
- (19) whatever it adopts, adopt a mechanism that is
- (20) consistent with promoting continued
- (21) infrastructure investment.
- (22) If you look at the current method
- (23) this is utilized, we believe it certainly has
- (24) been consistent with that. In looking at all
- (25) the investment that has been made in South

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- (1) Dakota, I think in large part we've been able
- (2) to do what we've done as a result of the
- (3) mechanisms that are in place today. So, in
- (4) our view, looking at – you know, there are
- (5) standards in the Act: specific, sufficient,
- (6) predictable. But first and foremost, look at
- (7) what the impact on the investment is going to
- (8) be, because if you don't have that investment,
- (9) that continued investment, you're certainly
- (10) not going to be able to preserve advanced
- (11) universal service, which is the general goal
- (12) that's set forth in the Act. Thank you very
- (13) much.
- (14) COMMISSIONER ABERNATHY: Very good.
- (15) Thank you very much.
- (16) Now, we'll move on to Paul Garnett
- (17) from the CTIA.
- (18) MR. GARNETT: My name is Paul Garnett
- (19) from CTIA. We represent, as you know, all of
- (20) the major providers of mobile wireless
- (21) services in this country in addition to a
- (22) number of small- and medium-sized carriers,
- (23) manufacturers and applications providers.
- (24) First of all, I'd like to thank the
- (25) Joint Board for including CTIA on this panel.

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- (1) Increasingly, the wireless industry is
- (2) contributing to the universal service
- (3) mechanisms, and we also increasingly are
- (4) receiving high-cost support. So, we feel it's
- (5) important that we be included in whatever
- (6) debate there is about the future of the
- (7) high-cost support mechanisms and other
- (8) universal service debates.
- (9) CTIA and its member companies think
- (10) that this proceeding along high-cost and
- (11) contribution-related proceedings and the
- (12) intercarrier compensation proceeding together,
- (13) will have a significant impact on the way
- (14) services – first of all, whether and how
- (15) services are deployed, both information
- (16) services and telecommunications services are
- (17) deployed in rural areas in the foreseeable
- (18) future. So, you have a significant task
- (19) before you.
- (20) In our comments CTIA has presented a
- (21) proposal for reforming the high-cost
- (22) mechanisms. And in developing that proposal,
- (23) we tried to do exactly what Billy Jack Gregg
- (24) described, which is to really try to have as
- (25) long a time period, as long a horizon as

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- (1) possible in developing those proposals; not to
- (2) just look at what the high-cost mechanisms
- (3) should look like in the next couple years, but
- (4) what the mechanisms potentially should look
- (5) like ten years from now when we really have a
- (6) different industry.
- (7) And we considered a lot of different
- (8) things. We considered keeping the embedded
- (9) cost system, competitive bidding, direct
- (10) consumer subsidy, forward-looking cost. We
- (11) considered all those things, and we sat down
- (12) with our member companies over a series of
- (13) calls, just like I know you will go through
- (14) this process on Joint Board calls and among
- (15) yourselves, tried to come up with a proposal
- (16) that basically moves us forward into the
- (17) future and has a mechanism in place that
- (18) basically accommodates what's been happening
- (19) in the industry.
- (20) Taking a step back, in developing our
- (21) proposal, we looked first at the Act, which
- (22) requires that the support mechanisms be – as
- (23) you have all mentioned – predictable,
- (24) sufficient, specific; that the mechanisms
- (25) focus on consumers first and foremost; and

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- (1) ensure that consumers in rural high-cost areas
- (2) have access to the same types of services and
- (3) the same options that are available to
- (4) consumers in low-cost urban areas.
- (5) Beyond the basic framework provided
- (6) in the Act, we also came to agreement on some
- (7) core principles for reform. The first thing
- (8) that we agreed on is that whatever system is
- (9) in place needs to be administratively as
- (10) simple as possible. We all agreed that the
- (11) current system has way too much administrative
- (12) complexity. The second thing we agreed on is
- (13) that whatever system is in place must
- (14) encourage and reward efficiency over time.
- (15) And thirdly, we agreed that whatever system is
- (16) in place has to appropriately target support
- (17) to high-cost areas. It's not enough for the
- (18) mechanisms to calculate what may on average be
- (19) high cost. You have to make sure that the
- (20) support, whatever it is, actually gets spent
- (21) and targeted to those high-cost areas that
- (22) need it.
- (23) So, with that in mind and having
- (24) considered a whole number of possibilities, we
- (25) ultimately agreed that the best system for

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- (1) achieving those goals is one based on
- (2) forward-looking economic cost, which is what
- (3) the Commission and the Joint Board has come to
- (4) agreement on in several instances in the past.
- (5) So, here's our proposal. Basically,
- (6) the way we have laid it out in our comments is
- (7) that over time we transition from our current
- (8) system of five high-cost support mechanisms
- (9) plus two derivative high-cost mechanisms
- (10) created under the high-cost loop mechanism
- (11) down to one high-cost mechanism that
- (12) calculates support based on forward-looking
- (13) economic costs. That mechanism would target
- (14) support to wire centers. Initially, it would
- (15) base support for both incumbents and
- (16) competitive ETCs on the incumbent LEC's
- (17) forward-looking cost for a specific wire
- (18) center. Ultimately, you would develop a
- (19) mechanism that would calculate support for
- (20) specific areas based on the most efficient
- (21) technology in that specific geographic area,
- (22) whether that's wireless or wireline or
- (23) whatever.
- (24) Under whatever mechanism is in place,
- (25) though, we think it's critical that equal

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- (1) per-line support be available on a
- (2) non-discriminatory basis. So, whatever the
- (3) support is based on, whether on wireless costs
- (4) or on wireline costs, support should be equal.
- (5) How do we get there? It's not
- (6) something that would happen overnight. It
- (7) would have to happen over a number of years.
- (8) We would transition, first, big carriers to
- (9) the forward-looking support mechanism. We
- (10) would need to make a number of changes to the
- (11) forward-looking mechanism in order to get
- (12) smaller carriers on it. We would have to get
- (13) rid of state-wide averaging, change the
- (14) benchmarks possibly.
- (15) But two things that definitely will
- (16) need to happen in order to get us there, first
- (17) of all, the Joint Board and the Commission are
- (18) going to have to devote resources to making
- (19) this happen. And I think one of the big
- (20) knocks on the forward-looking mechanism in the
- (21) past is that the Commission did not devote
- (22) appropriate resources to keeping that
- (23) mechanism up-to-date and keeping inputs to the
- (24) mechanism up-to-date. The rules should be
- (25) codified to require frequent updates to the

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- (1) mechanism, whatever it is. And the Commission
- (2) needs to set firm deadlines for that
- (3) transition.
- (4) And we look forward to discussing
- (5) this proposal further with you.
- (6) COMMISSIONER ABERNATHY: Thank you
- (7) very much, Paul.
- (8) And now we'll move on to Jeff
- (9) Reynolds of Parrish, Blessing, and Associates.
- (10) MR. REYNOLDS: Good afternoon. My
- (11) name is Jeffrey Reynolds. I'm a principal in
- (12) the economic consulting firm of Parrish,
- (13) Blessing, and Associates and testifying today
- (14) on behalf of the Independent Telephone and
- (15) Telecommunications Alliance. ITTA is an
- (16) organization of mid-sized telephone companies
- (17) serving thousands of rural communities. ITTA
- (18) member companies serve a large proportion of
- (19) the rural lines in the nation.
- (20) ITTA appreciates the opportunity to
- (21) offer this testimony on the continuing need to
- (22) provide specific, predictable, and sufficient
- (23) universal service, high-cost support for rural
- (24) carriers. ITTA urges you to recommend that
- (25) the FCC continue to use the statutory

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- (1) definition of rural telephone company to
- (2) determine eligibility for high-cost support.
- (3) ITTA advocates that the FCC continue to
- (4) calculate support on a study-area basis for
- (5) rural telephone companies. ITTA also asks you
- (6) to recommend retaining the use of embedded
- (7) actual cost in calculating support level for
- (8) rural carriers.
- (9) The use of the statutory definition
- (10) of rural telephone company to determine
- (11) eligibility for rural universal service
- (12) support has worked well. This definition
- (13) contains multiple criteria for a reason. No
- (14) single attribute could adequately define
- (15) carriers serving rural areas. The record in
- (16) this proceeding confirms that rural areas
- (17) should be treated differently than non-rural
- (18) areas. There also are substantial differences
- (19) among rural areas. Study areas served by
- (20) rural carriers vary significantly in many
- (21) aspects, including line density, topography,
- (22) and demographics. Because of this, use of the
- (23) definition of rural telephone company under
- (24) the Act reflects and captures the variability
- (25) of these markets better than any single test

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- (1) would.
- (2) Further, there is no compelling
- (3) reason to change this definition. Such a
- (4) change in eligibility likely would cause
- (5) certain rural carriers and the communities and
- (6) customers they serve to lose substantial
- (7) support. Considering the many comprehensive
- (8) reform measures currently before the FCC, this
- (9) is not the time to make radical changes to
- (10) universal service support eligibility rules.
- (11) In addition to considering major
- (12) changes to the current system of universal
- (13) service support, the FCC is considering
- (14) comprehensive reform to intercarrier
- (15) compensation. This proceeding will
- (16) disproportionately affect rural carriers. The
- (17) Joint Board must account for these shifts
- (18) before advocating any piecemeal changes to the
- (19) rural universal service fund eligibility and
- (20) calculation rules. The Joint Board should
- (21) take care not to exacerbate the volatile
- (22) regulatory environment already faced by rural
- (23) carriers.
- (24) Similarly, the Joint Board should
- (25) reject proposals to require carriers owned in

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- (1) a holding company structure to average their
- (2) costs holding-company wide or statewide. By
- (3) averaging costs across rural and non-rural
- (4) study areas, many study areas suddenly would
- (5) no longer qualify for high-cost loop support.
- (6) In other words, a rural study area could lose
- (7) its high-cost funding simply because it is
- (8) served by a telephone company that has
- (9) non-rural affiliates. Moreover, any averaging
- (10) approach to a cost-recovery mechanism creates
- (11) implicit subsidies and/or significant
- (12) increases in rates in rural areas. Either
- (13) result would be contrary to the goals of
- (14) section 254 of the Communications Act and work
- (15) to the detriment of rural consumers.
- (16) This proposed change also would
- (17) encourage holding companies that through their
- (18) operating subsidiaries serve both rural and
- (19) non-rural areas to sell off non-rural exchanges.
- (20) Such fractionalization of the industry would
- (21) destroy efficiencies that cannot be matched by
- (22) stand-alone telephone companies. The current
- (23) system fully captures the scale economies of
- (24) holding companies. These efficiencies lower
- (25) the company's reportable costs for universal

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- (1) service support purposes and reduce demand on
- (2) the high-cost fund.
- (3) Finally, ITTA advocates that rural
- (4) universal service continue to be calculated
- (5) using embedded costs and not a forward-looking
- (6) model. The embedded-cost mechanism is the
- (7) most precise method for determining network
- (8) cost. The differences between rural and
- (9) non-rural carriers make it problematic to apply
- (10) a forward-looking high-cost support mechanism
- (11) to rural carriers. The distortions caused by
- (12) a forward-looking cost models are far less in
- (13) the more homogenous non-rural areas. The
- (14) dislocations that have been demonstrated in
- (15) rural areas by using a forward-looking model
- (16) would produce disastrous decreases in funding
- (17) in rural areas.
- (18) There is good reason why the FCC has
- (19) twice declined to adopt the forward-looking
- (20) economic cost model for rural carriers. The
- (21) Joint Board should recommend that the FCC once
- (22) again reject the movement away from embedded
- (23) costs. Thank you.
- (24) COMMISSIONER ABERNATHY: Thank you
- (25) very much, Mr. Reynolds.

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- (1) And now we will hear from Joel Lubin,
- (2) who is with AT&T.
- (3) MR. LUBIN: Thank you very much.
- (4) Good afternoon. I want to thank
- (5) members of the Joint Board for putting the
- (6) hearing together and allowing me to
- (7) participate on the panel.
- (8) Before I address the questions asked
- (9) by the panel, I'd like to put some issues in
- (10) this proceeding in perspective. I'm going to
- (11) attempt to do that and summarize it in three
- (12) minutes, if I can.
- (13) Let me begin and talk about the issue
- (14) of rural versus non-rural in terms of the cost
- (15) methodology. As an individual who
- (16) participated in the Rural Task Force for about
- (17) 27 months, I learned a lot. And what I
- (18) learned at that point in time is that it's
- (19) extremely difficult to create a
- (20) forward-looking costing tool when you're
- (21) dealing with a thousand study areas, or 1200
- (22) or 1300 study areas. The record currently is
- (23) overwhelmed with information and data that
- (24) suggests the dilemma. I'm not saying it can't
- (25) be solved, but if it is going to be solved,

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- (1) you're going to have to spend a tremendous
- (2) amount of resources and a tremendous amount of
- (3) time. Up to this point in time, I have not
- (4) seen that.
- (5) Point number two, before we harmonize
- (6) the issues of costing between rural and
- (7) non-rural, from my point of view, I think there is
- (8) something even more important that requires
- (9) harmonization. And that is the patchwork
- (10) quilt of all forms of intercarrier
- (11) compensation methods. From my point of view,
- (12) I believe the intercarrier compensation issues
- (13) need to be addressed, have to be addressed,
- (14) and they can be addressed. I couple that with
- (15) universal service reform as well.
- (16) And the reason why I believe it is so
- (17) important is because, A, it's broken; and, B,
- (18) depending on how that gets changed, it will
- (19) affect how you answer the questions that are
- (20) before you today. It could, in fact,
- (21) eliminate the need for the questions to be
- (22) answered or, clearly, if they still need to be
- (23) answered, the way in which you solve it would
- (24) in my opinion be fundamentally different.
- (25) Second point is there's another

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- (1) docket - I guess it's the next panel on
- (2) eligible telecommunications carrier. There
- (3) again, I think you have to wait before you
- (4) answer some these questions until you see the
- (5) outcome of that docket. My company has put
- (6) forward the concept - and it's in the record
- (7) of other carriers or participants, as well -
- (8) of identifying a benchmark. That is to say,
- (9) over some level of subsidy that you obtain in
- (10) a particular geography, you conclude that you
- (11) only want to have one ETC. If you only have
- (12) one ETC, the question then becomes, is it
- (13) critical to have a TELRIC method for that one
- (14) ETC in that area if you're not going to have
- (15) multiple ETCs.
- (16) The other thing that I heard today
- (17) and is also in the record is this concept of
- (18) infrastructure. I think that code word for
- (19) infrastructure, as I understand it, is a code
- (20) word of we are in a circuit-switch world
- (21) moving to an IP world. And as we move from a
- (22) circuit-switch world to an IP world, I assume
- (23) incumbents want to ensure that the money that
- (24) they're getting in a circuit-based world will
- (25) still be potentially available in an IP world.

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- (1) I think that's a very legitimate question to
- (2) be looked at.
- (3) I also hear Billy Jack Gregg raise
- (4) the issue of where are we going in the future
- (5) with broadband. I think that's another
- (6) critical point that also has to get addressed.
- (7) And it also fits in with the whole
- (8) infrastructure question. And the reason why I
- (9) perceive it to be important is depending on
- (10) how this evolves, it's going to again help
- (11) begin to answer how these questions should be
- (12) answered and how one transitions the answers
- (13) to these questions in terms of operational
- (14) plans.
- (15) And I'll even just go one step
- (16) further. If we're talking about
- (17) infrastructure ultimately being supported by
- (18) universal service and we're ultimately talking
- (19) about a broadband pipe into the home, then the
- (20) question ultimately comes to how many
- (21) broadband types are you willing to subsidize
- (22) into the home. And so, I would hope we don't
- (23) take legacy solutions and try to superimpose
- (24) them in the new world. So, my bottom line is
- (25) I would hope that the Joint Board should

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- (1) proceed very cautiously with their
- (2) investigation, and it should certainly not
- (3) require devotion of resources, whether they be
- (4) state, federal, or industry resources, prior
- (5) to an order on intercarrier compensation and a
- (6) Commission order on ETC designation.
- (7) Thank you, and I'll be glad to
- (8) respond to questions.
- (9) COMMISSIONER ABERNATHY: Thank you
- (10) very much, Mr. Lubin. That was great.
- (11) Now, we'll hear from Mr. Weller with
- (12) Verizon.
- (13) MR. WELLER: Thank you, Madam
- (14) Chairman, and commissioners for the
- (15) opportunity to speak you today. My name is
- (16) Dennis Weller. As you just heard, I'm with
- (17) Verizon.
- (18) I think that we've all been reminded,
- (19) if we perhaps needed to be, by the recent
- (20) flap over accounting rules at USAC of the fact
- (21) that we're basically skating on the outer of
- (22) limit of what is possible for support in terms
- (23) of the overall size of the federal mechanisms
- (24) using any carrier contribution mechanisms and
- (25) not emphasize any - I think if we do long

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- (1) division by revenues or by connections or by
- (2) phone numbers, we still have a concern.
- (3) There's no magic wand that's going to solve
- (4) that funding dilemma, getting the same money
- (5) essentially to the same people.
- (6) That constraint being there, I think
- (7) we need to consider our main focus in the near
- (8) terms as controlling the size of the fund and
- (9) the measures that ensure incentives for
- (10) operating efficiently, that deal with costs of
- (11) duplication of supporting multiple networks,
- (12) and that also prevent us from expanding
- (13) without meaning to the entitlement that we
- (14) offer to consumers in rural areas in changing
- (15) the kinds of services that they can buy.
- (16) We've made four recommendations that deal
- (17) specifically with those concerns, and I'll
- (18) just list them quickly here.
- (19) First, we recommend that the FCC
- (20) should establish a rebuttable presumption that
- (21) there should be only one ETC in each rural
- (22) serving area.
- (23) Second, in areas where that
- (24) presumption's overcome and for whatever reason
- (25) they have more than one ETC, we need a second

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- (1) line of defense, another control mechanism.
- (2) We propose that that should be a primary line
- (3) approach that essentially de-couples the
- (4) carrier's - the customer's purchase decision
- (5) from how much subsidy they get, which I think
- (6) we need to do to avoid having somebody go
- (7) from, say, one wireline line to adding, say,
- (8) five wireless handsets. And so, \$20 in
- (9) subsidies turn into \$120 of subsidies.
- (10) The third measure that we would
- (11) propose is that at the outset of any new plan,
- (12) the support level should be based on the
- (13) incumbent carrier's actual expenditures during
- (14) the previous 12-month period rather than on
- (15) some level it's already cost us. However,
- (16) that should only be done once going forward.
- (17) And then that should be frozen and then
- (18) indexed so as to provide an incentive to all
- (19) ETCs in each area to operate efficiently.
- (20) And, finally, fourth, I think we need
- (21) to recognize that the larger carriers in rural
- (22) areas providing universal service have
- (23) characteristics in terms of density,
- (24) investment per line, portion of business
- (25) customers in the area, and so on, that really

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- (1) make them much more similar to the non-rural
- (2) carriers than they are to the smaller carriers
- (3) in rural areas.
- (4) And so, it makes more sense, we feel,
- (5) to consolidate study areas within each state
- (6) than on a consolidated basis that a carrier
- (7) that's serving more than 100,000 lines in a
- (8) given state ought to be treated the same way
- (9) as non-rural areas are.
- (10) Those are specific proposals. You'll
- (11) notice we provide incentives for efficiency
- (12) without going through what I think will be the
- (13) agony of developing a new cost model or
- (14) arguing about the inevitable errors in such a
- (15) mechanism.
- (16) I would also caution, given the
- (17) premise in which I started, in trying to
- (18) export the problems of the intercarrier
- (19) compensation world into this world where we're
- (20) already having enough problems dealing with
- (21) the difficulties we're facing here already.
- (22) And, finally, in conclusion, I'd like
- (23) to turn to the question that Billy Jack Gregg
- (24) asked, which is, what do we do about universal
- (25) service in a broadband age. And my answer to

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- (1) that is something completely different. I
- (2) don't think we should kid ourselves that the
- (3) near-term proposals that we're talking about
- (4) in these open proceedings are policy for the
- (5) ages or that they're going to survive more
- (6) than about, say, five years in the face of
- (7) changes I think we can all see coming.
- (8) I'm just going to list three of those
- (9) changes very quickly, and I invite your
- (10) questions during the remainder of the session.
- (11) First, we're all transitioning, we're
- (12) all building IP-based networks. So, as we do
- (13) that, we're going to exchange traffic, we're
- (14) all going to play by Internet rules, not by
- (15) the old circuit switch rules. Those new
- (16) networks and that change in the market is good
- (17) for the consumers. It's going to offer them
- (18) many more choices. But as a side effect, it's
- (19) going turn rural ILECs from net recipients of
- (20) access service to net payers of transit
- (21) service to interconnect with Internet
- (22) backbones.
- (23) Again, that's not a market solution
- (24) that we ought to try to change, but we need to
- (25) take account of it in considering what the

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- (1) requirements are going to be to meet our
- (2) universal service goals in the future.
- (3) Secondly, in terms of contribution,
- (4) simply put, we have a sector-specific approach
- (5) to contribution today, or certain
- (6) contributions from certain carriers. We're
- (7) one of only a handful of countries around the
- (8) world to try to do that. Most countries do it
- (9) out of general revenue. And by that, I don't
- (10) mean state plus interstate telcom revenue; I
- (11) mean the federal budget. A sector-specific
- (12) tax works if you can identify the sector.
- (13) Going forward as the telcom sector emerges
- (14) with a larger Internet, we're not going to be
- (15) able to do that and we're not going to tax the
- (16) larger Internet as whole. So, we have to work
- (17) through another funding source. That may be
- (18) painful but I think this may be like democracy
- (19) in that it's the worse solution except for all
- (20) the others.
- (21) And, finally, we have a certain
- (22) notion of how the universal service funding
- (23) mechanism works. Money goes into a fund,
- (24) comes out of a fund in terms of monthly
- (25) checks. The checks supported a fine, local

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- (1) service. And I think all of that framework is
- (2) going to be rethought for the future.
- (3) If I have a broadband connection to
- (4) the world, I may get my voice application from
- (5) anyone. It could be a VoIP provider in
- (6) Estonia. Unless we want to get into the
- (7) business of having USAC send checks to
- (8) Estonia, we probably need to rethink the
- (9) structure of that. We probably need to start
- (10) funding infrastructure more directly, perhaps
- (11) through up-front grants. One advantage of
- (12) that, I think, also is it decouples the
- (13) decision of what to support from the decision
- (14) about what to regulate. And I don't mean to
- (15) give you the answer to either of those, but I
- (16) suggest those decisions ought to be made
- (17) independently.
- (18) So, with that, I'll stop. And I
- (19) invite your questions. Thank you.
- (20) COMMISSIONER ABERNATHY: Thank you
- (21) very much, Mr. Weller.
- (22) And now, Mr. Dale Lehman from the
- (23) Alaska Pacific University. You probably came
- (24) the furthest. Thanks.
- (25) DR. LEHMAN: Probably flew the most

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- (1) hours, I think, yes.
- (2) Thank you for the opportunity to come
- (3) and participate in this panel. I don't
- (4) believe this panel exists because of the
- (5) theoretical differences between
- (6) forward-looking and embedded costs. I do
- (7) believe this panel exists because embedded
- (8) costs have a unique property in that they are
- (9) intimately tied to the actual costs of
- (10) providing universal service. And only
- (11) forward-looking costs provide the basis for
- (12) creating an illusion that somehow universal
- (13) service can be provided far more cheaply than
- (14) it is today. And I think that that illusion
- (15) is produced in three fundamentally flawed
- (16) ways, all of which have been provided to you
- (17) in various pieces of testimony.
- (18) One is this vision that somehow the
- (19) rural ILECs' costs are rapidly increasing. In
- (20) fact, they have pretty much matched inflation
- (21) on a cost-per-line basis. And I think the
- (22) best benchmark to compare that to is states'
- (23) own price cap proceedings in which 38 states,
- (24) their average X factor for productivity they
- (25) expect in a local exchange pretty much matches

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- (1) the inflation rate, which is what the
- (2) high-cost fund is also matching.
- (3) The growth in the high-cost funds,
- (4) which undeniably has been large in the last
- (5) five years, has been due primarily to a
- (6) restructuring from implicit to explicit
- (7) support, to some extent to the acquisition of
- (8) rural exchanges from larger carriers and
- (9) subsequent investment, to some extent through
- (10) the re-initializing of the cap that was in
- (11) place over the 1990s, and a very slight extent
- (12) to an increase in lines. But it's not that
- (13) the cost - the cost per line has not been
- (14) increasing dramatically. So, it's an illusion
- (15) to think that there's some waste that's
- (16) occurring suddenly in the last five years. It
- (17) was either there all along or it hasn't been
- (18) occurring.
- (19) The second is this perception, the
- (20) allegation of systematic waste and
- (21) inefficiency that goes on. And I think the
- (22) only evidence that's been provided of
- (23) systematic inefficiency concerns the issue of
- (24) the number of rural carriers and whether
- (25) massive consolidation would, in fact, be a

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- (1) good idea. And I suspect we may have some
- (2) more discussion of this, but I would just
- (3) point out that I don't think - I think the
- (4) cost savings are unproven and, in any case, I
- (5) think it is a very bad idea for rural areas to
- (6) think that you should be urging a massive
- (7) consolidation of rural telephone companies.
- (8) The third illusion of waste that goes
- (9) on is probably the most disturbing. And
- (10) that's this vision that technology is changing
- (11) and somehow it has dramatically reduced the
- (12) cost of providing universal service. I don't
- (13) think that comports with the facts on the
- (14) ground with the exception of possibly
- (15) switching. Loop costs have not experienced
- (16) that kind of technological progress. And
- (17) what's more troublesome is if you really
- (18) believe it has, we should be talking about a
- (19) different issue that's hardly been raised.
- (20) And that's that if carriers made
- (21) prudent investments in the past when
- (22) technology was different and now technology
- (23) has rendered the costs far lower than what
- (24) they already spent, they have under-recovered
- (25) those investments to this point in time, and

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- (1) we need to be talking about how to make them
- (2) whole in the sense of the prudent investments
- (3) they made in the past. And this is important
- (4) in a forward-looking sense because future
- (5) investment in rural areas depends on how you
- (6) treat the investments that were already made
- (7) in rural areas.
- (8) So, if you really believe that
- (9) technology has made the current technology
- (10) obsolete, we should be talking about how do we
- (11) ensure that carriers have an incentive going
- (12) forward to invest in the next generation of
- (13) technology, which will also be made obsolete
- (14) at some time in the future.
- (15) And, finally, I would say that I
- (16) think I agree with a couple of things that I
- (17) heard, that the choice of embedded costs and
- (18) forward-looking cost really shouldn't divert
- (19) you from far more important issues. And I
- (20) think intercarrier compensation, how to fund
- (21) competitive, eligible telecommunications
- (22) carriers, as well as the contribution that
- (23) comes in for USF are far more important and
- (24) far more worthy of your time than chasing
- (25) after a forward-looking cost standard.

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- (1) Thank you.
- (2) COMMISSIONER ABERNATHY: Thank you
- (3) very much, Dr. Lehman.
- (4) And, last but not least, Dr. Lee
- (5) Selwyn will be giving us a presentation from
- (6) Economics and Technology, Inc.
- (7) Thank you, Dr. Selwyn.
- (8) DR. SELWYN: Good afternoon,
- (9) commissioners. Thank you for the opportunity
- (10) to speak with you this afternoon. I will
- (11) summarize my written statement emphasizing a
- (12) couple of key points.
- (13) I think that the policy that has been
- (14) developed over the years, and you heard a lot
- (15) of it in the remarks so far this afternoon,
- (16) has been focused on rural carriers. I believe
- (17) that fundamentally universal service policy
- (18) has to be focused on consumers. And
- (19) consumers' interests may not coincide
- (20) precisely with the service providers that
- (21) serve these areas. Consumers' interest -
- (22) and, incidentally, consumer interests come
- (23) both with respect to rural consumers as well
- (24) as consumers in non-rural areas who are being
- (25) asked to contribute to the high-cost funding

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- (1) mechanism.
- (2) For the consumers who contribute,
- (3) obviously, as the total size of the fund
- (4) escalates and their surcharges continue to
- (5) rise, that's clearly a concern. But for
- (6) consumers in rural areas, if the size of the
- (7) fund continues to escalate at the rate at
- (8) which it has been escalating in recent years,
- (9) the political basis for continuing this
- (10) support mechanism could well erode. And the
- (11) very fact that some of the discussions that we
- (12) are having here today are taking place is
- (13) evidence of that. And that is not necessarily
- (14) in the interest of rural consumers who are
- (15) looking for ways to assure that service is
- (16) available in their community.
- (17) Second point is that there's been
- (18) some discussion about the effect of CETCs
- (19) entering in rural areas, getting
- (20) certification, and drawing funds from the
- (21) high-cost support mechanisms. Concerns are
- (22) expressed that if CETCs erode rural LEC
- (23) revenues, causing - further escalating the
- (24) size of the fund and not allowing the rural
- (25) LECs to shed costs as rapidly as they might be

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- (1) shedding revenues.
- (2) Interestingly, these are not new
- (3) arguments. We've heard these arguments. I've
- (4) been involved in this field now for
- (5) 30-some-odd years, and we've heard these
- (6) arguments at every stage of the entry of
- (7) competition into almost every sector of the
- (8) telecom industry. And this is simply the
- (9) latest incarnation.
- (10) If we have a national commitment to
- (11) competition, I don't think it's appropriate to
- (12) carve out certain segments of the country and
- (13) simply declare competition as nonfeasible and
- (14) not to be supported. If we subsidize
- (15) incumbents and do not subsidize competitors
- (16) serving the same types of customers in the
- (17) same areas, we create very perverse
- (18) incentives. We deny customers in those
- (19) communities access potentially to more
- (20) efficient, lower cost, and perhaps more
- (21) functional - more highly functional
- (22) technologies and alternate services. It's
- (23) hard for a competitor to come in and compete
- (24) with a subsidized incumbent. It's hard enough
- (25) for a competitor to compete with an incumbent.

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- (1) If the incumbent is subsidized, it may make
- (2) entry almost impossible.
- (3) Competition at a certain level is
- (4) going to happen as we move more toward
- (5) broadband. Intermodal competition that the
- (6) Commission has expressed such interest in in
- (7) recent years in other fora, it will come to
- (8) rural areas. And rather than bury our heads
- (9) in the sand and assume it won't have any
- (10) effect as long as the CETCs as are excluded
- (11) from the subsidy mechanism or CLECs are not
- (12) certified and therefore do not receive
- (13) subsidy, there will continue to be revenue
- (14) erosion.
- (15) With respect to the issue of embedded
- (16) versus forward-looking costs, years ago all
- (17) local exchange carriers were regulated on the
- (18) basis of embedded cost under a system
- (19) regulation known as rate-of-return regulation.
- (20) At that time, the carriers would submit
- (21) extensive rate cases, sometimes 15 or 20 or 25
- (22) witnesses, extensive financial and other data.
- (23) Commissions would review this, would determine
- (24) the legitimacy of investments, legitimacy of
- (25) various operating expenses, would conduct

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- (1) audits and reach conclusions as to the overall
- (2) revenue requirement. They would consider all
- (3) sources of revenue that were available to the
- (4) LEC.
- (5) When we speak of embedded costs in
- (6) the context of rural carriers - and the
- (7) notion that these somehow are actual costs, I
- (8) think raises some serious question. Nobody is
- (9) really looking at these costs. They may be -
- (10) they may not have increased in inefficiency,
- (11) but they certainly have an incentive to
- (12) continue to escalate spending and escalate
- (13) their operating costs if they can be assured
- (14) reimbursement.
- (15) It seems to me what we need to move
- (16) to is a system that will eliminate perverse
- (17) incentives, that will eliminate incentives of
- (18) larger carriers to sell off smaller exchanges
- (19) because they have been able to access more
- (20) high-cost support incentives that would favor
- (21) incumbent technology and incumbent carriers
- (22) over entrance. And, as a general matter,
- (23) doing these things will make - will really
- (24) satisfy and achieve the goals of the Telecom
- (25) Act, which is to give to rural communities

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- (1) access to the same and equivalent services
- (2) that are available in urban areas and at
- (3) prices that ultimately will come to be
- (4) comparable to those available in non-rural
- (5) areas.
- (6) Thank you. And I'd be happy to
- (7) respond to any questions.
- (8) COMMISSIONER ABERNATHY: I want to
- (9) thank all our panelists. You did exactly what
- (10) we asked you, to give us a high-level summary,
- (11) raise a lot of questions.
- (12) So, I think what I'll do is for the
- (13) first round we'll start to my right. We'll
- (14) start out with Commissioner Jaber, and then on
- (15) down to Commissioner Martin. And because
- (16) we've got enough time, I think each
- (17) commissioner can go with two questions. If we
- (18) still have time after that, we'll do another
- (19) run.
- (20) COMMISSIONER JABER: Let me seek your
- (21) guidance, Madam Chairman. I have a question
- (22) that I would like to pose to any panelist who
- (23) wants to comment on it. And then I have a
- (24) second specific question.
- (25) The first one is as I said in the

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- (1) introduction. I want to focus a little bit on
- (2) the definition of the rural telephone company.
- (3) And I heard panelists specifically address
- (4) that.
- (5) Mr. Coit, you took a specific
- (6) position on it. And my question to you, and
- (7) then generally to the panelists, is I think
- (8) that there's recognition that some carriers
- (9) are receiving support from the program having
- (10) met the definition of rural telecommunications
- (11) carrier company, but yet serve in a non-rural
- (12) area. In my state, in particular, I know of
- (13) one that is in the Disney area. Disney is not
- (14) rural in Florida. I pose that to anyone who
- (15) wants to comment on it.
- (16) And then, Dr. Lehman, my question to
- (17) you is one that comes from confusion and I
- (18) apologize for that. I'm not sure if you were
- (19) advocating that we go back and make companies
- (20) whole by doing rate cases. When you
- (21) referenced, you said that perhaps it's a
- (22) question of these incumbents who have not
- (23) fully recovered the cost of infrastructure.
- (24) All I could think of was, are you advocating
- (25) for rate cases?

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- (1) DR. LEHMAN: No. I think the rate
- (2) case is an inefficient way to go about that.
- (3) But I think the point is if the money was
- (4) already spent and it was spent when newer
- (5) technology that is presumably much cheaper -
- (6) which I actually don't accept as far as loop
- (7) access goes - but if that's your premise,
- (8) then it's much cheaper, to provide access to
- (9) loop facilities. The money was well spent in
- (10) the past, but it hasn't yet been recovered.
- (11) You can't just sort of pull out and say, oh,
- (12) well, the cost has gone down so now you get
- (13) half of what you got before. Because the next
- (14) round, nobody is going to invest in the newest
- (15) technology without a much more accelerated
- (16) fashion of recovery.
- (17) In some sense, it means the
- (18) depreciation was inadequate in the past
- (19) because we're now saying the economic reality
- (20) is these facilities really don't have much of
- (21) a life left or don't have much value left.
- (22) But you're stuck with them on the books
- (23) because the world has changed, not unlike
- (24) stranded costs in electrics, which I know you
- (25) have a lot of experience dealing with. And

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- (1) generally the principle has been accepted that
- (2) stranded costs are an issue that needs to be
- (3) dealt with. I think there is a huge stranded
- (4) cost issue in telecommunications if you
- (5) believe the premise that costs have
- (6) dramatically come down.
- (7) COMMISSIONER ABERNATHY: Go ahead,
- (8) Dr. Selwyn.
- (9) DR. SELWYN: We don't know that those
- (10) costs haven't been recovered because we don't
- (11) have any traditional rate of return analysis
- (12) of revenues and costs. What we have is a
- (13) funding mechanism that is sort of cost driven,
- (14) but is not really focusing on what we might
- (15) term a traditional revenue requirement.
- (16) What we do know is that when
- (17) exchanges are being sold off, rural exchanges
- (18) are being sold off, the prices that the buyer
- (19) is paying for them are multiples of book
- (20) value, which would certainly give an
- (21) indication that buyer expects not just to
- (22) recover the book value of that investment, the
- (23) embedded cost, but will in excess of the book
- (24) value.
- (25) So, I think in point of act, if

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- (1) you're going to continue to rely on embedded
- (2) costs, you must make the very kind of
- (3) determination that Dr. Lehman has suggested is
- (4) inefficient. That is, you must make a
- (5) determination as to whether or not that
- (6) subsidy is required, whether or not all
- (7) sources of revenue – some of which may be
- (8) below the line and non-regulated but
- (9) nevertheless flow to that infrastructure –
- (10) are, in fact, not fully sufficient to recover
- (11) the investment. And I don't believe there's
- (12) ever been a demonstration to the contrary.
- (13) COMMISSIONER JABER: And the
- (14) definition issue and whatever follows.
- (15) MR. COIT: Can I speak to that first,
- (16) please?
- (17) My name is Richard Coit. With
- (18) respect to the rural definition issue, and you
- (19) mentioned the fact that we had taken a
- (20) position on that. And in our comments, we
- (21) have taken the position that – with respect
- (22) to determining distribution of support that
- (23) the rural definition that's contained in the
- (24) federal Act should be used. It would seem
- (25) that that – I guess you can raise an argument

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- (1) as to, you know, what the legal ramifications
- (2) might be to try to pursue some other
- (3) definition.
- (4) But the fact of the matter is that
- (5) the law today defines rural telephone
- (6) companies differently under the ETC
- (7) designation provisions. And it would seem to
- (8) us that you have to maintain some consistency
- (9) with that because of the public interest
- (10) standard that is there. That is there for the
- (11) purposes of evaluating whether a carrier
- (12) should receive federal universal service
- (13) funding and through designation as an ETC.
- (14) One of the concerns that we have
- (15) with respect to the way things are working
- (16) today, is it appears to us that there are
- (17) competitive carriers that if you looked at them
- (18) in total, you know, certainly would not be
- (19) receiving rural support if you look at the rural
- (20) definition. They're receiving rural support
- (21) simply because they're providing service in a
- (22) rural area. And that accounts for – I think we
- (23) noted in our comments that it appears that that
- (24) may account for about 25 percent of the support
- (25) that's going out to competitive carriers. And

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- (1) that's a concern that we have that we do believe
- (2) should be addressed.
- (3) MR. WELLER: Commissioner, there's a
- (4) famous article in economics called the
- (5) Disneyland Dilemma and maybe that was
- (6) anticipating your question. I don't know.
- (7) Let me just mention a couple facts in framing
- (8) the answer to your question. First of all, a
- (9) large number of – as you know, midsized
- (10) carriers have been growing a lot recently.
- (11) And a lot of the lines that we're talking
- (12) about here are those that they have acquired
- (13) from larger carriers. So, there are already
- (14) constraints on the support that they receive.
- (15) So, for a lot of – a the large portion of the
- (16) ones we're talking about, this may not be that
- (17) great of a change to treat them as non-rural
- (18) because respectively they're capped at that
- (19) level already.
- (20) There are also some safety catches
- (21) already built into the system, the
- (22) safety-valve system. And it probably makes
- (23) sense to continue that sort of cap for
- (24) extraordinary circumstances where it's really
- (25) necessary to make large investments in a

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- (1) particular area. Having said that, though, I
- (2) think if you look across the larger
- (3) companies – incidentally, my company would be
- (4) affected by this. I think our estimate is it
- (5) would probably cost us about \$7 million per
- (6) year in support to do what I've proposed. But
- (7) we need to look at ways to preserve the
- (8) support so it's directed to where it's really
- (9) much needed.
- (10) I think if we're looking at carriers
- (11) who, either because of their size have
- (12) economies of scale similar to larger companies
- (13) in terms of large portions of their,
- (14) essentially, overhead parts of their
- (15) operations or else because of the areas that
- (16) they serve in terms of density loop investment
- (17) and so on, aren't that different an operation
- (18) than non-rural companies, then we do, I think,
- (19) have to start to think about the wisdom of
- (20) treating them in the same category as much
- (21) smaller companies.
- (22) And as far as the definition is
- (23) concerned, again, I'm not the attorney here.
- (24) This could be my revenge on lawyers trying to
- (25) do economics. My understanding is that the

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- (1) definitional differences set forth in the Act  
 (2) is with respect to certification of the ETCs.  
 (3) And the Commission is not obligated to use  
 (4) that as a dividing line in terms of the way  
 (5) funding is structured and indeed only arrived  
 (6) at that after several years of deliberations  
 (7) as a matter of convenience. So, they can  
 (8) depart from that if the Joint Board of  
 (9) commissioners finds that suits what they need  
 (10) to do.
- (11) MR. GARNETT: Just to follow on  
 (12) Mr. Weller's point, the Act in section 254  
 (13) does not talk about rural carriers. It talks  
 (14) about consumers in rural high-cost areas.  
 (15) This is a point actually made back in course  
 (16) of the RTF proceeding by the Vermont and Maine  
 (17) Commissions, and the Commission noted that in  
 (18) the order itself in a footnote buried in the  
 (19) back of the item, but I do remember it.  
 (20) I think the critical thing here is  
 (21) that whatever support mechanism we have has to  
 (22) target support to rural areas, not to rural  
 (23) carriers or to carriers based on whether they  
 (24) might be big or small. So, your example of  
 (25) Sprint in Florida is a good one but -

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- (1) COMMISSIONER JABER: Smart City.  
 (2) MR. GARNETT: I'm sorry?  
 (3) COMMISSIONER JABER: Just for the  
 (4) record, it's Smart City Telcom.  
 (5) MR. GARNETT: Okay. Well, the other  
 (6) example is Sprint has 2 million lines in  
 (7) Florida. That is the one I thought you were  
 (8) thinking of. But in any case it could be that  
 (9) Sprint does serve some high-cost areas or the  
 (10) company you were talking about does serve some  
 (11) high-cost areas. And whatever support  
 (12) mechanism we have in place should target  
 (13) support to those high-cost areas.  
 (14) One of the problems with the current  
 (15) system is we have this problem of averaging.  
 (16) So, under the current system if you have a  
 (17) study area that has 2 million lines in it and  
 (18) there are high-cost and low-cost areas in that  
 (19) study area, you're not going to get support  
 (20) under most cases. And the same thing is true  
 (21) under the non-rural mechanism where you average  
 (22) costs at the state level.  
 (23) We think ultimately the better system  
 (24) is to get rid of the statewide averaging and  
 (25) study area averaging and target support to

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- (1) wire centers or to a specific, small  
 (2) geographic region. And that, we think, is  
 (3) more consistent with requirement of the Act.  
 (4) COMMISSIONER ABERNATHY: Why don't we  
 (5) go ahead and move on to Billy Jack.  
 (6) CONSUMER ADVOCATE GREGG: It's hard  
 (7) to know where to start. There are so many  
 (8) issues and so many questions. But I guess we  
 (9) may as well start with this, I'm sure you all  
 (10) saw this on the cover of the USA Today  
 (11) yesterday, the story about universal service  
 (12) paid out to rural companies.  
 (13) The allegations in the story and the  
 (14) anecdotes that were given is that there are a  
 (15) number of small rural companies that were  
 (16) earning well into the 20 percent range, paying  
 (17) out large dividends and large salaries to  
 (18) their employees, that nevertheless pulled down  
 (19) large amounts of federal universal service  
 (20) funds.  
 (21) There are currently state universal  
 (22) service funds that take a last look after the  
 (23) mechanism has run before they determine  
 (24) whether any additional funds or support should  
 (25) be paid out. They look at a bottom line,

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- (1) whether that's earnings or a certain specified  
 (2) amount of revenues over the earnings. The  
 (3) federal universal service fund for rurals does  
 (4) not look at costs. And, in fact, local  
 (5) switching does not even - I'm sorry, looks at  
 (6) cost. Local switching does not even look at  
 (7) cost in paying out support.  
 (8) Has the time come for the federal  
 (9) universe service support mechanisms to take a  
 (10) last look, either based on total revenues  
 (11) produced by the loop - and we considered  
 (12) unseparated loop costs - or to look at the  
 (13) bottom line return in determining whether  
 (14) additional federal universal service funds  
 (15) should be paid out? And I'll just put that  
 (16) open to any of the panelists.  
 (17) MR. WELLER: I guess we need a  
 (18) volunteer. I'll step forward.  
 (19) I think this is sort of a fundamental  
 (20) question we have to ask ourselves about  
 (21) philosophy here before we get into specific  
 (22) details, because there are all sorts of ways  
 (23) that we can go back to more regularly  
 (24) approaches. I've already mentioned, you know,  
 (25) constructing cost models and tried to

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- (1) prescribe costs. We can also sort of – we
- (2) can go back and audit people trying to look
- (3) for bad actors, or we can suck back into
- (4) regulation, processes that are starting to
- (5) step away from it.
- (6) I think the answer to your earlier
- (7) question about what do we do in a broadband
- (8) age is that we don't get more with regulatory,
- (9) we get less from regulatory. As I said
- (10) earlier, I think we need to find ways to have
- (11) universal service be efficient, but we need to
- (12) be clever in thinking of ways to do that that
- (13) don't rely on more regulation because we
- (14) probably want to decouple universal service
- (15) from regulation. And the amount of support
- (16) that's needed in area may be separate from the
- (17) amount of regulation that's needed in an area.
- (18) So, I would be very concerned about a
- (19) mechanism that would require us to go back and
- (20) do essentially a rate case on every company at
- (21) the end of every year, even though I think
- (22) that's well intentioned.
- (23) I think something that sets incentives
- (24) in the structure of the payouts in the
- (25) manner that we've had good results from, is

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- (1) incentive regulation both at the federal level
- (2) and the state level in the last 15 years is a
- (3) simpler, less contentious, and ultimately more
- (4) productive way of going about things.
- (5) CONSUMER ADVOCATE GREGG: Dr. Selwyn?
- (6) DR. SELWYN: Thank you. You know,
- (7) the proponents of embedded cost as the basis
- (8) for support seem to want to have it both ways.
- (9) They want to retain the trappings of a
- (10) regulatory burden while not actually – in
- (11) terms of the basis for funding without
- (12) actually accepting the mechanism of regulation
- (13) to determine that the funding is reasonable.
- (14) What we have right now is – and I
- (15) think there's very strong evidence of this –
- (16) is that carriers in rural areas who are
- (17) getting high-cost support are also able to
- (18) exploit – and I don't mean that in a
- (19) pejorative sense. They're able to exploit
- (20) their infrastructure to develop new revenue
- (21) sources from broadband services, DSL, other
- (22) things that are capable of producing revenues
- (23) sufficient to defray all their costs. And in
- (24) those circumstances it seems to me that it's
- (25) entirely unreasonable for anyone outside of

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- (1) those communities to also be asked to provide
- (2) subsidy.
- (3) As I mentioned, there is strong
- (4) evidence that these properties are valued at
- (5) well in excess of embedded costs, which means
- (6) that people buying them – smaller companies,
- (7) smaller midsize companies that are buying
- (8) rural exchanges are prepared to – are willing
- (9) to in effect capitalize future excess earnings
- (10) by paying premium prices over the cost of
- (11) support for those assets.
- (12) That in itself is evidence of the
- (13) sufficiency of the existing revenues from all
- (14) sources, because that's what the buyer looks
- (15) to. The buyer does not limit the scope of a
- (16) decision to regulated revenue. The buyer
- (17) looks at all revenues. At an aggregate level,
- (18) the holding companies that own a lot of
- (19) exchanges that are receiving high-cost support
- (20) are similarly being traded. Their equities
- (21) are being traded well in excess of book
- (22) values. So, their investors, their public
- (23) stockholders, are making a similar kind of
- (24) choices.
- (25) We don't – in a sense – maybe I

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- (1) would be forced to agree that maybe we don't
- (2) need to do general rate cases on each of these
- (3) companies because the evidence is overwhelming
- (4) that their revenues are sufficient without
- (5) support. But if a company wants support, it
- (6) seems to me it has to be asked and made to
- (7) make a showing that that support is required.
- (8) MR. GARNETT: In response to your
- (9) question, we don't think that, you know, the
- (10) commissioners should get in the business of
- (11) punishing companies for making money. But at
- (12) the same time I think that we don't think it's
- (13) appropriate for universal service to be one of
- (14) an ETC's best profit centers.
- (15) And under the current system, under
- (16) embedded cost system, and also under the
- (17) forward-looking system, carriers are
- (18) guaranteed a rate of return under the
- (19) high-cost universal service mechanisms. And
- (20) that rate of turn, by the way, was
- (21) determined – was based on the then – the
- (22) cost of capital for Bell operating companies
- (23) 16 years ago, 11.25 percent.
- (24) I think that USAC does a pretty good
- (25) job of paying out high-cost subsidies to the

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- (1) carriers that receive them. I'm guessing that
- (2) they always get their check from USAC
- (3) eventually. There's no risk associated with
- (4) universal service. So, let's get risk-related
- (5) profits out of the universal service
- (6) mechanisms.
- (7) One thing that CTIA has proposed
- (8) among a number of fixes to the current system
- (9) is to basically reduce that 11.25 percent to a
- (10) lower number that would reflect – that
- (11) basically gets that risk-related profit out of
- (12) the universal service mechanisms. Ultimately,
- (13) we think that profits should come from
- (14) consumers, not from the universal service
- (15) mechanism.
- (16) COMMISSIONER NELSON: Mr. Reynolds.
- (17) MR. REYNOLDS: Jeff Reynolds with
- (18) ITTA.
- (19) Some of this rate-of-return-bashing,
- (20) I'll call it, is it's a little bit misplaced.
- (21) First of all, I'd like to correct the notion
- (22) that there's a guaranteed return that comes
- (23) out of rate-of-return regulation.
- (24) Particularly in the federal rules, it's the
- (25) opportunity to earn 11 and a quarter. And

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- (1) that just doesn't come cruising in there
- (2) easily.
- (3) Also, relative to the cost recovery
- (4) mechanism of high-cost universal service,
- (5) while I agree with Dr. Selwyn that in
- (6) evaluating acquisition companies certainly
- (7) look at all revenue streams that are
- (8) available. There's considerable time between
- (9) when deals are struck and when those deals are
- (10) consummated. Particularly for ILECs, there's
- (11) a considerable process where that's vetted
- (12) through both the state and the federal
- (13) regulatory agencies.
- (14) So, while there's obviously – you
- (15) know, what this historic revenue streams have
- (16) been as a practical matter when these
- (17) companies acquire rural exchanges, oftentimes
- (18) there's considerable investment, considerable
- (19) risk that goes along with that. You don't get
- (20) paid back instantaneously. You know, the
- (21) current embedded cost, rural high-cost
- (22) universal service mechanism works on a lag
- (23) basis. So, you're getting a return on your
- (24) unseparated loop costs, but it doesn't all
- (25) come back.

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- (1) And, in fact, as you lose lines to
- (2) competition over time, you're undergoing
- (3) considerable risk. In a way an embedded cost
- (4) mechanism – and without even the necessity
- (5) for a rate case, it's self-correcting in the
- (6) sense that – to the extent that the reporting
- (7) mechanisms are in place there, there's a lot
- (8) of accountability, and it can be measured and
- (9) monitored. And as Dennis suggested –
- (10) although you don't necessarily want to get
- (11) that business – if there are abuses and bad
- (12) actors out there, there's a way to get at them
- (13) right now. So, I don't – I find a lot of the
- (14) rhetoric on this unfounded.
- (15) DR. LEHMAN: This is Dale Lehman.
- (16) Returning to your pointing to the
- (17) newspaper, it seems to me there's three
- (18) courses of action to deal with with issues of
- (19) abuse.
- (20) One of them is, as you suggest, not
- (21) looking at the earnings of the company. But I
- (22) share Mr. Weller's concerns that we're headed
- (23) down a road of much more regulation and really
- (24) full blown rate cases for every single rural
- (25) company.

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- (1) A second course of action is better
- (2) auditing. Auditing is not perfect, but
- (3) certainly can be done and more resources put
- (4) into auditing can catch the, quote, bad
- (5) actors.
- (6) The third course is the one that Mr.
- (7) Weller suggested, and I think has a lot of
- (8) appeal, which is just to have better
- (9) incentives on the cost side and a price cap
- (10) mechanism which essentially you have on the
- (11) overall fund today, having frozen the size of
- (12) it. You know, it has a lot of appeal.
- (13) The only thing I caution you is to be
- (14) careful what you ask for because when you put
- (15) strong cost-reducing incentives in place, that
- (16) means strong cost-reducing incentives. And
- (17) some of those might be in terms of not rolling
- (18) out broadband as quickly because despite the
- (19) ability to leverage the existing
- (20) infrastructure and make broadband revenues,
- (21) many companies have such low take rates on
- (22) broadband currently that it is not a
- (23) profitable investment. And they will think
- (24) harder about making those investments in the
- (25) future.

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- (1) So, before you go down the road of
- (2) throwing out auditing and saying what you want
- (3) is stronger incentives, at least make sure
- (4) that you thought through that you really want
- (5) cost reduction to be first on the mind of all
- (6) the companies under universal service funding.
- (7) DR. SELWYN: Lee Selwyn.
- (8) I don't think this is an issue of bad
- (9) actors and good actors. Clearly, you can
- (10) always find some bad actors, and that's what
- (11) the USA Today article has identified.
- (12) But we have a system that does not
- (13) encourage efficiency, that rewards
- (14) inefficiency. And even without impugning the
- (15) integrity or honesty of anybody, the fact is
- (16) that when a company is confronted with an
- (17) opportunity to have its costs recovered, to be
- (18) made whole, irrespective of the way it runs
- (19) its business, that is an absolute, guaranteed
- (20) ticket to inefficient operations. And we try
- (21) to address that to the larger ILECs with price
- (22) cap regulation. And unless we are prepared to
- (23) do similar types of monitoring as we did in
- (24) the pre-price cap days under rate-of-return
- (25) regulation for these smaller companies, these

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- (1) inefficiencies will persist. And it's not an
- (2) issue of bad actors. It will persist simply
- (3) because the institution encourages it.
- (4) CONSUMER ADVOCATE GREGG: My second
- (5) question deals with the role of the states.
- (6) Under the current universal service mechanisms
- (7) of the federal government, if a rural company
- (8) qualifies for support, it receives that
- (9) support, irrespective of what the state does
- (10) with rates or with its state universal service
- (11) fund or whether it has a state universal
- (12) service fund. The Tenth Circuit Court of
- (13) Appeals directed the FCC and the Joint Board
- (14) to develop a support system for non-rurals that
- (15) contains some sort of inducements to the
- (16) states to help support universal service.
- (17) Indeed, the Tenth Circuit said that it had to
- (18) be a joint effort of states and the federal
- (19) government.
- (20) Do you believe that it would be
- (21) appropriate to require states to do certain
- (22) actions first in terms of rates, in terms of
- (23) state-supported state universal fund and to
- (24) maximize those state resources prior to
- (25) calling on consumers in other states to help

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- (1) support their rates within their state?
- (2) And I'll ask Mr. Quoit first and then
- (3) Mr. Garnett.
- (4) MR. COIT: Thank you. We definitely
- (5) believe that something needs to be done along
- (6) the lines of encouraging states to take a
- (7) share of the universal service burden. Over
- (8) the last several years we have seen in
- (9) non-rural areas, I think, two or three
- (10) additional ETCs designated. In the rural
- (11) areas of South Dakota – and not necessarily
- (12) all of the rural areas of South Dakota, but we
- (13) have at this time the incumbent has an ETC;
- (14) one wireless carrier has an ETC; another
- (15) wireless carrier that – actually, two other
- (16) wireless carriers have applied, and it
- (17) certainly appears that the second wireless
- (18) carrier that applied has a fair shot at
- (19) getting ETC status.
- (20) And I look at that and it seems to me
- (21) that the reason it is happening is that our
- (22) state Commission has absolutely no skin in the
- (23) game. They're looking at it as a way of
- (24) improving wireless coverage, period. And it's
- (25) made really without regard to, I think, the

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- (1) real facts of some of these – the reality of
- (2) the low densities in some of these areas.
- (3) Golden West Telecom cooperative is
- (4) the largest cooperative in the state of South
- (5) Dakota. It covers about 25,000 square miles.
- (6) If you look at that and you consider that area
- (7) to be a state, it would be the 41st largest
- (8) state in the country. And it serves only 2.1
- (9) access lines per route mile of facility
- (10) throughout that entire area on average. Does
- (11) it make sense to be designating two, three,
- (12) four ETCs within that area? We can talk about
- (13) inefficiencies and waste so forth, but that
- (14) whole issue of portability and the number of
- (15) ETCs that are designated, the states have to
- (16) be accountable. And I don't think today they
- (17) are.
- (18) You mentioned the benchmark. It
- (19) seems to me that that is a critical element
- (20) going forward to making sure that, you know,
- (21) there isn't some abuse. You know, should
- (22) companies be getting a bunch of USF if their
- (23) local service rates are 6, 7, 8, \$9 a month,
- (24) no. I don't believe they should, and I think
- (25) there's a reason for those benchmarks. And

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- (1) that is to not necessarily to require
- (2) companies to move their rate up to a
- (3) particular level, but make sure that if they
- (4) don't that the modest support they get is
- (5) going to be impacted by that.
- (6) MR. GARNETT: We definitely think
- (7) that states have an important role to play,
- (8) and the Tenth Circuit has said they do. And
- (9) in the non-rural proceeding that's certainly
- (10) something you looked at. And in our comments
- (11) one thing that we noted is that in many cases
- (12) you have a situation where rates in rural
- (13) areas are actually lower than they are often
- (14) in urban areas. Sprint went into considerable
- (15) detail on this issue in its comments. SBC
- (16) talked about this issue a couple of
- (17) proceedings ago, in the non-rural proceeding.
- (18) One idea that we talked about which
- (19) ultimately didn't make it into our comments
- (20) but I think is actually kind of an interesting
- (21) idea is to develop an affordable nationwide
- (22) rate and support a percentage of costs that
- (23) are above that benchmark, use that as your
- (24) benchmark. And that way you can encourage
- (25) states to do more to increase rates for rural

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- (1) ILECs and for ILECs generally and to get us to
- (2) a situation where rural ILECS are getting more
- (3) than 17, 18, 19, 20 percent of their revenues
- (4) from customers and away from a situation right
- (5) now where you have carriers getting 80
- (6) percent, in some cases 90 percent of their
- (7) revenues from a combination of universal
- (8) service and access.
- (9) COMMISSIONER NELSON: Let me pick up
- (10) on something Dr. Selwyn has mentioned. And
- (11) that is that no one is looking at the cost and
- (12) that there is certainly no incentive to
- (13) control cost under the system.
- (14) And I'd like to ask either Dr. Lehman
- (15) or Mr. Reynolds. I think Mr. Weller has a
- (16) proposal which responds to that point. And
- (17) that is to look at the indexing of actual
- (18) expenditures, looking back at the actual loop
- (19) cost over a 12-month period and indexing them.
- (20) Would this be a suitable way to look at
- (21) controlling costs for rural telcos and should
- (22) this be applied to all ETCs in the area?
- (23) Either Dr. Lehman or Mr. Reynolds.
- (24) DR. LEHMAN: This is Dale Lehman. As
- (25) I was trying to indicate, I think one of the

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- (1) real appeals of this proposal is that it does
- (2) give cost-reducing incentives. But whether or
- (3) not that's what you want, I mean, we all think
- (4) about the good kinds of cost-reducing
- (5) incentives, which are to avoid waste and
- (6) inefficiency. Some of the cost reduction
- (7) might take the form of not rolling out new
- (8) services well in advance of demand, which many
- (9) rural carriers have done. So, I'm not
- (10) entirely sure that maximizing cost reducing
- (11) incentives is always a wise thing to do.
- (12) But on the face of it, I think that
- (13) does address a lot of the concerns. And for
- (14) all practical purposes, we are doing that
- (15) today except not on a carrier level. In terms
- (16) of the whole fund, it is indexed to inflation,
- (17) and the fund is not allowed to grow - you
- (18) know, we re-initialize the cap, but it's still
- (19) capped.
- (20) CONSUMER ADVOCATE GREGG: Should this
- (21) be applied to all ETCs in the area, though?
- (22) DR. LEHMAN: I'll deal with that in
- (23) the second panel, because I don't believe this
- (24) is the basis for the competitive ETCs that are
- (25) sitting here today.

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- (1) CONSUMER ADVOCATE GREGG: Mr.
- (2) Reynolds?
- (3) MR. REYNOLDS: I think one of the
- (4) things with - I guess I regard the indexing
- (5) mechanism as unnecessary just from the
- (6) standpoint that the embedded cost mechanism
- (7) that's out there right now is self-correcting.
- (8) I want to circle back to something
- (9) that Mr. Weller said relative to the
- (10) efficiencies that come with holding companies.
- (11) Most of the operating costs associated with
- (12) high-cost loops exist at the operating company
- (13) entity. So, when you've got multiple entities
- (14) within a state, the efficiencies are not
- (15) happening in these non-contiguous areas. I
- (16) think the efficiencies that happen in
- (17) corporate operation expense exists back at the
- (18) holding company level. That flows down
- (19) through the mechanism, so in that sense it's
- (20) almost self-correcting.
- (21) It would probably be interesting to
- (22) look and see over time how the rural companies
- (23) on an embedded cost methodology have
- (24) performed. I know that just from dealing with
- (25) companies such as CenturyTel and AllTel that

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- (1) they're not even hitting the corporate
- (2) operating expense limits right now. So, that
- (3) cap is, to a certain extent, meaningless and
- (4) those efficiencies are flowing through. So, I
- (5) think that going to an indexing approach is
- (6) unnecessary at this point in time.
- (7) CONSUMER ADVOCATE GREGG: Joel?
- (8) MR. LUBIN: I wanted to clarify a
- (9) couple points and also ask Dennis a question
- (10) in terms of his indexing approach, because
- (11) AT&T also put forward an indexing. And I
- (12) don't know if it's the same, so I'm going to
- (13) describe what we talked about and so how
- (14) parties react.
- (15) But for me the dilemma here is that
- (16) the incumbent rural telcos are rate-of-return
- (17) regulated. And when you are rate-of-return
- (18) regulated and then you have, let's say, 1300
- (19) study areas, trying to figure out either a
- (20) price-cap mechanism or a forward-looking
- (21) costing tool for the diversity and richness of
- (22) the 1300 rural study areas, is a very
- (23) complicated process, whether it's a model or
- (24) whether it's a price cap. And so, right now
- (25) the way in which they're regulated is rate of

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- (1) return.
- (2) Now, it's true that we have a cap on
- (3) the high-cost fund, but that cap is only on
- (4) rural telephone company incumbents and it's
- (5) indexed in aggregate. The CLECs who come in,
- (6) be it wireless or wired, if they're a CETC,
- (7) however much money they get is above and
- (8) beyond the cap, the fund.
- (9) So, my question to Dennis is what
- (10) AT&T put forward was the concept of once a the
- (11) CETC shows up, be it wired or wireless you, in
- (12) effect, look at what the incumbent per line is
- (13) getting. The incumbent going forward, if they
- (14) lose a lot of lines such that their subsidy
- (15) per line could skyrocket because they're
- (16) rate-of-return regulated, their costs really
- (17) aren't shed, but if, in my extreme, let's say
- (18) they lose half their lines just to make a
- (19) point. The subsidy per line could be more
- (20) than doubled. And we said, that doesn't seem
- (21) to be fair if the incumbent, because a CETC
- (22) wins half the lines and doubles the subsidy
- (23) per line, that the new entrant should get the
- (24) same amount.
- (25) However, it did make sense that if a

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- (1) CETC entered, be it wireless or wired, they
- (2) should get the same amount on day one, but not
- (3) the inflated amount if you're rate-of-return
- (4) regulated and if the incumbent's losing a lot
- (5) of lines. However, there was a balancing act.
- (6) The balancing act is if the incumbent is going
- (7) to be investing aggressively for whatever
- (8) reason, moving from circuit switch to IP.
- (9) Whatever the reason, if they're investing
- (10) aggressively and the overall revenue
- (11) requirement was growing, index the day one
- (12) subsidy per line based on the overall revenue
- (13) requirement growth of the incumbent.
- (14) And all that is attempting to do is
- (15) create a rough-justice balancing act so that
- (16) if incumbent is losing a lot of lines and
- (17) they're rate-of-return regulated, the subsidy
- (18) per line skyrockets, the new entrant shouldn't
- (19) get the higher amount going forward. But if
- (20) the incumbent is investing a lot to upgrade
- (21) their infrastructure, then presumably someone
- (22) else who's going to try to compete is going to
- (23) also have to upgrade their infrastructure.
- (24) And so that was the indexing that we put
- (25) forward.

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- (1) So, my question for Dennis is, is
- (2) that the kind of indexing you were talking
- (3) about, because when I'm listening to some of
- (4) the respondents on the panel, I hear some
- (5) people saying that they really can't support
- (6) that concept? But my question is, if you
- (7) bifurcated it the way I have just done, do
- (8) people have a different view in terms of
- (9) seeing it as a rough-justice solution?
- (10) MR. WELLER: Rather than go back
- (11) through all of that, it might be easier for me
- (12) to explain what exactly I'm proposing.
- (13) First of all, I don't think we
- (14) should - first of all if we adopt my earlier
- (15) proposal of one ETC per area, then the issue
- (16) of bifurcation becomes moot. Where we haven't
- (17) done that, I don't think we should be
- (18) bifurcating. I think we should always be the
- (19) same. I don't think we should be setting up a
- (20) handicapping mechanism. We shouldn't be
- (21) saying to one, you're less efficient and we're
- (22) going to make you a handicap. I don't think
- (23) that's a good idea.
- (24) COMMISSIONER JABER: Excuse me. I'm
- (25) sorry. I just wanted to let you know that the

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- (1) court reporter has signaled that you all need
- (2) to use the microphone a little bit closer.
- (3) Sorry, Madam Chairman.
- (4) MR. WELLER: What we're proposing -
- (5) and I think this is also in answer to your
- (6) question you asked earlier, Commissioner
- (7) Nelson, is that unlike the current overall cap
- (8) on the fund, this would apply to all ETCs in
- (9) all areas, so sort of close that opening in
- (10) the control mechanism.
- (11) Second, it would be specific to each
- (12) area, not averaged over the entire fund. I
- (13) think a funny thing about the incentive
- (14) structure with the current fund is if carrier
- (15) A spends money in year one that affects
- (16) carrier B's draw in year two, and might create
- (17) a little better alignment of interest in
- (18) carrier A's decision, affecting carrier A.
- (19) So, we're proposing specific indexing in each
- (20) area.
- (21) And I already mentioned that there
- (22) might be extraordinary circumstances that
- (23) would require various escape patches or
- (24) safety-valve mechanisms. And I think that is
- (25) actually is a better way of dealing with the

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- (1) kind of service issues that Joel was talking
- (2) about, because ultimately all I can do is
- (3) compare to my own company's experience. We've
- (4) lot of lines over the last few years, and
- (5) nobody's given us a guarantee.
- (6) If you look at a lot of market
- (7) estimates, many on Wall Street predict that we
- (8) will have half as many lines in a few years as
- (9) we had a few years ago. And our response is
- (10) to invest more in our network to create more
- (11) value and generate more revenue. And we're
- (12) doing that without any guarantee or without
- (13) any sort of bailout. I think ultimately down
- (14) the line if you're giving rural carriers
- (15) infrastructure grants, you want encourage them
- (16) to do the same thing to get as much value out
- (17) of their network as possible, not as little.
- (18) And you'd have to ask how much
- (19) regulation or interference with their prices
- (20) you want to step in and do, because it might
- (21) interfere with that process. And, again, I
- (22) don't think you want to get in it sort of at
- (23) this stage on the way there, creating separate
- (24) mechanisms for different carriers in different
- (25) markets. I think you need a specific

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- (1) mechanism that pulls each carrier on a
- (2) per-cost standard. It's set on their starting
- (3) point. It's not based on which particular
- (4) cost model we're trying to take things away
- (5) from them, but saying that going forward
- (6) they're going to have to manage their business
- (7) on this basis.
- (8) COMMISSIONER NELSON: Real quickly,
- (9) Joel, and then we'll move on to another
- (10) question.
- (11) MR. LUBIN: Just to clarify, the
- (12) thought process that I shared with you is
- (13) really for a rate-of-return entity. What I
- (14) just described is unnecessary for, let's say,
- (15) an incumbent like Verizon. The reason why
- (16) it's not necessary is because we're using a
- (17) high-cost model. And the high-cost model is a
- (18) forward-looking model, which does not create
- (19) the problem.
- (20) The fundamental problem that we have
- (21) is we're not using a high-cost model to
- (22) independently calculate it. We're using the
- (23) incumbent's embedded cost. And because of
- (24) that and because we're using rate of return,
- (25) that's why we see the phenomena and the

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- (1) potential risk exposure on wireless expansion.
- (2) And the issue is is there a way to maintain no
- (3) model, rate of return, and create a
- (4) rough-justice balance. That was the question
- (5) I was highlighting.
- (6) COMMISSIONER NELSON: I have a
- (7) question for Dr. Selwyn.
- (8) Dr. Selwyn, in Mr. Reynold's
- (9) testimony he refers to the dubious track
- (10) record of TELRIC. Do you perceive it would be
- (11) more difficult to apply a TELRIC to rural
- (12) carriers having the experience of non-rural
- (13) carriers, or have we learned from that
- (14) experience that would benefit to applying it
- (15) to rural carriers?
- (16) DR. SELWYN: The dubious experience
- (17) with TELRIC is in the eye of the beholder. I
- (18) don't see specifically offhand why would we
- (19) necessarily not be able to construct models
- (20) that would establish some indication of order
- (21) of magnitude for different costs for rural
- (22) carriers given the parameters of their
- (23) circumstances. This is not - quite frankly,
- (24) it's not rocket science.
- (25) These companies, while they each

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- (1) confront unique terrain and density issues,
- (2) they are still, at bottom, using the same
- (3) technology, the same types of facilities, the
- (4) same engineering network architecture. And I
- (5) don't really believe that it is not possible
- (6) to develop - to incorporate them into a
- (7) modeling approach. And what that will do is
- (8) to de-link support from the company's own
- (9) self-serving cost investment and operations
- (10) decisions. It will also de-link the funding
- (11) mechanism from cost allocations, which - I
- (12) was describing to somebody yesterday - as 99
- (13) part art and 1 part science. And I think I
- (14) may be overly exaggerating the amount of
- (15) science.
- (16) We need to come up with mechanisms
- (17) that are out of the hands of the individual
- (18) companies and that provide a robust and
- (19) consistent basis for funding irrespective of
- (20) how these companies are individually managed.
- (21) I don't see in particular reason why that
- (22) cannot be done on a forward-looking basis.
- (23) COMMISSIONER ABERNATHY: Thank you.
- (24) DR. LEHMAN: Could I add something?
- (25) COMMISSIONER ABERNATHY: Not right

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- (1) now, but you'll get a chance. I'm sorry. I
- (2) really want to make sure everybody gets to ask
- (3) questions.
- (4) In fact, my question is kind of a
- (5) follow-up on what Commissioner Nelson started
- (6) with. And that is, I think - Mr. Lubin,
- (7) Mr. Reynolds, Dr. Lehman, the impression that
- (8) I got is you're basically saying - without
- (9) regard to what we do with ETC - that we just
- (10) keep the status quo. There is really no
- (11) changes that need to be or should be made
- (12) today. But most economists would argue that
- (13) we need to at least get a grip on how we can
- (14) create incentives for efficiency.
- (15) And so my question to all of you is,
- (16) is there anything that can be done today, or
- (17) are you saying, let's just - no change?
- (18) DR. LEHMAN: This is Dale Lehman.
- (19) I do think that the idea of the price
- (20) cap has some merit if you want to enhance
- (21) cost-reducing incentives. As I thought about
- (22) it a little more, I think my biggest concern
- (23) is with these very small carriers, some of
- (24) them have - their plant is in a different
- (25) shape. And sometimes carriers change, and all

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- (1) of a sudden they need invest more where
- (2) historically they may not upgraded facilities
- (3) very much.
- (4) And you can handle this through
- (5) special cases, but I guess I just want to
- (6) throw out another alternative, which is maybe
- (7) we cap the fund at the state level. Each
- (8) state gets indexed by inflation the amount of
- (9) high-cost funding it previously got in the
- (10) last 12 months. And then let the states work
- (11) out internally how that filters down to the
- (12) various companies they have within the state,
- (13) which I think on the face of it has the appeal
- (14) to me in terms of having the state make some
- (15) closer-to-the-ground decisions about where the
- (16) money is best used. So, it provides - I
- (17) think it provides a lot more discipline in the
- (18) marketplace without what I would call
- (19) handcuffing individual carriers in a way that
- (20) might be very difficult for a small carrier.
- (21) COMMISSIONER ABERNATHY: Mr. Lubin.
- (22) MR. LUBIN: It's a very tough, tough
- (23) question. My bottom line is the system is so
- (24) fundamentally broken, whether it's USF
- (25) methodology we're talking about now, whether

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- (1) it's USF contribution, whether intercarrier
- (2) compensation. It's fundamentally broken. And
- (3) from my point of view, the most important
- (4) thing in terms of prioritization of resources
- (5) is to try to figure out the intercarrier
- (6) compensation and the contribution methodology.
- (7) Once you've solved that - and, in
- (8) fact, in some of the solutions, in particular
- (9) the ICF, has included various components that
- (10) addresses these issues, in particular the one
- (11) that I've already described that says the
- (12) incumbent rate-of-return carrier should have a
- (13) different subsidy per line than an ETC if the
- (14) subsidy per line is rising because of the
- (15) incumbent losing lines. And the CETC
- (16) shouldn't be given that. And that should be
- (17) clear that that's not going to happen. So,
- (18) you create inefficient entry.
- (19) Thank you.
- (20) COMMISSIONER ABERNATHY: Mr.
- (21) Reynolds.
- (22) MR. REYNOLDS: Thank you,
- (23) Commissioner Abernathy.
- (24) I think one of the presumptions here
- (25) that efficiencies can only be created through

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- (1) regulation is a little bit off the mark.
- (2) Generally speaking, I think that there are a
- (3) lot of reasons why the companies want to
- (4) operate efficiently, certainly just not to
- (5) gain a system of universal service support.
- (6) One of the things – and this kind of
- (7) goes to Dr. Lehman said that you don't want to
- (8) create an incentive that removes an incentive
- (9) to invest in rural America. And aside from,
- (10) you know, kind of the strict language of what
- (11) we think Congress intended with the Act, which
- (12) is to have a specific, sufficient, and
- (13) predictable universal service fund, there's
- (14) also this concept of uncertainty that comes
- (15) along with the idea of continually changing up
- (16) the regulatory scheme so that as you go to the
- (17) capital markets, for instance, to draw down
- (18) money so that you can invest in rural markets
- (19) for rural consumers, that that creates a lot
- (20) of the uncertainty.
- (21) So, I think when Joel describes
- (22) sequencing some of these regulatory events,
- (23) it's – I wouldn't characterize it as business
- (24) as usual. I think that what ITTA is saying in
- (25) this instance is don't change the current

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- (1) system until we get some of these other items
- (2) sequenced properly. And they all need to be
- (3) taken in kind of the wholistic sense. And
- (4) we're not interested in operating in an
- (5) inefficient fashion at all.
- (6) Thank you.
- (7) COMMISSIONER ABERNATHY: And then –
- (8) MR. COIT: Excuse me. May I just
- (9) make a brief comment?
- (10) COMMISSIONER ABERNATHY: Sure.
- (11) MR. COIT: I would like to just – I
- (12) think this needs to be said. And with respect
- (13) to forward-looking cost models or any sort of
- (14) price-capping mechanism – Mr. Lehman
- (15) commented on this a little bit – we're
- (16) talking about a smaller company. I think
- (17) Mr. Lubin indicated earlier and made the
- (18) suggestion that, you know, Verizon loses lines
- (19) and they deal with it.
- (20) A rural carrier losing lines
- (21) obviously because of their limiting economies
- (22) is in a much more difficult position in terms
- (23) of dealing with. In addition to that, you
- (24) know, with respect to the forward-looking cost
- (25) model, you know, one of the reasons that the

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- (1) RTF after their studies recommended that it's
- (2) not appropriate or suitable for rural
- (3) companies was because of the disproportionate
- (4) impact on rural carriers as a result of errors
- (5) in the model.
- (6) I think the disproportionate impact
- (7) that we're talking about if you look at
- (8) that – looking at some sort of price-capping
- (9) mechanism is that when a rural carrier has to
- (10) replace a switch, the percentage of cost that
- (11) that makes up on the entire rural cost
- (12) carrier's of that year is much than for larger
- (13) carriers. They're not in a position to deal
- (14) as easily with substantial investments that
- (15) are needed in their networks because of
- (16) whatever technology that may be coming down
- (17) the road that they really feel their customers
- (18) need in order to get the services that they
- (19) deserve.
- (20) So, you know, I think that is a
- (21) caution that, you know, don't forget about the
- (22) economies that are faced. And they're much
- (23) different and the impacts are much different.
- (24) And I'm not sure that price capping mechanisms
- (25) just as forward-looking mechanisms can deal

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- (1) with that in a very easy way.
- (2) Thank you.
- (3) COMMISSIONER ABERNATHY: Well, that
- (4) sort of leads to my next question, which was,
- (5) in the old technology world, I think, yes,
- (6) that was true because all you were delivering,
- (7) the only revenue source you had from the loop
- (8) to home was voice. And there was a certain
- (9) amount that we believed that consumers would
- (10) pay for voice and that's where we were.
- (11) But as we're moving into a world
- (12) where the pipe to the home can deliver many
- (13) other valuable services so you've got multiple
- (14) revenues streams from that source, how does
- (15) that or how can we factor that in when we look
- (16) at what, if any, changes should be made?
- (17) Because it really changes the way that you
- (18) recover your cost for your plant, because all
- (19) of a sudden the plant can deliver more value
- (20) than it used to deliver in the old world.
- (21) Mr. Lubin, Mr. Coit, and then Mr.
- (22) Weller.
- (23) MR. LUBIN: I want to respond
- (24) directly, but I just want to make a highlight
- (25) on Mr. Coit's point.

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- (1) And my highlight to him is the very
- (2) reason that he is articulating his last point
- (3) is the reason why I was bifurcating the
- (4) difference between an incumbent like Verizon
- (5) versus a rate-of-return entity, literally
- (6) having two different approaches. With regard
- (7) to the broadband, for me, that's a wonderful
- (8) question in the following sense: it comes back
- (9) to the issue – and I'm going to focus on
- (10) rate-of-return rural companies – if you're
- (11) rate-of-return today and you are trying to
- (12) make a decision of do I market – not do I
- (13) deploy broadband investment because if you're
- (14) rate of return, I believe you have every
- (15) economic incentive to deploy investment. Do
- (16) you have the incentive to market the
- (17) broadband?
- (18) And when you're talking about 1300
- (19) companies, everybody is all over the place.
- (20) So, I'm just making a general observation.
- (21) And the general observation is, you made the
- (22) point, well-founded, that says there's going
- (23) to be new revenue opportunities. And the
- (24) point that I want to make, though, is if we
- (25) don't fix intercarrier compensation, then the

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- (1) average intrastate access revenue is five
- (2) cents per minute to originate and terminate
- (3) the rate, and that goes from anywhere from,
- (4) say, two cents to 35 cents – I just quoted
- (5) you the average of five – if they sell that
- (6) broadband pipe and then somebody puts an
- (7) application called VoIP, voice over the
- (8) Internet, over that, they're going to
- (9) cannibalize. And if that customer is a
- (10) high-toll generator in a high-toll traffic,
- (11) well, they're going to cannibalize. So, the
- (12) point is unless we fix intercarrier
- (13) compensation, we don't have the right
- (14) incentive. In fact, we have a disincentive
- (15) for the incumbent to aggressively market that
- (16) product to the rural customer.
- (17) COMMISSIONER ABERNATHY: And, yes, I
- (18) hear you on and – yes. We know that. And,
- (19) unfortunately, this Joint Board, we don't –
- (20) that's not our area or our proceeding. But I
- (21) think at the FCC there is a real recognition
- (22) that intercarrier comp distorts all kinds of
- (23) market behaviors and destroys business plans.
- (24) And the distortions flow over into rural areas
- (25) as well as the non-rural areas. So, I agree

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- (1) we've got to deal with that. And, you know,
- (2) at the FCC we're looking forward to putting
- (3) out a proceeding seeking comment on the most
- (4) recent proposals. And we really appreciate
- (5) all the work that's been done on it.
- (6) So, I think what we're trying to do
- (7) here today is say, in addition to that, what
- (8) else can we do. But thanks for pulling them
- (9) together.
- (10) I can't remember what three people I
- (11) called on, now. I think Mr. Weller and I
- (12) believe Mr. Coit.
- (13) MR. COIT: And I'll be brief. Just
- (14) with respect to the question of whether, you
- (15) know, given the increased value of – what the
- (16) effect of that might be, I would agree that
- (17) certainly there are additional services that
- (18) are provided over those facilities which
- (19) certainly offers some opportunity.
- (20) At the same time, though – I think
- (21) this is in part what Mr. Lubin was getting
- (22) to – we're dealing with the intercarrier comp
- (23) issues and rural carriers on average – and I
- (24) don't know exactly what the percentage is in
- (25) South Dakota today, but we all know that

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- (1) across the country in terms of total revenue
- (2) recovery, looking at rural carriers, much of
- (3) it is wrapped up in assets in USF.
- (4) And to the extent that you may gain,
- (5) you know, some additional revenue from some
- (6) additional services, maybe that's going to
- (7) just be necessary to replace what we've lost.
- (8) But, you know, certainly there's a lot of
- (9) pressures on the other revenues. So, that has
- (10) to be taken into account.
- (11) COMMISSIONER ABERNATHY: Mr. Weller,
- (12) you'll have the final word.
- (13) MR. WELLER: Thank you, Chairman
- (14) Abernathy.
- (15) I think, first of all, as far as
- (16) adding value is concerned, that's what you
- (17) want the carriers to do. You want to
- (18) structure the system so that you can give them
- (19) incentives to do that. Their circumstances
- (20) are very different from ours, of course, but
- (21) we want that same incentive to add value to
- (22) replace what you're losing in your traditional
- (23) business.
- (24) And I think that decoupling the
- (25) support from the variations that we've had,

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- (1) the calculations that we've done in the past,
- (2) is part of that. In other words, you want the
- (3) support to reflect some sort format that they
- (4) can get but they have to work with in order to
- (5) go forward.
- (6) Interestingly, I've just heard some
- (7) interesting programs that the British have
- (8) adopted to address this concern that
- (9) Mr. Lehman raised about putting broadband in
- (10) rural areas and not having anybody sign up.
- (11) That's a little outside of the scope of the
- (12) discussion here. I'd be happy to talk to you
- (13) about it off line.
- (14) But the final observation is simply
- (15) that market structure is an outcome in terms
- (16) of relative sizes of firms and how they're
- (17) organized. And I think that rather than try
- (18) to design the system to preserve the current
- (19) market structure, what we have to do is put
- (20) incentives in place and then let the firms
- (21) respond to those incentives possibly by
- (22) choosing different market structures. In
- (23) other words, if one of the concerns about the
- (24) incentive is to scheme, it's that it becomes
- (25) harder and harder for carriers the smaller and

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- (1) smaller they get and the less averaging you
- (2) have. This may create incentives for carriers
- (3) to restructure themselves so as to better
- (4) position themselves to deal with these market
- (5) realities going forward.
- (6) COMMISSIONER ABERNATHY: Commissioner
- (7) Dunleavy.
- (8) COMMISSIONER DUNLEAVY: Thank you,
- (9) Madam Chairman.
- (10) In honor of Bob Rowe, I was going to
- (11) try to formulate a really complex, multi -
- (12) (Laughter.)
- (13) COMMISSIONER DUNLEAVY: My colleagues
- (14) have asked all the questions and the panelists
- (15) have answered them, so I've got to get back to
- (16) basics here. The basic question posed by this
- (17) panel was, should rural carrier support be
- (18) based on embedded or forward-looking costs?
- (19) Not surprisingly, implicit in all of the
- (20) answers there seems to be significant
- (21) differences of opinion on whether the purpose
- (22) of that support should be to maintain the
- (23) financial health of an incumbent LEC or to
- (24) mitigate the higher cost.
- (25) Let me ask you to assume for a

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- (1) moment - and that's probably dangerous -
- (2) that the purpose of the high-cost support is
- (3) to mitigate cost differences among different
- (4) areas, rather than the different cost among
- (5) different carriers. Given that assumption,
- (6) our task would be to determine if cost
- (7) variations exist among various areas of the
- (8) country. Now, Mr. Coit, perhaps can do a
- (9) better - you might help me out.
- (10) Population density is or appears to
- (11) be a significant driver of cost disparities
- (12) among various areas of the country. Are there
- (13) any other characteristics, perhaps
- (14) topographical, climatic, that contribute
- (15) significantly to such cost differentials?
- (16) MR. COIT: Yes. I think there are a
- (17) lot of them. I think that that's primarily a
- (18) problem in trying to come up with a
- (19) forward-looking mechanism that would be
- (20) accurate enough that you don't have some
- (21) significant errors that cause some impacts
- (22) that you don't want to see. I think low
- (23) density, though, is a huge driver.
- (24) You know, in a lot of cases, I think,
- (25) it boils down to distance. You know, if you

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- (1) just look at the areas, if you only have 2.1
- (2) subscribers per route mile, it's pretty
- (3) obvious that you're going to spend a lot more
- (4) to reach those subscribers. And it's the
- (5) function, I think of a lot of things. And I
- (6) know I'm not giving you much of an answer
- (7) here, but do I think it's a multiple number of
- (8) factors. You know, size of the company
- (9) certainly has a lot to do with it as well in
- (10) terms of number of people that you have - the
- (11) number of people that you have working for the
- (12) company and the number of people that you're
- (13) serving.
- (14) COMMISSIONER DUNLEAVY: That being
- (15) the case, would it make any sense to identify
- (16) a half dozen or dozen types of service areas,
- (17) if you will, reflecting density and other
- (18) significant cost factors and then estimate
- (19) average costs of serving each type of that
- (20) area in an efficient manner?
- (21) MR. COIT: I personally don't believe
- (22) that you should necessarily look at just the
- (23) area served. I really do believe that larger
- (24) companies have some economies and somebody to
- (25) manage it that smaller companies do not have.

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- (1) In a competitive environment, it's certainly
- (2) harder to average and price the way you want
- (3) to price, but I don't think any of us could
- (4) say there isn't some averaging that occurs.
- (5) And I think that, you know, if you're
- (6) looking at areas served rather than the
- (7) companies, I think you're assuming that there
- (8) aren't any of those efficiencies. And I don't
- (9) think that's appropriate. I think you need to
- (10) look at areas served in part, but I think more
- (11) than anything it should be tied to the
- (12) companies directly, and we define the
- (13) companies appropriately based on the areas
- (14) they serve.
- (15) COMMISSIONER DUNLEAVY: I wonder, Dr.
- (16) Lehman, if perhaps - and maybe this is
- (17) further expanding on what Commissioner
- (18) Abernathy asked. Could we invent a similar
- (19) means of estimating costs and perhaps based on
- (20) actual costs, the best-in-class or something
- (21) like that?
- (22) DR. LEHMAN: Two different answers,
- (23) one to the first question. I'm in agreement
- (24) with Dr. Selwyn here. I actually think that
- (25) order of magnitude forward-looking estimates

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- (1) probably can be accurately obtained. My point
- (2) would be that order of magnitude is not good
- (3) enough for small carriers. It's the
- (4) difference between making far too much money,
- (5) far too little money, or possibly the right
- (6) amount.
- (7) And to Mr. Weller's point, I don't
- (8) really think you want to pre-guess the market
- (9) structure and put small companies out of
- (10) business because they can't live with the
- (11) degree of accuracy that you're able to produce
- (12) in the forward-looking cost model.
- (13) Now, having said that, to the last
- (14) question that you just asked, are there other
- (15) ways to come at what a forward-looking cost
- (16) might be. You know, I've done some
- (17) simulations of how forward-looking costs and
- (18) embedded costs differ across a number of
- (19) characteristics. And you can produce fairly
- (20) confident predictions about how different they
- (21) might be, and it's on the order of 10 percent
- (22) or less for loop costs.
- (23) But having done that, in the end,
- (24) what do you come up with? You come up with
- (25) something that's only validated by comparison

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- (1) to embedded costs anyways. It sounds like a
- (2) lot of work to still be - you have to
- (3) validate the results of this to know that you
- (4) have reasonable cost estimates. And there's
- (5) nothing else to look at other than embedded
- (6) costs. So, in the end embedded cost have to
- (7) be the guide to whether you came up with a
- (8) reasonable cost model. You have a thousand
- (9) inputs. And even if you 900 of them are
- (10) accurate, you don't know if you have a
- (11) reasonable output of that model unless you
- (12) compare it to something real. And
- (13) unfortunately the only real data we have to
- (14) compare it to is embedded cost.
- (15) COMMISSIONER DUNLEAVY: That's a
- (16) little different than Dr. Selwyn.
- (17) DR. SELWYN: Just one quick comment.
- (18) Dr. Lehman mentioned the model that he
- (19) developed which compares embedded and
- (20) forward-looking costs. I have looked at his
- (21) paper and reviewed his work. And basically
- (22) that analysis starts with the same set of
- (23) inputs. So, in other words, if the costs -
- (24) if the basic investments numbers are wrong to
- (25) begin with, then the relationship is

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- (1) identified while - while, you know,
- (2) interesting at an academic level, it doesn't
- (3) really teach anything about what happens if
- (4) you apply an efficient forward-looking cost
- (5) model one the hand versus just simply taking
- (6) the books - the costs on the company's books
- (7) as embedded costs as a given. We have no
- (8) information right now as to what that
- (9) relationship is.
- (10) We need to start - even an indexing
- (11) mechanism, for example, simply preserves -
- (12) unless it takes a fresh look at what the costs
- (13) ought to be, then it's simply preserving
- (14) whatever inefficiencies - locking in whatever
- (15) inefficiencies may already be present.
- (16) When the Commission - when the FCC
- (17) and the state commissions initially adopted
- (18) price cap regulation for the larger LECs, what
- (19) they did in virtually every case was to
- (20) conduct a full-blown general rate case to
- (21) establish a going-in rate level. And then
- (22) they indexed from that. They didn't simply
- (23) take whatever the pre-existing rate level
- (24) happened to be and go forward into a price cap
- (25) world.

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- (1) And so, if an indexing mechanism –
- (2) which might, in fact, have some merit going
- (3) forward at least on a transitional basis until
- (4) we get to forward-looking costs. If that were
- (5) to be adopted, we would still need to validate
- (6) the going-in cost levels as the Commission and
- (7) the state commissions did when we went to
- (8) price caps.
- (9) MR. GARNETT: Just getting back to
- (10) the original question, I think we would agree
- (11) that in rural areas you're going to have to
- (12) deal with – especially for small carriers,
- (13) you're going to have to deal with the number
- (14) of other inputs. The Alaska Commission in
- (15) their comments talks about a long list of
- (16) inputs the Commission could consider. We're
- (17) realistic that it's going to take a while to
- (18) put smaller carriers on a forward-looking
- (19) system, and that that system needs to account
- (20) for those differences.
- (21) But the fact is that 75 percent of
- (22) the 1300 study areas that Mr. Lubin has talked
- (23) about are 65 percent of the rural telephone
- (24) company access lines. And those are all
- (25) carriers with over 50,000 lines in a study

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- (1) area. Those aren't the companies that we're
- (2) talking about when we're talking about some of
- (3) the real problems with the forward-looking
- (4) mechanism that we have right now. And, you
- (5) know, we think that it's – it makes sense to
- (6) move those bigger companies. I think Verizon
- (7) said it should be if you have over 100,000
- (8) access lines in the state. In our comments we
- (9) say 50,000. You know, we can split the
- (10) difference, that's fine with us.
- (11) But the point is that for some of
- (12) these bigger rural telephone companies,
- (13) they're looking a lot more like non-rural
- (14) telephone companies that have been under a
- (15) forward-looking mechanism for several years
- (16) now. And in many cases they're much bigger
- (17) than some of the non-rural carriers that are on
- (18) the forward-looking mechanism.
- (19) I think it was either Sprint or
- (20) Verizon in their comments that noted that
- (21) Roseville in California has just over 100,000
- (22) access lines. They've been on a
- (23) forward-looking mechanism, and I think they're
- (24) still in business. They've haven't declared
- (25) bankruptcy. Things are going okay. And so,

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- (1) all of these predictions of sort of dire
- (2) consequences of going to a forward-looking
- (3) mechanism for – especially for the bigger
- (4) rural carriers, I think are a little bit of,
- (5) you know, seriously conclusory statements.
- (6) One of the other things I've also
- (7) heard from a number of people here is that we
- (8) shouldn't do it because it's difficult. I see
- (9) in a lot of the comments it's complex, it's
- (10) difficult. That shouldn't be a reason for not
- (11) picking the right outcome, the right
- (12) mechanism. And we think there are a lot of
- (13) smart people in this room and together we
- (14) could probably come up with pretty good
- (15) forward-looking mechanism that accounts for
- (16) all the differences that we've talked about.
- (17) COMMISSIONER DUNLEAVY: Mr. Reynolds,
- (18) briefly because I've overdone my time.
- (19) MR. REYNOLDS: I'll be brief.
- (20) Responding to Mr. Garnett, first of all, one
- (21) of the things – absolute line size has never
- (22) been an attribute at all to whether somebody
- (23) is rural, whether they have high cost, low
- (24) cost, or whatever. You can have poor study
- (25) areas and we have member companies in a states

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- (1) like Montana, the large, square states,
- (2) noncontiguous operating areas. Line size has
- (3) nothing at all to do with the operating
- (4) characteristics of those companies. It's not
- (5) captured in the cost models.
- (6) And I'd also go back and just –
- (7) there are a lot of smart people in this room.
- (8) There are a lot of smart people associated
- (9) with the Rural Task Force. And when you go
- (10) back and you look at the effort that they did
- (11) in there working paper number four to validate
- (12) how the FCC synthesis model would treat rural
- (13) companies, you find a dislocation of about
- (14) \$1.1 billion in loss of support to the rural
- (15) companies, which included holding companies
- (16) that have rural companies and stand alone
- (17) rural companies.
- (18) Thank you.
- (19) COMMISSIONER MARTIN: Mr. Weller, I
- (20) saw in your testimony and was intrigued about
- (21) your discussion about a presumption of one ETC
- (22) in each area. And I was wondering if you
- (23) could give us insight into how and who would
- (24) chose what the one ETC would be in your
- (25) proposal.

(1) MR. WELLER: That's an interesting  
 (2) question. You keep coming back to who gets  
 (3) the money, don't you? Frankly, I think in the  
 (4) near term there may be a strong presumption  
 (5) that it would be the incumbent because of the  
 (6) cost of dislocation to consider. I think down  
 (7) the road if you're talking about something  
 (8) completely different, thinking beyond the near  
 (9) term, I'd say infrastructure grants.  
 (10) I just sat through a couple days of a  
 (11) conference at the OECD looking at efforts to  
 (12) support rural broadband networks throughout  
 (13) the world. And almost without exception there  
 (14) are upfront grants and almost without  
 (15) exception they're awarded on an itinerant  
 (16) basis, option basis.  
 (17) So, I think in the near term if we're  
 (18) talking about who gets the existing  
 (19) regulation, who gets the existing support, as  
 (20) you know, I have made some proposals along  
 (21) those lines in the past. But I'm not sure  
 (22) they're really applicable today when we're  
 (23) trying to change the framework.  
 (24) So, I think these sort of mechanical  
 (25) changes that I've proposed here today are more

(1) the same kind of service.  
 (2) But I am concerned about one of the  
 (3) things you raise in your testimony and talk  
 (4) about the expansion of the base of universal  
 (5) service contributors to ensure everyone  
 (6) contributes on an equitable basis. And you  
 (7) talk about wanting to have facility and  
 (8) non-facility-based providers of Internet  
 (9) service, all IP-enabled service providers, all  
 (10) cable providers, wireless and satellite  
 (11) providers, and other providers all  
 (12) contributing into the universal service fund.  
 (13) I was wondering if you would assume  
 (14) then that all of those same providers would be  
 (15) able to take out of the universal service fund  
 (16) as well. And if they wouldn't, why is it an  
 (17) equitable basis, which is what keep using as  
 (18) your phrasing, for these providers to pay into  
 (19) a fund that they are not able to take out of?  
 (20) MR. COIT: I guess just generally -  
 (21) and this goes back to, I think - at least  
 (22) ties into some of my opening comments.  
 (23) Whatever mechanism - whatever the mechanism  
 (24) is, you know, as a result of this process and  
 (25) in the future, you know, it really seems to me

(1) reasonable things to deal with to do in the  
 (2) near term. Again, it may seem unfair, but I  
 (3) think in the near term given dislocation costs  
 (4) it's not unreasonable, excepting unusual  
 (5) circumstances to give a strong preference to  
 (6) the incumbent. But I think as we go forward  
 (7) beyond that, let's say, for five years from  
 (8) now, that we'll be freer to think of different  
 (9) solutions, and they would become maybe part of  
 (10) the answer.  
 (11) COMMISSIONER MARTIN: I do know  
 (12) you've laid out some other proposals that we  
 (13) have some interest in as well. But this  
 (14) presumption issue, that's one of the five  
 (15) things that you think should be done in the  
 (16) short run, right?  
 (17) MR. WELLER: Yes.  
 (18) COMMISSIONER MARTIN: The other  
 (19) question I had, Mr. Coit, I certainly agree  
 (20) with many of the concerns you expressed about  
 (21) forward-looking costs, some of your concerns  
 (22) about the wireless and other ETCs' ability to  
 (23) obtain support on the basis of the ILEC's  
 (24) costs without having necessarily incurring  
 (25) some of those costs themselves or providing

(1) that it's got to be tied to those that are  
 (2) investing in the network. And not all  
 (3) providers do that. The other thing -  
 (4) COMMISSIONER MARTIN: But then I just  
 (5) do want to understand. Then what you would  
 (6) say, though, is any provider that does should  
 (7) be able to take out; is that right?  
 (8) MR. COIT: Not necessarily.  
 (9) COMMISSIONER MARTIN: Not necessarily  
 (10) any - not necessarily?  
 (11) MR. COIT: And that's because if we  
 (12) look at the current situation, we've got a  
 (13) situation today where there are carriers that  
 (14) are getting money out of the universal service  
 (15) fund that have stated very clearly that they  
 (16) don't believe that they have  
 (17) carrier-of-last-resort responsibilities. And  
 (18) if you look at cost drivers for rural  
 (19) carriers, in a lot of cases it's those  
 (20) customers that are so remote that they they're  
 (21) the ones that to some - to a significant  
 (22) degree drive high cost. And if there isn't a  
 (23) sincere commitment to serve throughout the  
 (24) area, I just don't believe the carrier should  
 (25) get any money.

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- (1) And I've sat in two ETC hearings and
- (2) that question has been asked. And, you know,
- (3) does the CETC carrier have carrier-of-last-
- (4) resort obligations, and the answer has been
- (5) the same both times: no. And I don't agree
- (6) with that. I think that there's
- (7) distinguishing - you know, I think you have
- (8) to look at who's providing the facilities and
- (9) who's meeting the obligations. And I also
- (10) think you have to look at the area and really
- (11) ask yourself, you know, is this the sort of
- (12) area where it makes sense to be funding
- (13) multiple carriers regardless of who that
- (14) carrier might be.
- (15) MR. GARNETT: If I could actually
- (16) respond to both of your questions in one
- (17) answer, and this is sort of - kind of a
- (18) five - sort of the five years out sort of
- (19) time frame that Mr. Weller was talking about,
- (20) that type of a proposal. You know, once a
- (21) wireline or wireless carrier or whomever
- (22) satisfies the structural obligations for
- (23) getting an ETC designation, whether it's state
- (24) or the FCC, ultimately the true arbiter of who
- (25) should get the support should be the customer.

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- (1) And for that reason, the Commission
- (2) really should think about a long-term solution
- (3) as direct consumer subsidy where you basically
- (4) have a situation wherein you determine, is
- (5) this a high-cost area. It's a narrowly
- (6) defined area. You determine, you know, what
- (7) the most efficient technology is for that
- (8) area. You figure out how much support you
- (9) have available for each customer in that area,
- (10) and let the customer decide who they spend
- (11) their dollar on.
- (12) And that way you deal with both of
- (13) the issues you raised. You deal with who gets
- (14) to get the money out. It should be anybody as
- (15) long as the customer wants that carrier to be
- (16) their provider. And you deal with the issue
- (17) of, you know, whether you should limit support
- (18) to one carrier in an area. If the customer
- (19) chooses a wireless carrier or wireline
- (20) carrier, that choice should be respected and
- (21) that's how the dollar should be spent.
- (22) COMMISSIONER ABERNATHY: Thank you
- (23) very much, Commissioner Martin.
- (24) Thanks to our panelists. What I
- (25) think we will do now is we will take a

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- (1) ten-minute break before we start with panel
- (2) two. I do want to thank everyone, and I know
- (3) some of you are coming back for panel two.
- (4) This was very, very informative and we
- (5) appreciate you traveling here.
- (6) (Whereupon, a break was taken.)
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- (1) \*\*\*
- (2) COMMISSIONER ABERNATHY: Thanks again
- (3) to our panelists. We really appreciate you
- (4) coming all this way. We don't want to waste
- (5) your time, so I think we'll start right away
- (6) with Scott Bergs with Midwest. Again, a
- (7) three-minute presentation, if you could, so we
- (8) can leave plenty of time for Q and A.
- (9) MR. BERGS: Thank you. Again, I'm
- (10) Scott Bergs with Midwest Wireless. And first
- (11) of all, I want to say thank you for the
- (12) opportunity to address these really important
- (13) issues. In this proceeding the Joint Board
- (14) and the FCC will make some decisions that will
- (15) dramatically impact customers' options for
- (16) communications services in the high-cost areas
- (17) of the United States and the overall cost of
- (18) communication services throughout the United
- (19) States.
- (20) The Joint Board and the FCC will be
- (21) guided and informed by representatives of
- (22) small ILECs, from medium-sized ILECs, from
- (23) wireless carriers like Midwest Wireless, and
- (24) many, many others. But in taking into
- (25) consideration all of these important views,

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- (1) perhaps the greatest challenge to each of you
- (2) is to distinguish between how your choices
- (3) will impact Midwest Wireless, CenturyTel,
- (4) small independents, or AT&T, and instead focus
- (5) on how your choices will impact the people who
- (6) are living and working in rural, high-cost
- (7) areas in purchasing communications anywhere
- (8) within the United States.
- (9) I know the dramatic disparity between
- (10) wireless consumer contributions to the fund,
- (11) approximately 22 percent, and the small amount
- (12) of consumer-received benefit from the fund –
- (13) the small amount of wireless-consumer-received
- (14) benefit, about 3 percent. I'd point out and
- (15) highlight that point, the customer
- (16) contribution and receipt, notwithstanding my
- (17) own reference in my written comments to the
- (18) provider contributions. They really are not.
- (19) That's a misnomer. They are passed along to
- (20) the consumer, and I think it's important to
- (21) highlight that fact.
- (22) And, of course, finally, the benefits
- (23) derived, if the funds are appropriately used
- (24) or inappropriately used and efficiently used,
- (25) are consumer benefits. And if they are lost,

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- (1) it's the consumer who loses those benefits.
- (2) Rather than focusing a lot on the actual
- (3) economic disparities, I'd like to focus my
- (4) comments briefly on how those consumers will
- (5) be impacted under the various changes that are
- (6) proposed here today.
- (7) The impetus for U.S. commercial
- (8) dominance throughout the world is really our
- (9) consumers' insatiable thirst for innovation and
- (10) additional value. They continually drive
- (11) providers like Midwest Wireless and everyone
- (12) represented in this panel to be more creative
- (13) and efficient in how they provide services.
- (14) By making changes in this proceeding, we have
- (15) to avoid taking away that customer's power to
- (16) force us to be more innovative and more
- (17) efficient.
- (18) As Congress determined in the '96
- (19) Act, customers in rural high-cost areas
- (20) deserve the same types of services and same
- (21) choices of services as those folks living in
- (22) urban areas, and at prices that are comparable
- (23) to their urban counterparts. While USF reform
- (24) is needed now to ensure the long-term
- (25) realization of these goals, we must be mindful

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- (1) that recently great strides have been made
- (2) towards those acts.
- (3) For example, since our designation as
- (4) an eligible telecommunication carrier in
- (5) Minnesota, Iowa, and Wisconsin, Midwest
- (6) Wireless has expanded its coverage through
- (7) additional power facilities and other
- (8) facilities. That has provided health and
- (9) safety benefits in emergency situations –
- (10) giving consumers the ability to dial 911 in
- (11) areas where they simply could not do that
- (12) before – and for emergency responders who are
- (13) responding to those calls, to be able to
- (14) communicate, to learn facts during the
- (15) sometimes sizable drives or transportation
- (16) periods that don't exist at least to the same
- (17) extent in urban areas as they're trying to get
- (18) to that emergency situation.
- (19) So, the residual benefits that
- (20) Midwest Wireless has been able to provide
- (21) consumers in those rural markets that we serve
- (22) is the provision of broadband. We do that
- (23) through a couple of different networks that
- (24) get an ancillary benefit from the funds and
- (25) the facilities that are developed through

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- (1) those funds. We have a 1xRTT network, which
- (2) will be evolving to an 1xEV-DO network; true,
- (3) high-speed broadband access with mobility; and
- (4) also operate an 802.11 network. The
- (5) efficiencies that are gained are that we can
- (6) share facilities with our standard voice
- (7) provision service facilities. And also, we
- (8) can share personnel, our engineers and our
- (9) service technicians.
- (10) In essence, between Midwest Wireless
- (11) and the other carriers competing in our
- (12) markets, we are giving the customers choices
- (13) for service, service provider, customer
- (14) service, and other incremental value that the
- (15) customers demand. These are the benefits that
- (16) were envisioned by Congress to be derived from
- (17) a dynamic and competitive marketplace, and it
- (18) is important that we keep those incentives in
- (19) place.
- (20) So, what do we need to do? Just a
- (21) couple of quick points. First, I want to
- (22) point out that there is growth in the fund,
- (23) and we need to be careful to not let the fund
- (24) get out of control. But there is an inherent
- (25) cap, at least on the CETC side, in the fund

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- (1) itself. While certainly in the short term,
- (2) because we made some accommodations for the
- (3) ILECs back in the RTF order, there is going to
- (4) be growth in the fund as CETCs enter the
- (5) market.
- (6) In the long term as customers
- (7) continue to fill out the number of connections
- (8) that they're going to acquire, they're not
- (9) going to have six, seven, eight connections.
- (10) So, the unlimited and ever-expanding growth of
- (11) the fund is simply not a reality. We must
- (12) preserve the equality in support to preserve
- (13) those motivations to keep carriers entering,
- (14) competitive carriers entering into these
- (15) markets, and to make sure that the carriers
- (16) there are, in fact, being as efficient as they
- (17) possibly can be. We are starting to see that
- (18) by some of the rural ILECs in our service
- (19) territory. We're seeing the handwriting on
- (20) the wall, and anticipating changes, and are
- (21) therefore starting to find efficiencies that
- (22) they previously claimed simply could not be
- (23) achieved, through shared switching facilities
- (24) and other common service components.
- (25) Making these incremental reforms can

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- (1) ensure that the carriers are motivated to
- (2) passionately fight for those customers,
- (3) ultimately reducing the carrier's reliance on
- (4) government-provided subsidies which are
- (5) furnished at the expense of the customers
- (6) themselves. Specifically, in the short term,
- (7) we can mandate disaggregation, targeting
- (8) high-cost support to the highest cost areas of
- (9) a study area. We can move toward
- (10) forward-looking costs. We can stop system
- (11) gaming of large ILECs acting as small ILECs,
- (12) or identifying themselves as small ILECs. And
- (13) we can eventually move towards portability of
- (14) support as mandated by the Act.
- (15) Taking these steps now will ensure
- (16) the customers have a right to an ever
- (17) increasing expectation of value even in these
- (18) rural areas. Thank you.
- (19) COMMISSIONER ABERNATHY: Thank you
- (20) very much.
- (21) And now we'll turn to David Cole from
- (22) CenturyTel.
- (23) MR. COLE: Thank you. Good
- (24) afternoon. My name is David Cole. I'm the
- (25) Senior Vice President of Operations Support

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- (1) for CenturyTel. I'm testifying today on
- (2) behalf of the Independent Telephone and
- (3) Telecommunications Alliance. ITTA is an
- (4) organization of midsize telephone companies
- (5) serving thousands of rural communities across
- (6) the nation. ITTA appreciates this opportunity
- (7) to testify at this hearing. Through this
- (8) testimony, ITTA urges you to recommend that
- (9) CETCs receive universal service support based
- (10) on their own costs as opposed to the costs of
- (11) the carrier-of-last-resort. ITTA also hopes
- (12) you will recommend that the FCC modify its
- (13) safety-valve rules so as not penalize carriers
- (14) that make investments in the first year after
- (15) acquiring a rural exchange.
- (16) CETCs should have to justify their
- (17) receipt of support based on their own costs.
- (18) The costs of the incumbent simply aren't
- (19) relevant. As carriers-of-last-resort
- (20) throughout the communities that they serve,
- (21) rural ILECs have a fundamentally different
- (22) role. Carriers-of-last-resort must serve
- (23) every single customer that requests service.
- (24) CETCs do not. Carriers-of-last-resort must
- (25) comply with strict service quality and outage

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- (1) reporting requirements to ensure that the
- (2) communities they serve are receiving
- (3) high-quality telecommunications services.
- (4) CETCs do not. Perhaps most important,
- (5) carriers-of-last-resort open their books up to
- (6) regulators and have to prove that their costs
- (7) justify the level of universal service
- (8) support. CETCs do not.
- (9) Just like the ILECs, CETCs should
- (10) have to prove that their costs justify receipt
- (11) of support at the level they request. Today,
- (12) the FCC oversees a system that hands out
- (13) hundreds of millions of dollars to CETCs
- (14) without considering how they perform, what
- (15) their costs may or may not be, or how accurate
- (16) their reporting of customer lists may be.
- (17) Indeed, CETC funding is growing far faster
- (18) than the funding for rural ILECs. From 2002
- (19) to 2005, rural ILEC high-cost loop funding is
- (20) projected to grow approximately \$22 million
- (21) while CETC funding is projected to grow five
- (22) times that amount, or \$110 million dollars.
- (23) Many rural ILECs are actually experiencing
- (24) declines in USF funding today in 2004, and are
- (25) projected to experience even larger declines

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- (1) in support in 2005. Considering the fact that
- (2) ILEC funding is already capped, the best way
- (3) that the FCC could control fund growth would
- (4) be to simply require CETCs to justify their
- (5) receipt of these funds.
- (6) The Joint Board should also recommend
- (7) changes to the method of calculating the
- (8) support for acquired rural exchanges. Today's
- (9) rule creates disincentives to investment in
- (10) these acquired exchanges. When carriers
- (11) acquire rural exchanges, the
- (12) telecommunications plant in these exchanges
- (13) typically it's neglected and requires
- (14) immediate investment to meet minimal service
- (15) standards, let alone to allow provision of
- (16) advanced telecommunications capabilities. The
- (17) current safety valve rules actually provide an
- (18) incentive for carriers to delay by a year or
- (19) more expenditures that would improve service
- (20) for these rural customers. If the FCC wishes
- (21) to encourage carriers to make needed repairs and
- (22) improvements to these exchanges, the FCC rules
- (23) should be changed.
- (24) To alleviate these problems, ITTA
- (25) proposes that acquiring carriers be eligible

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- (1) for support immediately following the
- (2) acquisition of the exchanges, and that the FCC
- (3) should measure the baseline cost-per-loop in
- (4) an acquired exchange on the cost at the time
- (5) of acquisition in order to most accurately
- (6) show the increased investment.
- (7) In closing, ITTA reiterates that the
- (8) continued disbursement of universal service
- (9) funds to CETCs as a factor of carriers-of-
- (10) last-resort costs and a billing address
- (11) customer list is inappropriate and should be
- (12) discontinued. CETCs should receive universal
- (13) service support based on their own costs. It
- (14) is the only means of providing accountability
- (15) needed to ensure that universal service funds
- (16) are efficiently used to accomplish the
- (17) purposes of the Act.
- (18) Thank you.
- (19) COMMISSIONER ABERNATHY: Thank you,
- (20) Mr. Cole.
- (21) Now, we'll hear from Mr. Gene
- (22) Johnson, who is with Fairpoint Communications.
- (23) MR. JOHNSON: Thank you, Commissioner
- (24) Abernathy. You may have remembered that last
- (25) time I appeared before the en banc hearing and

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- (1) you had a clock in front of us. So, therefore
- (2) I have written my statement out to make sure I
- (3) don't go over three minutes.
- (4) I'm Gene Johnson, Chairman and CEO of
- (5) Fairpoint Communications, and we're a holding
- (6) company for rural ILECs operating in 16
- (7) states. Fairpoint's average study area has
- (8) just 8,500 access lines, and many of these
- (9) areas are very costly to serve. Without the
- (10) cost recovery Fairpoint obtains through
- (11) universal service support, we would literally
- (12) be unable to provide these customers with
- (13) affordable, high-quality service. This
- (14) morning - or this afternoon, I'm here on
- (15) behalf of OPASTCO and its 560 rural telephone
- (16) company members, many of which face operating
- (17) challenges similar to ours.
- (18) You may recall that last year in
- (19) Denver I participated on a panel concerning
- (20) the very same subject we're here to discuss,
- (21) the basis of support for competitive ETCs. It
- (22) seems like it's been a lifetime. Over the
- (23) past six quarters since I was last before you,
- (24) the projected support for CETCs in rural
- (25) service areas has increased by something like

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- (1) \$60 million. It represents 80 percent of the
- (2) total growth in the rural high-cost program
- (3) over that same two-year-time period. It's
- (4) clear that the support going to CETCs is
- (5) driving the rapid growth of the high-cost
- (6) program and placing its future viability at
- (7) great risk.
- (8) OPASTCO continues to believe that the
- (9) best way to address this problem is to base
- (10) support for CETCs in rural areas on their own
- (11) embedded costs. This would introduce the same
- (12) rationality and accountability into the system
- (13) for these carriers that already exists in the
- (14) mechanisms for rural ILECs. Moreover, it
- (15) would help to sustain the high-cost program in
- (16) a way that provides every ETC with sufficient
- (17) support and continues to achieve the universal
- (18) service objectives of the '96 Act.
- (19) OPASTCO recommends that the joint
- (20) board or FCC hold industry workshops to
- (21) develop charts of accounts for CETCs in each
- (22) industry segment that will be used for cost
- (23) reporting purposes. Although the types of
- (24) costs reported by wireless ETCs will obviously
- (25) differ from those reported by LECs, there

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- (1) should still be cost reporting parity between
- (2) the ILECs and the CETCs.
- (3) During the period of time when
- (4) accounting rules are being developed, we
- (5) recommend the adoption of the interim wireless
- (6) safe harbor plan that was filed by OPASTCO,
- (7) RICA, and the RTG in the portability
- (8) proceeding. Under that plan, wireless CETCs
- (9) would receive a safe harbor percentage of the
- (10) rural ILEC's per-line support with the
- (11) specific percentage based on the size of the
- (12) wireless carrier. Again, this plan is
- (13) intended strictly as an interim measure that
- (14) would sunset after the FCC adopted
- (15) cost-reporting rules for CETCs.
- (16) In closing, the current portability
- (17) rules have placed the sustainability of the
- (18) high-cost program in serious jeopardy and
- (19) change should not be delayed any longer. It
- (20) seems almost too obvious to say, but the
- (21) high-cost program should only provide support
- (22) to carriers that can actually demonstrate that
- (23) they have high costs. The system needs to be
- (24) accountable to the ratepayers nationwide, the
- (25) consumers, who ultimately fund it.

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- (1) Thank you for inviting me to
- (2) participate in the hearing today. I'd be
- (3) happy to answer any questions you may have.
- (4) COMMISSIONER ABERNATHY: Thank you
- (5) much, Mr. Johnson.
- (6) And now we'll hear from Denise
- (7) Parrish who is with the Wyoming Office of
- (8) Consumer Advocate.
- (9) Thank you, Ms. Parrish.
- (10) MS. PARRISH: Thank you. I
- (11) appreciate the opportunity to be here, not
- (12) only on behalf of Wyoming Office of Consumer
- (13) Advocate, but also as a representative of
- (14) NASUCA.
- (15) I'd like to begin as I did in my
- (16) written statement by reminding you of the
- (17) overarching principals that you need to
- (18) balance. And while I know that you know these
- (19) principals, they're not always discussed in
- (20) the - to the extent that I think that the
- (21) balance requires.
- (22) For instance, there's been a lot of
- (23) talk about the sustainability of the fund, but
- (24) there has been very little mention about
- (25) affordability. And we think that

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- (1) affordability is one of the key items that
- (2) should override your decision making and be
- (3) part of the balance here, and it doesn't get
- (4) discussed to the same degree that many of the
- (5) other principles in 254 get discussed.
- (6) Similarly, access to quality services
- (7) does not get the same amount of discussion
- (8) that access to the fund gets. There was on
- (9) the first panel discussion about who should be
- (10) able to access the fund, but without the
- (11) reminder that the whole purpose of accessing
- (12) the fund is to maintain access throughout the
- (13) nation. We have a wonderful, ubiquitous
- (14) quality network in America, and the whole
- (15) purpose of the fund is to maintain that, not
- (16) to develop competitors, not to develop
- (17) competition, but to, in spite of or in
- (18) conjunction with competition, to maintain the
- (19) network that we have. So, we hope that you'll
- (20) keep that in mind.
- (21) Similarly, the comparability issue,
- (22) we remind you that that ought to be one of the
- (23) key items that goes to the end test. Whatever
- (24) decision that you make as a result of this
- (25) hearing and many other hearings and

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- (1) discussions that you'll have, it ought to be
- (2) the final test of whether your decision is the
- (3) right one should be the comparability of
- (4) rates. Even if that means that you do
- (5) something similar to what you did for the
- (6) non-rurals, which was, if all else fails, a
- (7) state can come in and ask for supplemental
- (8) funding just to show that the comparability
- (9) test is being met.
- (10) So, the NASUCA comments in this
- (11) proceeding go to trying to balance all of
- (12) those issues as well as trying to rationalize
- (13) the fund. We understand that there's a
- (14) sustainability problem, and we understand that
- (15) there's a - are competitive issues. We're
- (16) not against competition. We're not trying to
- (17) create discrimination for or against the
- (18) competitors, but we believe that the fund
- (19) needs to be rationalized.
- (20) And in that regard, relative to the
- (21) two issues that I've been asked to speak to,
- (22) the specific comments suggest that competitive
- (23) ETCs should have support based on their own
- (24) costs but capped at the level of support
- (25) provided to the incumbents. We - I won't go

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- (1) into it now. You have the written statements
- (2) as to why we believe that it's both a fair
- (3) competitive method as well as a
- (4) nondiscriminatory method. We also believe
- (5) that this is the way to remind ourselves that
- (6) the incumbents do have carrier-of-last-resort
- (7) responsibilities at this point,
- (8) responsibilities that have not been picked up
- (9) by many of the CETCs.
- (10) As to the second issue, the issue of
- (11) dealing with bought and purchased exchanges,
- (12) we have not taken a formal position at this
- (13) point. We expect to do so in our reply
- (14) comments. But again, the overarching concern
- (15) should be to not provide incentives to make
- (16) purchases, but at the same time to recognize
- (17) that the buyers have done some marvelous
- (18) things in rural areas once those exchanges
- (19) have been purchased.
- (20) And with that, I would look forward
- (21) to your questions.
- (22) COMMISSIONER ABERNATHY: Thank you
- (23) very much, Ms. Parrish.
- (24) And now we will turn to Dr. Lehman
- (25) from Alaska Pacific University.

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- (1) DR. LEHMAN: Thank you. We hear a
- (2) lot of the phrase, competitive neutrality,
- (3) invoked as reasons why we need the equal
- (4) support rule. And there is nothing in
- (5) economic theory. You won't find the phrase
- (6) competitive neutrality. What you will find,
- (7) the closest concept is the idea of
- (8) discrimination and nondiscrimination. And
- (9) discrimination takes place when equals are
- (10) treated unequally or whenever unequals are
- (11) treated equally. And that last phrase is what
- (12) I think applies here.
- (13) Wireless and wireline technologies
- (14) are just different. They're different in a
- (15) litany of technological, regulatory, and
- (16) market ways, many of which appear in lots of
- (17) the testimony you've been provided with. And
- (18) I'd add one to the list that came from the
- (19) previous panel. It's very appealing, the idea
- (20) of eventually moving to system of consumer
- (21) subsidies where the consumer gets the subsidy,
- (22) the ultimate person we're trying to help. But
- (23) that is not technology neutral.
- (24) In a wireless world that works fine
- (25) to give the customer the subsidy because

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- (1) wireless networks are not built to serve
- (2) particular addresses and customers. They're
- (3) served to - they're built to serve particular
- (4) areas that customers may travel through.
- (5) Wireline technology is geared to specific
- (6) locations. And if you give the customers the
- (7) subsidy, you run into the problem that one
- (8) person may want to use their subsidy for
- (9) wireline and the next house down the road may
- (10) not. But you still have to build the network
- (11) down that road in any case. So, there are
- (12) some important differences in technology that
- (13) need to be recognized, and you can't do it
- (14) through the equal support rule.
- (15) I don't think it is efficient to try
- (16) to equalize wireless and wireline services.
- (17) One of the wonderful things about them is they
- (18) are so different. So, rather than try to say
- (19) we're going to have the same standards and
- (20) they all have to look the same - they don't
- (21) look the same. And I think the principle of
- (22) competitive neutrality, or from the
- (23) discrimination concept, would be that they
- (24) should be treated differently. And by
- (25) treating them differently, I mean that the

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- (1) wireless costs should determine wireless
- (2) support. I have not seen a demonstration that
- (3) wireless carriers in high-cost areas are, in
- (4) fact, the same areas as high-cost areas for
- (5) the incumbents. In fact, I think that quite
- (6) possibly some of the urban areas are, in fact,
- (7) higher cost areas for wireless carriers than
- (8) rural areas. So, I think we need really need
- (9) to have to a demonstration of where the costs
- (10) are a barrier to achieving comparable services
- (11) at comparable rates. And then that should be
- (12) the basis for support.
- (13) I think we should also not mistake
- (14) the intense competition for revenues and
- (15) minutes for competition between the services.
- (16) There is relatively little competition
- (17) directly between wireless and wireline service
- (18) for access. And, in fact, they are
- (19) complementary to a great extent. In answer to
- (20) the point raised about whether wireless
- (21) carriers take as much out of the funds as they
- (22) put into it, one the benefits wireless
- (23) consumers get is the ability to reach anybody
- (24) on a wireline phone by using their wireless
- (25) service. And that was achieved largely

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- (1) through our universal service policies that
- (2) built out the wireline network to reach
- (3) everyone. So, they are benefitting even if
- (4) they are not getting the same number of
- (5) dollars out of the fund as they put in.
- (6) And, finally, I'd make two notes.
- (7) One of them is that to the extent that there
- (8) are allegations that the rural incumbents are
- (9) inefficient, grossly inefficient, to me, that
- (10) undermines any last reason why we should have
- (11) equal support. I mean, presumably, if money
- (12) is being wasted by the incumbents, why does a
- (13) wireless carrier need the same amount of waste
- (14) in order to compete? They simply don't have
- (15) to waste it to begin with.
- (16) And the other point I'd make is that
- (17) there is a sense of competitive sense of
- (18) neutrality that is important and that has
- (19) already come to past. And that is the
- (20) competitive neutrality among wireless carriers
- (21) themselves. We have a rural area in Alaska
- (22) now where there are three wireless ETCs along
- (23) with the wireline ETC. And it seems to me if
- (24) you're going to provide high-cost support to
- (25) one wireless carrier, you pretty much have to

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- (1) provide it to all, because they are competing
- (2) directly for the same customers. And that, I
- (3) think, enlarges the fund considerably.
- (4) COMMISSIONER ABERNATHY: Thank you
- (5) very much.
- (6) Now, we'll hear from Dr. Lee Selwyn.
- (7) DR. SELWYN: Thank you,
- (8) Commissioners. Glad to be back on this panel.
- (9) I appreciate the opportunity to speak with you
- (10) on this subject.
- (11) I was reviewing the statutory
- (12) language and the statute that we've been
- (13) talking about. The statutory language, let me
- (14) just read it again: that customers in rural
- (15) high-cost areas shall have access to
- (16) telecommunications and information services
- (17) that are reasonably comparable to those
- (18) services provided in urban areas.
- (19) That to me implies that the policy
- (20) that the Commission has been pursuing for
- (21) 30-some-odd-years now of encouraging the
- (22) development of competition, the policy that
- (23) was adopted by Congress in the '96 Act, in
- (24) looking to competition to support the
- (25) telecommunications demands of this country,

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- (1) cannot be distinguished between non-rural and
- (2) rural areas. If you develop and maintain a
- (3) support system that in some manner limits the
- (4) opportunities for consumers to benefit from
- (5) competition in rural areas, then the statutory
- (6) mandate is not being fulfilled.
- (7) Now, that said, let me speak about a
- (8) couple of the specifics that are being
- (9) discussed. First of all, let's talk for a
- (10) minute about the equal support rule. My
- (11) belief is that the equal support rule is
- (12) absolutely essential to assure that consumers
- (13) are confronted with efficient choices between
- (14) and among various providers and various
- (15) technologies.
- (16) Now, I actually find myself in
- (17) agreement up to a point, which perhaps is
- (18) unusual, with Dr. Lehman, as to the idea of
- (19) carrying inefficiencies over from rural ILECs
- (20) into CETCs. And the solution to that is to
- (21) use as the basis for support the cost level of
- (22) the most efficient provider. So, if the CETC
- (23) is able to do it cheaper than the rural
- (24) carrier - or the rural ILEC than it is the
- (25) CETC's cost and not the rural ILEC's costs

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- (1) that provide the basis for funding. So, we
- (2) eliminate your concern about inefficiency and
- (3) we eliminate my concern about a lack of
- (4) competitive neutrality.
- (5) CETCs are carriers-of-last-resort.
- (6) There is no proposal out there that suggests
- (7) that any competitor that happens to wander
- (8) into a particular rural community is
- (9) immediately entitled to high-cost support.
- (10) Carriers have to comply with the requirements
- (11) of certification as ETCs, which includes a
- (12) commitment to serve their communities
- (13) ubiquitously. If multiple CETCs and multiple
- (14) wireless carriers are certified as ETCs, that
- (15) doesn't necessarily expand the size of the
- (16) fund since the funding would be based upon the
- (17) number of lines provided by each carrier. So,
- (18) if three carriers divide up the wireless
- (19) segment of the market, then the total draw
- (20) would be essentially the same.
- (21) If you provide differential support
- (22) based upon each carrier's costs or each
- (23) technology's cost, you distort consumer
- (24) choice, you distort investment choice. You
- (25) discourage entry by lower cost - inherently

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- (1) lower cost providers who are being forced to
- (2) compete with subsidized higher-cost companies.
- (3) That denies those customers in those
- (4) communities access to competitive service.
- (5) Finally, on the issue of whether or
- (6) not wireless and wireline are the same, first
- (7) of all, the Commission, I think, needs to be
- (8) consistent. If intermodal competition is to
- (9) be viewed by the Commission as a general
- (10) matter, as demonstrating the presence of
- (11) competition in a market – and certainly this
- (12) has been raised in other areas in section 271
- (13) cases and the triennial review among other
- (14) places, in broadband proceedings – then you
- (15) can't simply decide that oh, gee, in rural
- (16) areas it's a different story.
- (17) Now, are they perfect substitutes?
- (18) Absolutely not. No question about it. But
- (19) they are economic substitutes and there is a
- (20) price at which a consumer – a price
- (21) differential at which a consumer may be
- (22) indifferent as between one or the other. If a
- (23) price of a wireline service is \$100 a month
- (24) and then the price of a wireless service is
- (25) \$20 a month or \$30 month, then there will be

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- (1) consumers who while preferring wireline
- (2) service might decide at that point that the
- (3) preference isn't worth the price difference.
- (4) And that's exactly the kind choices we want
- (5) consumers – we want to encourage consumers to
- (6) make. If we distort those choices by
- (7) subsidizing wireline service to the tune
- (8) of the difference between 100 and 30, that choice is
- (9) eliminated.
- (10) No one is saying they are the same
- (11) service, but they are at a certain level
- (12) economic substitutes. And if intermodal
- (13) competition is going to be a focus of
- (14) Commission policy, you can't change the rules,
- (15) as it were, in rural areas. It seems to me
- (16) that rural, in order to establish a level
- (17) playing field, to encourage efficiency, to
- (18) eliminate the various perverse incentives in
- (19) the present system that looking to provide an
- (20) equal level of support for carriers based upon
- (21) the most efficient carrier's costs is a
- (22) reasonable policy approach. Thank you.
- (23) COMMISSIONER ABERNATHY: Thank you
- (24) very much, Dr. Selwyn.
- (25) And now we'll move to the Q and A, we

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- (1) will start with Commissioner Martin.
- (2) COMMISSIONER MARTIN: Mr. Johnson, I
- (3) heard you state a – I think I heard you state
- (4) a fact that I wanted to follow up on. You
- (5) said that 80 percent of the growth in the
- (6) high-cost fund was not a result of CTEC
- (7) growth. Is that – could you –
- (8) MR. JOHNSON: That's correct. If you
- (9) remember when we re-balanced rates, moved
- (10) things from implicit cost to explicit cost,
- (11) there was a dramatic increase in the high-cost
- (12) fund. Since that was completed, however,
- (13) something like 83 percent of the growth has
- (14) been from CETCs. The fact is that for the
- (15) last, I think, two years the total growth in
- (16) the high-cost fund from incumbents is
- (17) something like 3.1 percent.
- (18) COMMISSIONER MARTIN: And no one on
- (19) the panel disagrees with that?
- (20) MR. JOHNSON: That's based USAC's
- (21) numbers.
- (22) MR. COLE: I agree. The numbers that
- (23) I used were 22 million and 110. And that is
- (24) from 2003 to 2005 the projection by USAC. And
- (25) some of the numbers have been used in the

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- (1) earlier time period. But if look at the
- (2) growth between 2003 and 2005 projected, using
- (3) USAC numbers, you look at the high-cost loop
- (4) fund, it is basically the same percentage. 83
- (5) percent is the increase driven by CETCs.
- (6) MR. BERGS: I have to plead partial
- (7) ignorance and then a little disagreement.
- (8) I've got to admit, I don't know if we look at
- (9) only the last two years. But if we looked at
- (10) 2000 and 2003, 87 percent of the growth in the
- (11) fund was attributable to ILECs.
- (12) MR. JOHNSON: That's correct. As I
- (13) said, that was the period of time when we
- (14) re-balanced rates and moved things
- (15) specifically into the ICLS rates.
- (16) COMMISSIONER MARTIN: And then my
- (17) next question was for Dr. Selwyn. I agree
- (18) with you that the Commission ultimately has to
- (19) be consistent in its approach on intermodal
- (20) competition. I mean, that's an important
- (21) point as we're trying to figure out how we're
- (22) approaching this. And you're right, that has
- (23) been raised in a series of proceeding
- (24) including the TRO.
- (25) But it has also been raised in some

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(1) of the mergers that we've had in front us  
 (2) recently. And in that context, I think we've  
 (3) actually been more skeptical in our  
 (4) conclusions about the current substitutability  
 (5) of wireless per wireline service. So, does  
 (6) that have an impact in your comments today?  
 (7) DR. SELWYN: In fairness I, myself,  
 (8) have been skeptical about the  
 (9) substitutability. So that nobody goes – and  
 (10) I'm sure there will be people here who would  
 (11) go and try to dig out my prior testimony and  
 (12) say, see, he's being inconsistent. As I said,  
 (13) they are not perfect substitutes. But at a  
 (14) certain point they are economic substitutes.  
 (15) I think that in particular in rural  
 (16) areas where we are confronting unusually –  
 (17) what are alleged, at least, to be unusually  
 (18) high costs for wireline services, wireless may  
 (19) be a more viable technical economic substitute  
 (20) than in other areas. And we certainly want to  
 (21) encourage the exploitation of that technology  
 (22) if, in fact, that is true.  
 (23) And then the last thing we should be  
 (24) doing is distorting that or discouraging  
 (25) investment. So, I absolutely agree that we

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(1) are – I don't believe they are perfect  
 (2) substitutes. I don't believe the market  
 (3) has – in the mainstream market, despite  
 (4) attempts by certain incumbent LECs to portray  
 (5) it otherwise, I don't think the mainstream  
 (6) market has made that demonstration. But in  
 (7) particular in rural areas, the potential  
 (8) for – as an alternative, as a lower cost  
 (9) alternative is real and certainly should not  
 (10) be distorted. And that's all I'm saying.  
 (11) COMMISSIONER MARTIN: Thank you.  
 (12) COMMISSIONER ABERNATHY: Commissioner  
 (13) Dunleavy.  
 (14) COMMISSIONER DUNLEAVY: Thank you,  
 (15) Madam Chair.  
 (16) Ms. Parrish, if we base the CETCs  
 (17) support on its own costs, are we assuming or  
 (18) just hoping those costs are lower than the  
 (19) ILEC's costs?  
 (20) MS. PARRISH: Well, our proposal to  
 (21) base its on own costs up to the amount of  
 (22) the ILEC costs. So, it would – the support  
 (23) would also always be lower than or equal to  
 (24) that of the ILEC. I don't think you can  
 (25) assume that it's always going to be higher or

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(1) lower. It's that it's going to depend on the  
 (2) area; it's going to depend upon the density  
 (3) and the build-out. It's that they have some  
 (4) of the same density issues that the wireline  
 (5) carriers do.  
 (6) And, in fact, if you – the other  
 (7) concern I have is that some of the suggestions  
 (8) that have been made that we base it on the  
 (9) model of the lower of the costs, whether it's  
 (10) wireline or wireless, is that I think that  
 (11) again goes to the issue of build-out and  
 (12) assuring that the build-out built in the model  
 (13) is sufficient to actually serve the entire  
 (14) service area. Because if you use the actual  
 (15) construction that's out there now, you might  
 (16) not actually be supporting enough coverage  
 (17) based on some of the wireline model  
 (18) descriptions.  
 (19) COMMISSIONER DUNLEAVY: And one  
 (20) little follow-up. When you're talking about  
 (21) support of customer lines, you're talking  
 (22) about the primary line or all lines?  
 (23) MS. PARRISH: Either way. I think –  
 (24) because the model's generally built to a  
 (25) household, and the addition of one line or two

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(1) lines in terms of the cost models doesn't make  
 (2) very much difference. Now, what we're seeing  
 (3) in terms of the current system where you  
 (4) have – it's based strictly on the number of  
 (5) lines and the ported amount from the incumbent  
 (6) is you're seeing three and four lines in a  
 (7) household being supported, and that clearly  
 (8) doesn't have the cost basis because you don't  
 (9) have four times the cost to serve a household  
 (10) as you do for serving one. I mean, the math  
 (11) doesn't work. You don't multiply by four for  
 (12) every line into that same household.  
 (13) COMMISSIONER DUNLEAVY: That being  
 (14) the case, how do we reconcile that? Do we  
 (15) need Mr. Johnson's workshops and teach people  
 (16) how to do that?  
 (17) MR. JOHNSON: Well, I think you do.  
 (18) I think if you're going to take public money  
 (19) and if you have an obligation to provide a  
 (20) level of service that says that it's good  
 (21) public policy – that you get public money to  
 (22) do that, then I think we have to develop a  
 (23) methodology for insisting that people justify  
 (24) what they're doing with the public money. If  
 (25) that means we have to develop workshops as a

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- (1) way of doing it, put the safe harbor plan in  
 (2) place that we recommended, first to allow that  
 (3) to happen so we can kind of stop this thing  
 (4) from growing any larger right now, yes. This  
 (5) is not easy, but it's doable. And it's a lot  
 (6) easier than a lot of things I have to deal  
 (7) with every day.  
 (8) COMMISSIONER DUNLEAVY: Go ahead, Mr.  
 (9) Bergs.  
 (10) MR. BERGS: I would just add that  
 (11) some of the proposals that you've heard today  
 (12) are that we ultimately move the support to an  
 (13) individual. In that environment that problem  
 (14) is solved, especially when the lowest cost  
 (15) provider sets the basis for the per customer  
 (16) support. At that point, you aren't concerned  
 (17) about overfunding either of the two carriers  
 (18) that's available.  
 (19) And I'd just add – and this kind of  
 (20) ties into this question as well as one of your  
 (21) earlier ones – that even assuming that the  
 (22) growth in the fund has been of a result of the  
 (23) competitive ETCs in the last year, to distort  
 (24) that number, ultimately – again, a customer  
 (25) is only going to have so many connections.

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- (1) We're not going to end up in an environment  
 (2) where there is an unlimited number connections  
 (3) for every person in those high-cost areas.  
 (4) So, there's an inherit cap with the current  
 (5) mechanism if we base it on per lines. By  
 (6) allowing that, the only way to fund growth is  
 (7) in that environment. Once we have established  
 (8) a competitive environment and are funding the  
 (9) most efficient provider, is it more people  
 (10) move to those rural areas? I think most of us  
 (11) would agree that might be a good thing.  
 (12) COMMISSIONER DUNLEAVY: Does anyone  
 (13) have a specific idea of how we verify that?  
 (14) MS. PARRISH: Well, I mean, I can't  
 (15) lay out the details for you, but I think that  
 (16) one of our ideas is you have to look at  
 (17) affordability and comparability. And  
 (18) comparability, we've started looking at on a  
 (19) state level where you might have a \$40  
 (20) cellular phone bill that includes lots of  
 (21) bells and whistles. And to try and get it  
 (22) down to the comparable price of plain, old  
 (23) dial tone, you, you know, take \$3 off for call  
 (24) waiting and \$5 off for voice mail and so  
 (25) forth. And then you can start doing an apples

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- (1) to apples comparison of at least what the  
 (2) prices of those services are. And I think  
 (3) that you have to assume that there's some  
 (4) relationship between price and cost.  
 (5) COMMISSIONER ABERNATHY: With regard  
 (6) to the growth of the fund being related to the  
 (7) CETCs, of course, it is because they didn't  
 (8) exist before. So, that's no great surprise.  
 (9) It doesn't really concern me, because they  
 (10) didn't exist before and so it would make sense  
 (11) that as we decided to embrace competition for  
 (12) rural America that in fact that would drive up  
 (13) the size of the fund.  
 (14) The real question for me is, are we  
 (15) directing the funds in the right way at the  
 (16) right amounts? And as Ms. Parrish said  
 (17) earlier, I think instead of focusing on  
 (18) carriers with high costs, I think our focus  
 (19) should be on consumers in high-cost areas.  
 (20) And in some respects I think we would want to  
 (21) embrace lower cost technology, not embrace  
 (22) higher cost technology.  
 (23) And so, that leads to me see if  
 (24) anyone wants to comment on one of the  
 (25) proposals that's been out there, which is you

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- (1) basically seek out a bid to serve that area  
 (2) and the one with the lowest cost bid – this  
 (3) is what a number of developing countries are  
 (4) doing – the one that comes in and says, I  
 (5) will serve this for the least amount of the  
 (6) subsidy, that's then what any provider gets  
 (7) who serves that area.  
 (8) I've heard concerns about that, that,  
 (9) well, what about the folks who entered under  
 (10) the old regime and they're there and they've  
 (11) got embedded costs. But I'd like to hear some  
 (12) debate around that proposal.  
 (13) DR. LEHMAN: I'm not sure what people  
 (14) would be choosing between. I mean, what kind  
 (15) of service are they going to get? They like  
 (16) their cell phone. They use it a lot of the  
 (17) time. They can't use it in their rural  
 (18) residence because the service doesn't reach  
 (19) there. So, when you face them with this  
 (20) choice and take the lowest bid, how are you  
 (21) going to educate them as to exactly what it is  
 (22) that they're getting for that choice?  
 (23) COMMISSIONER ABERNATHY: Well, you  
 (24) have to have certain criteria that any vendor  
 (25) would have to meet. And we'd certainly

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- (1) addressed that, I think, at the FCC and in the  
 (2) Joint Board when we said, if you want to be an  
 (3) ETC, you have to have carrier-of-last-resort,  
 (4) you'd have to have certain obligations. So, I  
 (5) think you – you'd have certain criteria that  
 (6) would have to be met.  
 (7) So, let's assume for a minute that  
 (8) the technology – let's say it's not wireless,  
 (9) it's some other technology. Assume that it  
 (10) could do that. Is this overall approach  
 (11) reasonable?  
 (12) DR. LEHMAN: The house I used to live  
 (13) in in a rural area, you could not have gotten  
 (14) a bid from other than the existing wireline  
 (15) provider if you required that they provide  
 (16) service to my home. Now, that's not the way  
 (17) the current rules read. If you're going to  
 (18) write rules that say you must be able to  
 (19) provide this level of quality of service to  
 (20) where the person's residence is and it must  
 (21) work X percent of the –  
 (22) COMMISSIONER ABERNATHY: ILECs today  
 (23) only have to serve based upon reasonable  
 (24) request. Even the incumbents don't have to  
 (25) serve anyone. So, you'd have the same test

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- (1) for the new provider.  
 (2) Gene, do you want to talk about this  
 (3) or Scott?  
 (4) MR. JOHNSON: Well, I'm just thinking  
 (5) about we have to be careful that we don't  
 (6) dismantle this marvelous telephone system we  
 (7) have in this country to do that. So, I'm a  
 (8) potential competitor and I come in say, you  
 (9) know, put out the bid in the area that you  
 (10) live in, your study area, I guess, that I'm  
 (11) going to bid to do this. And so now, maybe I  
 (12) already have a network in place; maybe I  
 (13) don't. But to be sure, the network probably  
 (14) is not as good as the existing network that's  
 (15) there. If that was true, we'd be losing  
 (16) customers right and left to wireless carriers  
 (17) that we're not. And I think that's probably  
 (18) true in general in rural communities. It's  
 (19) not like in urban communities where you're  
 (20) losing customers to wireless carriers. It's a  
 (21) secondary service not replacing the primary  
 (22) service.  
 (23) So, the concern I would have is as  
 (24) they build this out, when do you cut the – I  
 (25) have a lot of concerns, obviously – but when

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- (1) do you cut the funding out to me? I've got  
 (2) embedded costs. I've got this compact I've  
 (3) entered into with regulators that's 100 years  
 (4) or more old, certainly goes back into the  
 (5) '30s. And all of a sudden you're going to  
 (6) pull this compact out and say, we're just  
 (7) going to leave you stranded. Well, what  
 (8) happens to my stranded investment when you do  
 (9) that in these variable areas?  
 (10) And at the end of the day, more  
 (11) importantly, what happens to the rural  
 (12) customers when the company that won the bid  
 (13) doesn't perform? You see construction  
 (14) projects every day that are taken over by a  
 (15) bonding company at great delay and cost many  
 (16) times to the owner because the low cost bidder  
 (17) just was not able to perform.  
 (18) MR. BERGS: Actually, I agree with a  
 (19) portion of what Mr. Johnson said. I think  
 (20) that in a bid proposal what the Commission  
 (21) would in essence be doing is picking a point  
 (22) in time and identifying the most efficient  
 (23) carrier at that point in time. Maybe most  
 (24) efficient isn't even the right  
 (25) characterization. The provider who will

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- (1) generate the most value to the customer at  
 (2) that point in time.  
 (3) And today, I believe in a lot of our  
 (4) areas, we are that carrier. It may be a  
 (5) slightly biased opinion, I admit. But I do  
 (6) expect that at some point in time another  
 (7) technology, either provided by us or another  
 (8) carrier is going to displace CMRS technology as  
 (9) the most efficient. I'm afraid the bid  
 (10) proposal would limit the ability of new  
 (11) technologies to be easily entered into those  
 (12) high-cost areas.  
 (13) However, if competition under the  
 (14) current mechanism is in place and portability  
 (15) is in place, customers will choose the most  
 (16) high-value service available in that market,  
 (17) thereby alleviating the need for the bid  
 (18) proposal. It will target support to the most  
 (19) high-value provider.  
 (20) COMMISSIONER ABERNATHY: Okay. And  
 (21) then one quick follow-up is if – let's assume  
 (22) for a second this approach can't work because  
 (23) of the distortions and you've got the  
 (24) incumbents with other prices and we said, all  
 (25) right, we're not going to try this bid

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- (1) proposal. We're going to continue to have  
 (2) ETCs, but we're going to ask them to somehow  
 (3) justify their support through some kind of  
 (4) proceeding. If we came up with a new way of  
 (5) justifying support, wouldn't it make sense  
 (6) then to apply it to all the carriers who are  
 (7) serving that area if you came up with a better  
 (8) way? That was our first panel. It was really  
 (9) how you figure out the amount of support. It  
 (10) sounds to me like it might be whatever  
 (11) methodology you come up with, you would apply  
 (12) it to both the new guys coming in as well as  
 (13) the incumbents. Does that make sense?  
 (14) MR. JOHNSON: I think that's what we  
 (15) said in our filing is that we think  
 (16) essentially what is good for the goose is good  
 (17) for the gander. We believe the right way to  
 (18) do that right now is based on embedded costs,  
 (19) so we would suggest that the CETCs submit  
 (20) appropriate kinds cost models or cost studies  
 (21) of some kind, perhaps if there are average schedule  
 (22) type costs that could be developed in order to  
 (23) do that. We absolutely agree with that.  
 (24) MR. COLE: I guess one of the things  
 (25) Mr. Bergs talked about, I think you mentioned

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- (1) also in the start of yours as far as not  
 (2) focusing on the company, focus on the people  
 (3) involved. And it may be a given, but just a  
 (4) moment to visit. I think it is important. I  
 (5) understand the purpose of the universal  
 (6) service fund is - what it was meant to do  
 (7) versus what we may be doing now.  
 (8) And I just happened to think while I  
 (9) was sitting in the back a while ago. I went  
 (10) to my parents' this weekend with my  
 (11) seven-year-old, just to take her there. And  
 (12) they live in a very rural area, much of what  
 (13) we're talking about. It's actually a  
 (14) CenturyTel area. I believe it does receive  
 (15) USF support. I went there and it's easier to  
 (16) visit my parents, and they live across the  
 (17) street from my grandparents, and my sister  
 (18) lives next door. And they live in several  
 (19) little houses right at the top of the hill.  
 (20) And they're probably the only houses within a  
 (21) mile of there. And you go past there about 50  
 (22) feet and the road stops and you have dirt.  
 (23) And then there's about one house per mile  
 (24) after that.  
 (25) But I think we talked about what has

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- (1) changed since then. I remember when I was a  
 (2) seven-year-old and went up there and my  
 (3) grandparents were across the street. That was  
 (4) my first introduction to phone service. And I  
 (5) learned real quickly when the phone rang, and  
 (6) their house was no bigger than this area up  
 (7) here, that there was two different rings.  
 (8) When one of them rang, it was your  
 (9) grandparents and you answered the phone and  
 (10) said, hello. And when it was the other ring,  
 (11) it was her mother-in-law, my  
 (12) great-grandparents across the street. And  
 (13) when it rang, you just picked up real quietly  
 (14) and didn't say anything and handed it to your  
 (15) grandmother. That was my introduction to  
 (16) telephone service and party lines and what it  
 (17) is.  
 (18) And then I go there this weekend and,  
 (19) you know, we've long ago done away with party  
 (20) lines. We have single party, all digital  
 (21) service in that area. My father has his  
 (22) Internet hooked up to our telco service and  
 (23) has that. I look at the things that universal  
 (24) service means for that community. They now  
 (25) have one-party service. They really couldn't

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- (1) have had that without that. They now have  
 (2) 9-1-1. The biggest challenge with 9-1-1 was  
 (3) not the technology, but it was coming up the a  
 (4) name for all the roads. So, we did that.  
 (5) And then we had an ice storm there five  
 (6) years ago. We were able to stay in touch,  
 (7) but they were out of electricity for five  
 (8) years (sic). So, those are the kinds of  
 (9) things I want to talk about when you think  
 (10) about universal service.  
 (11) At the same time, my father has a bag  
 (12) phone, a wireless phone that he's had for ten  
 (13) years. It's the same bag phone and I know I  
 (14) should have bought him one by now, but he's  
 (15) stuck on that bag phone. And so, he's had  
 (16) that same service for ten years. He can't  
 (17) really use it at home. He has to use it in  
 (18) the car between the old saw mill after the  
 (19) turn. He goes there and he can pick up  
 (20) service and between Monroe. But he could not  
 (21) use that as a substitute for his home.  
 (22) However - and that's where the  
 (23) struggle is because, again, assuming that  
 (24) there is a wireless ETC there, I'm not sure  
 (25) that it's not going to have the

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- (1) qualifications. I don't understand after a  
 (2) telco made that investment, made those  
 (3) commitments to that community, provided those  
 (4) services, if they're getting \$10 or \$20 of USF  
 (5) a month for that line, why should that bag  
 (6) phone that has been in that car for ten  
 (7) years - as far as I know, any towers had been  
 (8) built in that time - should also receive the  
 (9) same \$10 or \$20 a month?
- (10) COMMISSIONER ABERNATHY: I think I'm  
 (11) going to stop now, because I do want to give  
 (12) my colleagues time to ask questions. Thank  
 (13) you.
- (14) COMMISSIONER NELSON: I do want to  
 (15) welcome a former member of the Michigan  
 (16) Commission staff, Ms. Parrish, who used to  
 (17) work for us and did a great job many years  
 (18) ago.
- (19) I want to focus on rule 305, which is  
 (20) one of the issues that was teed up in this  
 (21) proceeding. And I know, Mr. Cole, you  
 (22) indicated you'd like to see the Commission  
 (23) amend that rule. But would you agree with  
 (24) Dr. Selwyn that the need for that rule goes  
 (25) away if we redefine rural to look at the

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- (1) geography as opposed to the individual  
 (2) characteristics of the carrier? And wouldn't  
 (3) that also mean that perhaps we wouldn't be  
 (4) getting premiums paid in the amounts they're  
 (5) being now for new territories because the  
 (6) acquiring carrier would be getting the same  
 (7) level of support as the carrier that gave up  
 (8) the territory?
- (9) MR. COLE: As far as Dr. Selwyn's  
 (10) proposal, I'm not sure I understand the  
 (11) complexities of it. But I will answer as far  
 (12) as to the premiums. I think at the same time  
 (13) there has been a not a lot of transactions in  
 (14) the last couple, three years. And I think  
 (15) that's a part of it. Again, are those  
 (16) premiums still applicable for those parties  
 (17) based upon current regulatory and cost  
 (18) environment within rural telcos?
- (19) Again, I think the purpose of the  
 (20) safety valve was to take a look at those  
 (21) markets that were acquired and say, are they  
 (22) the same level of service that we would like  
 (23) to see those markets? Have they have received  
 (24) the same attention that the urban areas have  
 (25) received? And if not, is there any incentive

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- (1) or anything we can do where those customers  
 (2) can get those same levels of service?  
 (3) And I think that was the intent. I  
 (4) think it's important to note that. I believe  
 (5) as of this date, there has never been a dollar  
 (6) disbursed under the safety valve program  
 (7) because of this limitation. So, I think all  
 (8) we're saying is that is the intent. And I  
 (9) know in the properties we acquired we made  
 (10) significant investments to upgrade not only  
 (11) the loop and the plant, but also switching  
 (12) facilities. And I believe our customers saw  
 (13) definite improvements. And a lot of our  
 (14) investments were made in that first year  
 (15) because we felt it was so critical. And we  
 (16) made commitments to local mayors, and we made  
 (17) commitments to state regulators that we would  
 (18) improve that service. And we did it  
 (19) regardless of the fact that by spending those  
 (20) dollar in the first year we were, in fact,  
 (21) penalized because that set our base going  
 (22) forward and precluded us from receiving the  
 (23) same level of USF support.
- (24) COMMISSIONER NELSON: Dr. Selwyn?  
 (25) DR. SELWYN: I want to make one brief

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- (1) observation. The reference was made to  
 (2) switching. I find it really very interesting  
 (3) that the rural carriers feel an entitlement to  
 (4) support for switching. In the TRO the  
 (5) Commission concluded that CLECs, many of which  
 (6) are smaller and more geographically disbursed  
 (7) than some of the larger small rural carriers,  
 (8) are not impaired with respect to switching.  
 (9) CLECs are expected to go out and use risk  
 (10) capital and purchase switching equipment and  
 (11) are not going to have access to switching UNES  
 (12) at forward-looking TELRIC prices because of  
 (13) the nonimpairment finding.
- (14) There are relatively few serious  
 (15) scale economies associated with switching that  
 (16) would be that particularly impacted by rural  
 (17) areas. CLECs have been confronting the  
 (18) problem having to connect exchanges located  
 (19) over communities - located over very broad  
 (20) distances to a relatively small number of  
 (21) switches. And the Commission has found that  
 (22) that's an acceptable business model. And I am  
 (23) concerned about the notion that the ILEC, the  
 (24) rural ILECs feel that they have some specific  
 (25) separate entitlement with respect to switching

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- (1) costs that are being denied, in effect, to  
 (2) other providers.  
 (3) MR. COLE: Just to clarify, I don't  
 (4) believe I made any statement that those  
 (5) switching costs should have been included in  
 (6) anything. I was only making that statement  
 (7) about us replacing switches because we had one  
 (8) state, the State of Wisconsin, as part of our  
 (9) acquisition. The Commission made it a  
 (10) requirement that we replace or that we  
 (11) provide - there were a number of them that  
 (12) were there, and we were specifically required  
 (13) to replace those switches as part of the  
 (14) acquisition.  
 (15) DR. SELWYN: But had rule 305 been  
 (16) amended as you were proposing, then the cost  
 (17) base would have been lower, and you would have  
 (18) potentially been able to receive some  
 (19) high-cost support based on that switching  
 (20) investment, if I understand correctly what the  
 (21) proposal is.  
 (22) MR. COLE: I don't know that I'm  
 (23) qualified to address that one.  
 (24) COMMISSIONER NELSON: Dr. Lehman.  
 (25) DR. LEHMAN: Your question about the

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- (1) acquisitions disappearing, if it were done by  
 (2) geography, there's one real concern  
 (3) about that. And that's that we should expect  
 (4) the fund to increase about tenfold. I mean,  
 (5) if you look at the California results where  
 (6) they do have the fund at the state level and  
 (7) the size of that fund, we have the RBOC  
 (8) territories that have a lot of high-cost  
 (9) territories in them that would then become  
 (10) eligible for high-cost funding.  
 (11) And the problem that poses then is we  
 (12) can't tolerate a tenfold increase in the fund.  
 (13) So, what we'll do is we will then have to use  
 (14) a forward-looking model of some sort because  
 (15) that's the only model we can manipulate to get  
 (16) a level of costs low enough to sustain the  
 (17) existing size of the fund but extend it to all  
 (18) geographic areas.  
 (19) There is some appeal to me, the idea  
 (20) that non-rural and rural carriers should be  
 (21) treated the same. If a customer lives in a  
 (22) high-cost area, who cares who their provider  
 (23) is? Except we can't ignore history. There  
 (24) has been a historical compact, if you like,  
 (25) struck where non-rural carriers have agreed to

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- (1) serve high-cost areas. And they have not  
 (2) asked for a re-doing of the funds so that they  
 (3) get the same treatment as rural carriers. So,  
 (4) they're still willing to do that. And I think  
 (5) really the best we can practically achieve is  
 (6) to try to facilitate the transfer of exchanges  
 (7) from those carriers that now consider it sort  
 (8) of a burden to carry this along to carriers  
 (9) that are willing to invest in those exchanges  
 (10) and make the service better. And it doesn't  
 (11) require the fund going up by a factor of ten;  
 (12) it doesn't require some arbitrary reduction in  
 (13) costs that can't be actually achieved by rural  
 (14) carriers.  
 (15) COMMISSIONER NELSON: You would  
 (16) agree, though, that these carriers, you know,  
 (17) to be a burden for them, probably have a lower  
 (18) level of service than other rural carriers?  
 (19) DR. LEHMAN: I think in many cases  
 (20) they do, yes.  
 (21) COMMISSIONER DUNLEAVY: Dr. Selwyn.  
 (22) DR. SELWYN: I'm not sure that  
 (23) characterizing the large RBOCs, for example,  
 (24) in terms of their high cost of exchanges is  
 (25) necessarily being a burden and that was the

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- (1) basis upon which they chose to divest them.  
 (2) They chose to divest those exchanges because  
 (3) they were able to do so and capture a premium  
 (4) value. The exchanges were worth more to the  
 (5) buyer than to the seller, which is typically  
 (6) why an economic exchange takes place. And  
 (7) until the funding mechanism was modified to  
 (8) provide those incentives - until the  
 (9) regulatory structure was modified to allow  
 (10) carriers to earn revenues that - and carry  
 (11) them below the lines so they don't get  
 (12) included in any reckoning of revenue  
 (13) requirement, those perverse incentives didn't  
 (14) exist.  
 (15) We didn't see the Bell companies  
 (16) selling off high-cost exchanges until very  
 (17) recently. We didn't see it for the first,  
 (18) almost, 100 years. They were net acquirers,  
 (19) not divestors. And I'm not sure they ever  
 (20) considered the burden. It's just that the  
 (21) structure was changing and it became  
 (22) profitable to sell them.  
 (23) MS. PARRISH: To speak to Wyoming's  
 (24) experience about sold exchanges is that Quest -  
 (25) U.S. West sold 20-something exchanges ten

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- (1) years ago. They were not very high quality.  
 (2) They've become very high quality. But I think  
 (3) that there can be abuse in the system as well.  
 (4) So, that's the torn judgment that, has it  
 (5) hurt. Because we have at least one company  
 (6) that has essentially gold-plated that system  
 (7) since acquiring it. But the other 20  
 (8) exchanges have just become nice, wonderful  
 (9) rural exchanges. So that's the problem is to  
 (10) avoid the gold-plating or the abuse.  
 (11) COMMISSIONER NELSON: I have one more  
 (12) question for Dr. Lehman, and I promised I'd  
 (13) come back to this in the previous panel. This  
 (14) idea of indexing and if we agree that perhaps  
 (15) we have different levels of calculations of  
 (16) support for a rural carrier and a wireless  
 (17) ETC, could we not index both of those and  
 (18) perhaps move towards more harmonization of the  
 (19) two methodologies over time?  
 (20) DR. LEHMAN: Yeah. The idea of  
 (21) indexing would have the same appealing  
 (22) characteristics for both sets of ETCs. The  
 (23) thing I would want to avoid is the equal level  
 (24) of support, because who knows if it's equal.  
 (25) In fact, I am willing to think that some

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- (1) wireless carriers might deserve more support  
 (2) than the current rural ILEC is getting, if  
 (3) they could justify what the investments are  
 (4) going to actually do and if some appropriate  
 (5) regulatory Commission looks at it and says,  
 (6) this is really something that's needed that's  
 (7) going to be provided. So, I don't think the  
 (8) levels of support should be the same, but  
 (9) capping them does provide incentives for cost  
 (10) reduction for both kinds of carriers.  
 (11) COMMISSIONER NELSON: Thank you,  
 (12) Madam Chair.  
 (13) CONSUMER ADVOCATE GREGG: Dr. Lehman,  
 (14) following up on that. If you believe that it  
 (15) is not proper to equalize support and that  
 (16) wireless and wireline technologies are  
 (17) different, do you think that the current  
 (18) support system for non-rurals, which provides  
 (19) equal per-line support to all ETCs is wrong?  
 (20) DR. LEHMAN: Yeah. I think it's just  
 (21) as wrong as it is for the rural carriers, but  
 (22) it probably matters less since it's so much  
 (23) less support being collected by non-rural  
 (24) carriers. It's very concentrated where it is,  
 (25) and that's where you see competitive ETCs

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- (1) apply for that status.  
 (2) And the concern that I would have is  
 (3) what demonstration do we have that the higher  
 (4) support – that high-costs are what those  
 (5) wireless carriers are actually experiencing  
 (6) there, and that they're using the money to  
 (7) actually upgrade service there. So, that's  
 (8) all I would ask for is that they demonstrate  
 (9) their need for the support and their use for  
 (10) the support, whether it's a rural or non-rural  
 (11) territory.  
 (12) CONSUMER ADVOCATE GREGG: Mr. Bergs,  
 (13) you stated that there was a natural cap on the  
 (14) amount of support that would be paid to  
 (15) support multiple lines in high-cost areas.  
 (16) Given that the projections for incumbent rural  
 (17) LECs for the first quarter 2005 on an  
 (18) annualized basis is for support of two and a  
 (19) half billion dollars, what level of cap would  
 (20) you think that we would ultimately reach if we  
 (21) allowed the fund to just continue to rise to  
 (22) its natural level?  
 (23) MR. BERGS: Well, first of all, I  
 (24) want to clarify. The amount of support  
 (25) provided to a competitive ETC is what I think

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- (1) has a natural cap attached to it because,  
 (2) again, as each competitor enters a market, a  
 (3) consumer is only going to purchase one or  
 (4) maybe two lines. And, in fact, I believe that  
 (5) in the long run while it's been demonstrated,  
 (6) I think there's some agreement amongst the  
 (7) panel that wireless isn't currently accepted  
 (8) as a substitute for wireline. That number has  
 (9) increased over the last couple of years from  
 (10) an estimated 3 percent up to, now, an  
 (11) estimated 6 or 7 percent.  
 (12) And over time – well, first of all,  
 (13) the reason for that, I think, is wireless  
 (14) hasn't received funding in the past, and as a  
 (15) result hasn't been able to build the  
 (16) infrastructure required to avoid the  
 (17) antiquated equivalents of a party line only in  
 (18) wireless terms. So, I think in the long run  
 (19) you're going to have some more substitution  
 (20) and, in fact, you're going to see a downward  
 (21) turn in the overall amount of support.  
 (22) I can't give you a number for where  
 (23) this is going to top out, but one way to  
 (24) control that is to maintain a cap or at  
 (25) least – until we can come to a true

- (1) portability of support from wireline to
- (2) wireless, we maintain a cap on the wireline
- (3) cost portion of the funds and allow CETCs to
- (4) enter. As competition comes in, again, we can
- (5) pick our number and we can create our
- (6) multiplier, X dollars of per line support
- (7) times two connections for every person living
- (8) in that high-cost area.
- (9) And, again, one of the keys to
- (10) reducing the impact of the current mechanism's
- (11) ability to grow in the short term is to
- (12) disaggregate that support. If we put it only
- (13) in the high-cost areas, the only way that
- (14) growth increases astronomically is if more
- (15) people move into that highest cost area of a
- (16) study area, breaking it into the zones has
- (17) that inherent cap effect.
- (18) MR. COLE: I would comment on the
- (19) concept of a natural cap if you have multiple
- (20) wireless carriers within that. I guess I
- (21) would disagree and maybe reference to some of
- (22) the testimony that was in the pre-filed
- (23) document that I had, where there had been
- (24) situations of where there are more wireless
- (25) subscribers on a billing list than there are

- (1) population in the area. I mean, that's one
- (2) wireless carrier. If you add multiple, that
- (3) can happen.
- (4) I know this is similar to the article
- (5) we talked about earlier. You're always going
- (6) to have anomalies. You're going to have
- (7) things that aren't done appropriately and
- (8) don't make that rule instead of the exception.
- (9) But I would point you to those references to
- (10) say that under the current system that
- (11) incentive exists.
- (12) In the past ten years - or until
- (13) about five years ago, I was in the wireless
- (14) area of our business and was the president of
- (15) our wireless operation for a couple of years.
- (16) And I can tell you it was a constant
- (17) challenge. When you have compensation
- (18) programs, at that point for distribution,
- (19) whether it be agents or others, that promote
- (20) uneconomic things to happen, they're going to
- (21) happen. The things you incent are going to
- (22) happen. And if you incent funds based on
- (23) customers on a billing list, that billing list
- (24) is going to be higher probably than it should
- (25) be, whether that's going to a bank in a

- (1) metropolitan area that has 50 branches and 1
- (2) branch in the rural area. And the salesman
- (3) says, hey, if you'll let me send all the bills
- (4) to that branch, I'll give you a 10 percent
- (5) discount. I'm not saying those things are
- (6) happening but the incentive is there, and that
- (7) is some of the risk you run with the current
- (8) system that we have in place.
- (9) COMMISSIONER JABER: I thought it
- (10) would be appropriate to end the questioning by
- (11) delving into the logistical aspects of
- (12) whatever gets implemented, and Mr. Johnson
- (13) touched on that a little bit with regard to
- (14) workshops. But the general question for any
- (15) of you is that in determining what the
- (16) appropriate methodology will be going forward
- (17) and calculating support, what is the best
- (18) procedural mechanism the FCC should use to
- (19) adequately determine the best approach? And
- (20) I'd ask, and you have already, to think
- (21) outside the box of the traditional paper
- (22) hearing that the FCC and the Joint Board uses.
- (23) That's the first general question - and not
- (24) that there's anything wrong with that.
- (25) The second question relates to the

- (1) logistics associated with administrative
- (2) expenses and what ongoing role USAC would
- (3) have, and is there a mechanism that mitigates
- (4) the concern as it relates to cost studies that
- (5) get presented and USAC implementation going
- (6) forward. Those are the two questions.
- (7) MS. PARRISH: Commissioner, as to
- (8) your first question, in addition to any
- (9) process that is used to come up with -
- (10) whether it's a form for the wireless
- (11) submitting their embedded costs or a model for
- (12) forward-looking costs, I think there should be
- (13) some procedure prior to implementation but
- (14) after development for parties to comment.
- (15) It's that I think that when the non-rural model
- (16) was developed there were a number of parties
- (17) that late in the game said, wait, some of the
- (18) inputs are wrong. But it was too late,
- (19) really, to change it before it needed to be
- (20) implemented. So, I think there needs to be to
- (21) general-to-the-world opportunity to look at
- (22) what has been developed and say, you know,
- (23) here are the key inputs; you know, do these
- (24) look right for your company or for your state.
- (25) And so, I would offer that suggestion.

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- (1) COMMISSIONER JABER: Anything  
 (2) relating to the USAC concern?  
 (3) MS. PARRISH: My suggestion for USAC  
 (4) may be a little off point of this hearing, but  
 (5) one of the concerns I have has to do with the  
 (6) certification of the funds. I think that some  
 (7) of the – I think I can speak for my own  
 (8) state, is that on the wireless certification  
 (9) it was simply a self-certification done by the  
 (10) carrier to the Commission, forwarded to the  
 (11) FCC. And there were some strong concerns  
 (12) about that self-certification. And I don't  
 (13) believe USAC is doing any auditing of those  
 (14) certifications at this point, and I understand  
 (15) resources issues and so forth. But, you know,  
 (16) in my ideal world, I think that the auditing  
 (17) or spot-checking of certifications would be a  
 (18) very useful thing.  
 (19) MR. JOHNSON: I was to going comment  
 (20) on that second question as well. We've been  
 (21) told that USAC has been directed to conduct a  
 (22) number of audits of receivers of high-cost  
 (23) funds over the 2005 calendar year. And I  
 (24) understand they're gearing up to do that. And  
 (25) it struck me that if CETCs should – you know,

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- (1) we develop a mechanism for CETCs to report  
 (2) their own costs and receive funds based on  
 (3) that, they ought to have a similar audit  
 (4) process. There's not going to be much  
 (5) difference in the process itself, you're  
 (6) obviously auditing different numbers. But  
 (7) you're not auditing a different process.  
 (8) COMMISSIONER JABER: Dr. Selwyn.  
 (9) DR. SELWYN: As to your first  
 (10) question, it seems to me that any carrier,  
 (11) whether it's an ILEC or a CETC, that is going  
 (12) to be relying on its own costs as a basis for  
 (13) support, should be required to provide  
 (14) information with respect to that if we're  
 (15) going to adopt any sort of embedded cost  
 (16) standard. And it's been suggested that CETCs  
 (17) should also provide embedded costs. I don't  
 (18) think that – for reasons I've talked about  
 (19) that having a different level of funding for  
 (20) CETCs versus ILECs is appropriate.  
 (21) In any event, if the ILEC funding  
 (22) mechanism is to be maintained, the support  
 (23) needs to be examined with respect to all  
 (24) revenue sources associated with that  
 (25) infrastructure, not just sources of revenue

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- (1) that are considered to be associated with  
 (2) local service. If the ILEC is capable of  
 (3) operating profitably with all it's revenue  
 (4) sources, it shouldn't be entitled to – and  
 (5) support in whatever it does draw should be  
 (6) based upon the deficiency relative to all  
 (7) revenue sources.  
 (8) I believe that going forward we  
 (9) should be looking at forward-looking costs  
 (10) that are not based on specific carrier costs,  
 (11) but are based upon model costs which reflect  
 (12) what would be expected from an efficient  
 (13) provider. And that should be the basis for  
 (14) funding all carriers. And that, in effect,  
 (15) gets us out of the rate case and auditing  
 (16) requirements. If a carrier wants and believes  
 (17) that it – it confronts such extraordinary  
 (18) conditions that the model costs simply do not  
 (19) capture those conditions and it wants to make  
 (20) a case, then it should, in effect, make a  
 (21) revenue requirement case.  
 (22) MR. JOHNSON: Can I make the comment,  
 (23) please, related to that? I heard in the  
 (24) earlier panel something that I thought was  
 (25) just blatantly wrong. And that is that rural

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- (1) LECs are not – no one is looking at their  
 (2) costs and therefore no one is – they're just  
 (3) free to run wild.  
 (4) I said the last time I appeared  
 (5) before you that we have lots of reasons to be  
 (6) efficient, not the least of which is we have  
 (7) competition in many of our operating areas.  
 (8) But at least one commissioner before me right  
 (9) now is a commissioner in a state in which we  
 (10) do business in which they do rate reviews  
 (11) quite often and look very hard at our cost  
 (12) studies and our separations and what we're  
 (13) actually doing and asks very, very difficult  
 (14) questions. So, this idea that somehow we're  
 (15) not being regulated as to rates and just  
 (16) allowed to run wild and rampant is just  
 (17) absolutely and patently false and absurd.  
 (18) MR. BERGS: I'd just comment on the  
 (19) second question that you asked. If we move to  
 (20) a system where CETCs' support is based upon  
 (21) their own costs, not only are we taking  
 (22) away – are we in fact motivating that CETC  
 (23) the same way we have historically motivated the  
 (24) ILEC to increase its cost in order to get more  
 (25) support, hopefully the net result being more

(1) infrastructure is developed, but even in an  
 (2) inefficient manner.  
 (3) But beyond that, logistically, you  
 (4) are forcing an absolute duplication of an  
 (5) effort that we admittedly - or I believe USAC  
 (6) admitted has not been historically been able  
 (7) to maintain. One of the comments I noted in  
 (8) the USA article that was referenced earlier is  
 (9) that USAC staff is simply unable from a  
 (10) manpower standpoint to do the kinds of audits  
 (11) that they would need to do. Now, what we  
 (12) would be asking them to do is double first,  
 (13) upfront the cost studies that they have to  
 (14) initially identify to create the basis for  
 (15) support and double an unattained level of  
 (16) audit to ensure that those funds are actually  
 (17) being spent appropriately.  
 (18) MR. COLE: One thing I might - just  
 (19) to your question, because I do - it's a tough  
 (20) question to answer because I think it does  
 (21) entail a lot. I would say, though, that from  
 (22) my prior experience - I did serve, I think,  
 (23) at one time on the finance committee at the  
 (24) CTIA when I was in the wireless business. And  
 (25) I know we endeavored at that time to try to

(1) appreciate all your time here, for your  
 (2) written submissions, and for your willingness  
 (3) to come there. So, with that, we are  
 (4) adjourned.  
 (5) (WHEREUPON, the second panel  
 (6) concluded at 4:55 pm.)  
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(1) come up with some standard accounting, some  
 (2) standard ways of recognizing the commissions  
 (3) and other things. Well, being involved in our  
 (4) partnerships and also in others, I think there  
 (5) is some pretty standard accounting methodology  
 (6) that would not make that an impossible task.  
 (7) Also in a number of the rural service  
 (8) areas because of the way the incentives began  
 (9) are represented by separate rural service  
 (10) areas. Independent telcos and others have a  
 (11) separate set of accounting records, even for  
 (12) their specific area, not necessarily that  
 (13) service area, but at least more defined  
 (14) geographically. So, I do think it's possible,  
 (15) and I do think there is some consistency. And  
 (16) I think the analysis of costs would be  
 (17) possible. How to take that and equate that to  
 (18) USF support would be very challenging. Thank  
 (19) you.  
 (20) COMMISSIONER ABERNATHY: Thank you  
 (21) very much to the commissioners on the joint  
 (22) board and also to the panelists. This was  
 (23) very, very informative for us. No doubt we  
 (24) will have many interesting debates as we go  
 (25) forward dealing with all of this. But I do

(1) REPORTER'S CERTIFICATE  
 (2)  
 (3) STATE OF TENNESSEE  
 (4) COUNTY OF DAVIDSON  
 (5)  
 (6) I, MELISSA M. SCHEUERMANN,  
 (7) Court Reporter, with offices in Nashville,  
 (8) Tennessee, hereby certify that I reported the  
 (9) foregoing public meeting on HIGH-COST  
 (10) UNIVERSAL SERVICE SUPPORT FOR AREAS SERVED BY  
 (11) RURAL CARRIERS AND RELATED ISSUES by machine  
 (12) shorthand to the best of my skills and  
 (13) abilities, and thereafter the same was reduced  
 (14) to typewritten form by me.  
 (15) I further certify that I am  
 (16) not related to any of the parties named  
 (17) herein, nor their counsel, and have no  
 (18) interest, financial or otherwise, in the  
 (19) outcome of the proceedings.  
 (20)  
 (21)  
 (22) MELISSA M. SCHEUERMANN  
 (23) Associate Reporter  
 (24) Notary Public  
 (25) State of Tennessee At Large.



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